



# Financial Inclusion: A Foothold on the Ladder toward Prosperity?

An Evaluation of World Bank Group Support for Financial Inclusion  
for Low-Income Households and Microenterprises



**IEG**  
INDEPENDENT  
EVALUATION GROUP

**WORLD BANK GROUP**  
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WORKS**

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**An Evaluation of World Bank Group Support for Financial Inclusion for Low-Income Households and Microenterprises**

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<http://ieg.worldbankgroup.org/evaluations/financial-inclusion>.

# Abbreviations

AAA	analytic and advisory activities
AFI	Alliance for Financial Inclusion
AMP	Africa Microfinance Program
CGAP	Consultative Group to Assist the Poor
FSAP	Financial Sector Assessment Program
FY	fiscal year
GDP	gross domestic product
GNI	gross national income
GPFI	Global Partnership for Financial Inclusion
ICR	Implementation Completion and Results Report
IEG	Independent Evaluation Group
IFC	International Finance Corporation
KYC	know your customer
M&E	monitoring and evaluation
MFI	microfinance institution
MFS	mobile financial services
MIGA	Multilateral Investment Guarantee Agency
MIMOSA	Microfinance Index for Market Outreach and Saturation
MIX	Microfinance Information Exchange
MNO	mobile network operator
MSME	micro, very small, and medium-size enterprises
NBMFI	nonbank microfinancial institution
SACCO	savings and credit cooperative
SME	small and medium-size enterprise
UFA	Universal Financial Access

*All dollar amounts are U.S. dollars unless otherwise indicated.*



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Team members (in alphabetical order) were Feruza Akbarovna Abduazimova, Jacqueline Andrieu, Nadia Asgaraly, Amit Banerjee, Mariano Cortes, Jack Glen, Wasiq Ismail, Takatoshi Kamezawa, Anjali Kumar, Jimena Luna, Victor Malca, Daniel Palazov, Maria Elena Pinglo, Elizabeth Wallace, and Disha Zaidi. The report built on a comprehensive literature review, conducted for this study by Thorsten Beck, professor of banking and finance at Cass Business School in London. The report also benefited from contributions from Leonardo Bravo and Beata Lenard on International Finance Corporation Advisory Services and investments. Heather Dittbrenner edited the report and Emelda Cudilla provided administrative support and formatted the report.

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# Overview

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Access to financial services has long been believed to lift people out of poverty by allowing them to seize economic opportunities and improve their welfare. Despite the rapid progress of 700 million people gaining access to formal financial services, 2 billion remain excluded. Financial inclusion—access by poor families and microenterprises to financial services—has been an objective of the World Bank Group for a long time, reaffirmed in 2013 by President Jim Kim’s commitment to the Universal Financial Access goal by 2020.

This evaluation examines the relevance and effectiveness of seven years (fiscal years 2007–13) of World Bank Group support to financial inclusion and its impact on the poor. It found that the World Bank Group contributed significantly to progress in financial inclusion globally and in client countries. It has “reached” a substantial share of the microfinance industry. Its support is strategically aligned with countries’ needs, focusing primarily on countries with low inclusion rates and addressing development priorities. The Bank Group has also contributed to the sustainability of microfinance services.

Yet the World Bank Group’s approach to identify and tackle constraints to financial inclusion at the country level is not sufficiently comprehensive. This is of particular concern for areas that are not subject to prudential regulations, such as mobile money and rural savings and credit cooperatives. Even though the World Bank Group was able to leverage its impact through international partnerships, these bear costs and risks and often lack results frameworks.

But most importantly, the commitment to the Universal Financial Access goal and the resulting “push” for enabling access to financial services through transaction accounts may create a bias for driving up sheer access numbers. This may be problematic for several reasons: (i) Access does not necessarily lead to *inclusion*, given high dormancy rates of newly created accounts; (ii) the link between access to finance and poverty alleviation is neither certain nor well understood, given the evidence that, in spite of modest benefits, the promise of microfinance pulling millions out of poverty has not been fulfilled; and (iii) current trends suggest that 1 billion people may still lack access by 2020. These remaining financially excluded will increasingly be broadly distributed across many countries and predominantly in rural areas. Providing access to them is likely to require subsidization. Striking a balance between the costs and benefits of universal inclusion and weighing these against the cost and benefits of other competing development priorities will be essential. The Independent Evaluation Group thus recommends the following:

- ❖ **Clarify the World Bank Group’s approach** on financial inclusion by making it evidence-based and comprehensive, focused on enabling access to a range of financial services with benefits for the poor in a sustainable manner, and specifying when and how to use subsidies.
  - ❖ **Find and replicate innovative delivery models** through a sequenced and evidence-based approach to innovation.
  - ❖ **Strengthen partnerships** by advocating clear strategies, results frameworks, and monitoring and evaluation arrangements.
  - ❖ **Implement new tools in country-level diagnostics** and strategies to guide financial inclusion work.
-

## Financial Inclusion and the Fight against Poverty

The poor face immense financial challenges. They are more likely to send family members to faraway cities or even abroad in the hope that they will send money home. The income of the poor is not only lower but also more volatile, as they rely on a range of often unpredictable jobs or on weather-dependent agriculture. Transforming irregular income flows into a dependable resource to meet daily needs represents a crucial challenge for the poor, and so do the funding needs if their homes require repair, a relative dies, or a breadwinner falls ill. Savings, credit, insurance, and remittances can each help smooth the volatile incomes of poor people, providing a margin of safety when income drops or expenses rise, or provide the needed funds for children's education or health care. At the same time, probably the best-known argument for microfinance has been the expectation that credit could lift people out of poverty by providing microentrepreneurs with funds they need to seize growth opportunities. All these arguments have hitherto formed the bases of the "case for financial inclusion."

Yet the poor are largely excluded from financial services, despite recent progress. Although the number of unbanked dropped from 2.5 billion in

2011 to 2.0 billion in 2014, an estimated 46 percent of adults in developing countries are unbanked, compared with only 6 percent in developed countries. The poor are hit the hardest: of those living on \$2 per day, 77 percent lack a bank account. Recognizing the possibilities for the poor, a microfinance industry grew over the last 20 years, culminating in a dramatic growth spurt in the last 3–5 years. In some countries, growth has reached a saturation level so that, according to some estimates, about 6 percent of countries are at risk of overindebtedness and about 13 percent warrant a detailed analysis of market stability factors—including evaluation of levels of overindebtedness. Yet, in spite of rapid progress and a record number of people reached by a variety of formal financial services, there remains a substantial credit gap and high levels of exclusion.

The Andhra Pradesh crisis is one example of when overindebtedness led to ripple effects through the microfinancial community. In late 2010, Andhra Pradesh state authorities reacted to claimed abuses and breakneck growth of the microfinance industry, including overlending, inadequate consumer protection, and abusive collection practices. State politicians, who favored a state-led alternative that offered subsidized financing to the poor, responded with legislation that was so restrictive that

no microfinance institution (MFI) could operate. The crisis deeply shocked the microfinance industry and India's central bank – stimulating both to take remedial action. The result was a better-regulated (and self-regulated) commercial microfinance sector with a code of conduct, monitoring, and a high-quality national credit information system. Commercial microfinance resumed substantial growth everywhere except the state where the crisis began.

With the growth of the microfinance industry, the evidence base on how financial inclusion affects the poor also grew. To reflect the current status of the academic knowledge, IEG commissioned an independent literature review covering more than 140 articles and publications, with a focus on the most recent research. The evidence indicates that the expectations of microcredit pulling millions out of poverty have not been fulfilled. The overall picture is one of mixed but modestly positive (not transformative) effects of microcredit on the poor. Credit – and along with it other financial services such as payments, savings, and insurance – can, however, help the poor manage their day-to-day struggle. These financial services provide choices and options that did not exist before, in particular with regard to education, health, and buffering income shocks. In fact, benefits from noncredit services appear to have a higher

potential than microcredit alone, which may make them more suitable entry points for the poor into formal financial services.

IEG's review also covered all International Initiative for Impact Evaluation-listed impact evaluations and systematic reviews on financial inclusion. It indicated that microcredit is – overall – fairly well studied and savings more modestly studied, whereas payments, insurance, financial literacy, and consumer protection represent major gaps in rigorous understanding. However, even with regard to credit, the long-term impact has rarely been studied, with most studies focused on the short term. Nor do rigorous studies shed much light on macroeconomic or fiscal impact of interventions, the role (or potential role) of government, intergenerational effects, or enablers of microenterprise (and household) success.

The World Bank Group has spent 2–3 percent of its annual commitments on financial inclusion-related projects, based on the rationale that its support for financial inclusion would improve markets by overcoming limitations to demand and supply so more and better financial services could be provided to the poor.

IEG reviewed the experience of the World Bank Group's support to financial inclusion over fiscal years (FY)07–13. The large majority (70

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percent) of the evaluated interventions are relatively young, that is, approved FY06–13. Relying mainly on this set of rather recent interventions, IEG also factors in ongoing trends and developments to ensure relevance and timeliness of its conclusions and recommendations.

One of the key purposes is to inform the World Bank Group Management on its experience in supporting financial inclusion at a time when the World Bank Group is designing the road map for its future work helping client countries achieve the Universal Financial Access Goal by 2020. The access goal had become of the highest strategic relevance to the World Bank Group as President Jim Yong Kim committed the organization to this goal in 2013 and is closely monitoring progress.

IEG has also tried to determine the extent to which the current campaign for the 2020 Universal Financial Access Goal is grounded on evidence of actual benefits to the poor – which is important, as the latest research points to more modest benefits for the poor from financial services than originally hoped for. The report also assesses if the World Bank Group has been responsive to emerging evidence in designing its operational financial inclusion agenda.

The evaluation is equally meant to inform the strategic discussion in and outside of the World Bank Group

about the role of financial inclusion in the post-2015 development agenda and the ways the World Bank Group can support it.

### **The World Bank Group's Operational Response to the Challenge of Financial Inclusion**

Operationally, the World Bank Group has deployed a wide range of services and products, through the World Bank, the International Finance Corporation (IFC), and the Multilateral Investment Guarantee Agency (MIGA): 884 inclusive finance projects committed between FY07 and FY13 (an average of 125 projects per year), with a total commitment value of \$9 billion (an average of \$1.3 billion per year).

Throughout the evaluation period, financial inclusion projects accounted for approximately 3 percent of total World Bank Group commitments. IFC accounted for the highest share of financial inclusion projects, both by number of projects (65 percent) and commitment value (49 percent). The World Bank's lending accounts for 32 percent of total Bank Group projects and 45 percent of commitments, because of its larger average project size. MIGA's relative share is only 3 percent of projects and 6 percent of value (measured by gross exposure).

Over the last six years, World Bank Group support to financial inclusion

grew by about 20 percent. During FY09 and FY10, the World Bank Group's commitments to financial inclusion exhibited a marked increase, likely in response to the global economic crisis.

With a growing realization that poor households and small firms need broader financial services than just credit, the World Bank Group's inclusive finance support gradually embraced other services, such as payments and savings, which are known to have higher potential to improve the lives of the poor. Along with this development came an increased emphasis on upstream work in client countries to create a stronger enabling environment for financial inclusion.

### Strategic Relevance

The growth in its commitments toward financial inclusion indicates the World Bank Group's intent to respond to the global challenge of financial inclusion. To illustrate the World Bank Group's reach, IFC supported — either through investments or advisory services — MFIs that jointly make up 39 percent of the global microlending volume. Supporting an MFI through an investment or advice may not necessarily indicate that IFC was responsible for the entire loan volume that this MFI subsequently issues, as IFC typically invests along with

several others. A “reach” of 39 percent still exemplifies IFC's leadership role.

Despite the World Bank Group's growth and relative reach, its support to financial inclusion is small, given the large number of unbanked (2 billion globally) and the size of the microenterprise credit gap, according to IFC's calculation (more than \$1 trillion). This calls for a strategic allocation of the World Bank Group's resources, devoting its scarce resources where they are needed the most and where they can have the highest impact, either in terms of creating new markets or scaling up existing markets.

IEG found that, globally, the World Bank Group's allocation of its resources devoted to advancing financial inclusion are strategically well aligned with countries' needs; that is, they primarily reach countries with low inclusion rates and where the countries' microcredit markets actually reach the poor, and they are relevant, as they address country development priorities in the given institutional and policy context.

In particular, World Bank lending, IFC advisory work, and World Bank analytical and advisory activities (AAA) are strongly geared toward the countries with lowest inclusion. IFC's investments are also well synchronized with countries' needs. Given the self-sustaining potential of IFC investments, IFC's presence in the

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lowest and low-inclusion countries is remarkable, as these are typically served by MFIs that rely on donations or subsidies.

The Bank Group's resource allocation was not only in sync with country exclusion levels, but it also reflected patterns of overindebtedness. Overindebtedness of microfinance clients is one of the many risks facing the industry these days. IEG found that, broadly speaking, the World Bank Group's strategic resource allocation to client countries reflects market saturation levels. In other words, markets at risk of overindebtedness were provided with advisory and AAA work rather than with funding.

World Bank Group funding of microfinance operations in countries that are saturated or even at risk of overindebtedness was significantly lower than volumes provided by the general market. This is a good thing, as it indicates that the World Bank Group refrains from further "fueling" market saturation and instead focuses on building capacity in these markets to deal with the risks of the microfinance markets, including issues of overindebtedness. Such an approach is likely to limit the "collateral damage" of overindebtedness as a result of microcredit. Given the evidence that microcredit has not fulfilled expectations of lifting people out of poverty, it seems vital to limit the

potential of poor people becoming overindebted.

At the country level, World Bank Group support for financial inclusion was relevant in the sense that it addressed a clear development priority. Yet well-functioning markets require well-informed consumers with accurate information about services and their costs. Within the evaluation period FY07–13 the World Bank Group rarely pursued consumer protection and financial literacy in its country engagements, even though the World Bank Group supports the Global Survey on Consumer Protection and Financial Literacy in compiling data from over 100 central banks and bank supervisors.

Increased efforts in this space that the World Bank Group undertook in FY15 point at an encouraging new emphasis. The danger of overindebtedness exemplifies why consumer protection and financial literacy matter. Bank Group interventions most frequently address the constraints of lack of capacity and financing of financial intermediary institutions, as well as weakness in financial infrastructure (for example, credit reporting) and regulation.

Across the portfolio, most projects identified target beneficiaries, such as microenterprises, but most lacked a definition of what the World Bank Group considers a microenterprise. This is important, as projects may end

up supporting larger companies and loans with financing intended for microfinance.

Of those projects that mention women beneficiaries, a minority provides an in-depth description of this target population. More broadly, financial inclusion projects often fail to spell out the constraints specific to their intended beneficiaries.

### **World Bank Group Support through Partnerships**

An important part of the World Bank Group's approach to financial inclusion lies in its contribution to global knowledge, standards, and policy norms in ways that benefit the poor. The World Bank Group supports policy reform through both international partnerships and its country-level engagement to create adequate regulatory frameworks.

The Bank Group has been able to leverage its impact at the country and global level through global partnerships. Partnerships clearly extend reach, resources, and influence to promote access to financial services by the poor and microenterprises. Organizations such as the Consultative Group to Assist the Poor (CGAP), the Global Partnership for Financial Inclusion, the Center for Financial Inclusion, and the Alliance for Financial Inclusion have a strong standing with relevant stakeholders

and can provide opportunities for knowledge sharing, policy influence, and piloting and disseminating innovative approaches. Partnerships play a large role in the World Bank Group's goal of universal financial access and longer-term inclusion goals as well.

The World Bank Group has also been able to have a strong impact on global standard-setting bodies through its partnerships with CGAP and the Global Partnership for Financial Inclusion (through the Regulations and Standard-Setting Bodies subgroup) and by engaging with major global standard-setting bodies. Similarly, the World Bank's leadership is exercised in the policy-setting arena on global remittances. Its efforts through the Global Working Group on Remittances have been credited with reducing the cost of remittances, resulting in tens of billions of dollars of savings to migrant workers and their families.

At the same time, these partnerships bear risks: they require resources and senior staff, can inhibit or dilute the World Bank Group's own "branding," and may at times pursue goals or methods not squarely aligned with the World Bank Group's own strategy. Partnerships involve compromise and coordination. Going forward, it will be important for the World Bank Group to encourage its partner organizations to adopt high standards, especially with regard to accountability and



learning systems. In this context, Bank Group staff report advocating for such systems is likely to gain more traction in partnerships where the World Bank Group is a major stakeholder, hosts the secretariat, or contributes with financial resources.

### **World Bank Group Support for Policy Reform through Country-Level Support**

For financial intermediaries to thrive and better serve the needs of the poor, an enabling environment has to be in place at the country level. This includes an adequate framework of proportional regulation and effective supervision, comprehensive and reliable credit information, procedures for account openings, sound consumer protection practices, and adequate policies for branchless or mobile banking.

To assist countries in policy reforms and in creating an enabling environment, the World Bank Group implemented 232 interventions during FY07–13, about one-fourth of the total financial inclusion interventions. Such interventions are provided by both the World Bank and IFC, with two-thirds of the total number of interventions delivered by the former.

The World Bank upstream interventions (that is, policy, regulatory, and institution-building) were delivered through lending

instruments and AAA. IFC upstream interventions were delivered through its advisory services. These advisory services interventions are usually delivered in the context of related investment interventions as a way to establish or strengthen a regulatory framework.

On balance, World Bank Group upstream interventions were broadly effective. In most areas of upstream involvement, the objectives were fully achieved in more than half of the cases. For both the World Bank and IFC, interventions focused on oversight, regulations, and financial infrastructure obtained the best ratings. Financial literacy interventions for the World Bank and financial inclusion strategy interventions for IFC Advisory Services are the two areas of involvement in which effectiveness has most substantially faltered.

AAA work delivers an important contribution to reforms. This support focuses mainly on upstream issues (80 percent) and almost doubled from FY10 to FY13, compared to FY07–09. The share of AAA work that focused on noncredit issues – that is, savings, payments, and insurance – increased as well, amounting to 41 percent recently. This is an important response to the emerging evidence that noncredit financial services are equally – if not more – beneficial for the poor.

The single most important field of AAA is informing government policy (25 percent), including providing strategic advice, followed by stimulating public debate and raising awareness (18 percent). The World Bank's self-rating scheme suggests far greater success in laying the groundwork for a new World Bank loan than in shifting other donors' policies.

In some countries, the lack of traction in policy dialogue at the strategic level may have contributed to the absence of a coherent national strategy for financial inclusion. The case studies indicate a wide range of variability in the level of government commitment and strategic coherence.

Despite the World Bank Group's significant role in policy reform and its success, its approach to identifying legal and oversight gaps was not part of a holistic assessment of the adequacy of the various elements of the financial inclusion framework. In a growing number of countries, payment systems, remittances, and financial infrastructure were covered by structured surveys or tool-based diagnostics; in other areas, stronger analytical support is under way or planned, such as in the area of consumer protection and financial literacy. At the same time, there is no dedicated tool in the World Bank Group financial inclusion tool kit designed to provide a comprehensive

and systematic assessment of the various aspects of financial inclusion.

This lack of a systematic diagnostic is a particular concern in areas where prudential regulations would not be applied, for example, stability and consumer protection issues related to mobile network operator-led mobile banking systems or savings and credit cooperatives, which are of particular importance for the rural poor.

The World Bank Group is developing potentially important instruments such as the Financial Inclusion Support Framework and a new template for the financial inclusion module of Financial Sector Advisory Programs. There is a strong potential for complementarity by using a combination of the World Bank's lending and AAA instruments and IFC's investment and advisory capacity, yet in many countries the benefits of strategic coordination and complementarity go unrealized. Therefore, it would seem appropriate that the current increased attention to financial inclusion is used as an opportunity to continue developing – and proceed to implementing – a holistic and systematic diagnostic tool for financial inclusion. IFC advisory interventions that foster elements of an enabling environment for financial inclusion are very relevant and important, despite their small scale. Following the recent Bank Group restructuring, some staff and responsibility have been transferred

from IFC Advisory Services to the Global Practice on Finance and Markets. IFC Senior Management envisages that future IFC Advisory Services mandates will be linked to investment opportunities, a characteristic most upstream advisory services interventions do not fulfill. The intention creates risks of curtailing or altogether stopping this type of advisory support. At the same time, the integration of IFC's Access to Finance Advisory Services into the global practice and IFC Financial Inclusion Group also has the potential to strengthen synergies and overall effectiveness.

### **Did Financial Inclusion Interventions Deliver the Expected Financial Services to the Poor?**

The World Bank Group “downstream support,” that is, support that targets financial intermediaries in delivery of services to the poor, encompasses a range of efforts: (i) World Bank lending, often including lines of credit, (ii) IFC's direct investments in or advisory services to MFIs, and (iii) MIGA's guarantees.

The World Bank's downstream support to financial inclusion represents 2 percent of its entire lending portfolio in volume and 6 percent in terms of number of projects. For IFC, the share of investments in MFIs represents a larger segment of its portfolio, 10 percent in number of

projects and 4 percent in volume. For MIGA, guarantees in support of MFIs amount to 4 percent of its gross exposure.

Overall, World Bank lending activity heavily focuses on the countries with the lowest levels of financial inclusion. Its work is mainly on credit, even though a significant share of its downstream technical assistance relates to payments, savings, and insurance. This is a promising trend, given that noncredit services are increasingly proving to have equal – if not higher – benefits for the poor. A challenge in World Bank lending projects has been excessive complexity, often manifested in too many components and subcomponents. The global practice has internalized this lesson, however, during the last few years and design complexity has improved. For monitoring and evaluation (M&E) the trend is less pronounced, for although the design of M&E systems improved, the usage rate of indicators generated is low.

An important issue in downstream work is subsidies, given the increasing difficulties of MFIs in recovering costs the more they approach the very low retail end of the market. Technological progress and innovative business models, such as agent banking or mobile money, may eventually allow MFIs (or other financial service providers) to reach the lower end of the retail market. Still, some level of

subsidization may be unavoidable also going forward, in particular in the area of rural microfinance, for example, through self-help groups, or when it comes to mass rollouts of no-frill accounts or digitalizing government-to-people or people-to-people transfers. Although digitalizing cash transfers may in fact save costs under the right circumstances—for example, reducing “leakage” and making delivery of public benefits more efficient—it cannot be assumed universally.

In particular, as those who are more proximate and easy to reach gain access, those who remain unbanked in the future are likely to be spread over a large number of countries, making mass rollouts increasingly difficult. Moreover, the unbanked of the future will increasingly be the rural poor. In these rural areas, digitalizing cash transfers and implementing mass rollouts are likely to face more fundamental challenges, for example, lack of network coverage in case of digitizing of cash transfers or creating a sufficiently dense agent network to cash out these transfers.

Although the World Bank Group has tended to discourage subsidies of interest rates, it has traditionally accepted subsidized interest rates in financial intermediation projects for poverty alleviation when they are “transparent, targeted, and capped,” explicitly budgeted, fiscally sustainable, equitably distributed, and

economically justified. Governments may choose to subsidize credit to overcome market failures that lead consumers to demand or providers to supply suboptimum amounts of financial services.

In such cases, the question of how to structure the subsidy arises. Up-front subsidies to address institutional costs of establishing or extending services are generally regarded as preferable to ongoing operational subsidies, because of both reduced price distortion and potentially lower risk of diversion or capture.

However, a more fundamental question surrounds the efficiency of subsidizing a single good, such as credit, versus an equivalent cash transfer to poor households to spend as they choose. What is clear from the World Bank Group’s portfolio is that, in practice, there is no consistent philosophy, with significant variations across projects and organizational units and practices. Very few of the World Bank’s downstream projects were evaluated during the period—only 14 downstream technical assistance projects and 6 downstream finance projects. Of these, development outcomes of financial inclusion projects corresponding to the portfolio overall, that is, about 70–75 percent, were rated successful. Projects using a mix of upstream and downstream or downstream technical assistance and finance in the same project were more common and had

## OVERVIEW

more successful development outcomes.

IFC's investments in financial inclusion are small, but they occur in markets where they matter; that is, they often reach countries that have high exclusion rates. IFC typically supports fully licensed banks but also supports nonbank MFIs.

When looking at development outcomes, financial inclusion investments perform slightly below average: 63 percent were rated satisfactory or better compared with a success rate of 67 percent across the entire IFC investment portfolio.

The investments by IFC in MFIs often struggle to achieve adequate business performance, but many also exhibit remarkable private sector development effects and good economic sustainability. The root causes for the low profitability of IFC's MFI investments include higher start-up costs and slower loan growth. IFC work quality was found to be high – and is hence not a factor behind the low business success.

Microloans represent about 5–10 percent of the loan portfolios of those banks that IFC supports with investments in which microenterprises or poor households are a declared beneficiary. The majority of IFC-supported banks (90 percent) have mixed portfolios; the rest of the portfolios are up to 10 times larger and

go to clients taking out significantly larger loans, including small and medium-size enterprises (SMEs). This indicates that IFC plays a role in the microsegment, but only a fraction of its support caters to the very small retail segment of the microcredit market.

This is not necessarily a bad thing, as, at least, SMEs are likely to benefit from such loans – and eventually microenterprises may benefit from the strengthening and deepening of the smaller end of the commercial finance market. But it argues for better segmentation and targeting of the micro and small and medium-size enterprise market as well as more accurate reporting on the reach to the very small retail segment of the microcredit market.

Within the microloan segment, IFC-supported banks issue loans slightly larger than their peers, indicating that they do not necessarily cater to the very lowest end of the microcredit market. The very low retail end of the market would, in many countries, be the rural poor that MFIs typically find hard to supply. The exceptions here are IFC-supported MFIs in South Asia that issue loans with a consistently small average value.

Monitoring and transparently reporting the extent to which IFC's loans reach the poor and microenterprises is important going forward. Based on IFC's current

approach, it is somewhat difficult to determine the share of the microloans reaching the poor and/or microenterprises, as IFC's reporting tools do not take into consideration the country-specific income situations and granularity of the economies.

Currently IFC calls loans smaller than \$10,000 "micro" loans, with which they aspire to support "microenterprises." IFC defines microenterprises as having less than \$100,000 in assets and/or annual sales and as having fewer than 10 employees.

In reality, according to IFC's own records, the median and average annual sales of IFC-supported microenterprises amount to \$152,000 and \$530,000, respectively – both considerably above the set threshold of up to \$100,000. Similarly, the median and average total assets amount to \$131,000 and \$352,000, respectively. IFC-supported microenterprises appear to meet the criteria only with regard to the number of employees, that is, 6 employees compared with the threshold of 10.

This raises doubt as to whether the institutions supported by IFC are effectively reaching microenterprises. In addition, the thresholds themselves raise questions, as they are set without reference to local conditions and income levels. What is adequate for Turkey is way too high a threshold for

"micro" in, for example, Tanzania. The Microfinance Information Exchange market can serve as an indicator for what is a normal value of a microloan: Microfinance Information Exchange reporting MFIs typically issue microloans averaging about 1.6 times the gross national income per capita in a respective country. This appears a reasonable proxy for a relative loan size and would translate into microloans averaging \$10,970 in Turkey but about \$860 in Tanzania.

The current practice of labeling investment as "in support of microenterprises" hence causes confusion and may raise undue expectations as to the number of microenterprises it is helping. Importantly for poor clients of microfinancial services, IFC-supported MFIs that reported data systemically on savers and borrowers managed to increase resource mobilization by increasing the number of savers among their clients – more so than their peers.

This is a potentially promising development, given that the literature indicates that savings have more positive effects for the poor than credit. It is promising that an increasing share of the entire World Bank Group's interventions go beyond credit – that is, address issues (or institutions) related to payments, savings, and insurance.

IFC's experience with MFIs illustrates the value of supporting *new* clients and investing in small and relatively pioneering projects that take longer to turn profitable, but that have a significant development impact. Some of IFC's greenfield investments in Africa are a good example of partnering with new clients and have resulted in projects with significant private sector development impact. At the same time, these projects illustrate that supporting projects that do not necessarily provide quick profitability may still be worthwhile. They also underscore the necessity for IFC to support relatively small projects, some of which can be quite transformational in that they establish industry leaders in the provision of financial services.

IFC advisory projects build capacity with local MFIs, help client MFIs develop products and services, and improve risk management processes. Measured by their development outcome rating, 64 percent of these projects are successful, corresponding roughly to the remaining access to finance advisory portfolio. IFC advisory projects rate high on output achievement (83 percent rated successful) and on strategic relevance (75 percent rated successful).

Performance drops when it comes to outcome achievement, for which only 62 percent of projects are successful — 10 percent lower than the average access to finance advisory service. Yet IFC advisory projects stand out for

their high-impact achievement — at least in relative terms — and for their high level of efficiency.

Mobile channels have the potential to provide access to financial services, in particular to payment systems, in ways that are more cost-efficient, safe, and convenient than existing alternatives. Uptake of such services, however, has been uneven across the globe, largely concentrated in eastern Africa. Of the 54 percent of adults in developing countries who own an account, almost all have an account at a *financial* institution: only 1 percent has both a financial institution account and a mobile money account, and 1 percent have a mobile money account only. The one regional exception is Sub-Saharan Africa, where mobile money accounts drove the growth of financial inclusion during 2014. Current challenges include interoperability and inadequate regulatory frameworks, which affects as many as 2 billion adults.

The World Bank Group has played a role as thought leader in setting the global agenda on digital payments for financial inclusion, along with a small group of international policy makers. At the country level, however, outside of Sub-Saharan Africa, the World Bank Group has played less of a leadership role in facilitating wider use of mobile money for broad-based financial inclusion, with the exception of a few countries.

With regard to working as “one World Bank Group,” IEG found that, based on the small number of countries with financial inclusion strategies in place during the portfolio period, there was potential for gaps, lack of complementarity and sequencing, and use of ad hoc work. Although instances of coordination showed great potential for synergy, country case studies also indicate the existence of frequent gaps, as well as lack of knowledge on the part of each institution (or even each global practice) about what others are doing.

Within the newly adopted Financial Inclusion Support Framework, however, the World Bank and IFC have increasingly worked together. The two institutions have developed joint financial inclusion approaches and action plans for the top 25 priority countries that are at the strategic focus of the World Bank Group at present.

### **Implications for the World Bank Group’s Financial Inclusion Strategy**

The Universal Financial Access goal 2020 is central to the World Bank Group’s strategy in financial inclusion. Accordingly, the World Bank Group’s approach—at least since its public commitment to this goal in 2013—centers on financial *access* through transaction accounts.

The public commitment to a measurable and tangible access goal

has contributed to sustaining an international dialogue and a multipartner campaign, and fostered consensus to advance the financial inclusion agenda. However, despite its public commitment to the Universal Financial Access goal, questions remain as to how the World Bank Group will operationalize this goal. The Bank Group’s current approach, characterized by the Financial Inclusion Support Framework, delineates principles of actions and key building blocks, but it remains to be seen how this goal will be translated into practice.

Conceptually, the link between access and inclusion (active use) of financial services is clear, but empirically, nonutilization rates in some schemes raise questions.

Whether access *results* in inclusion depends on the quality, design, and utility of this initial access. For example, the promotion of access through government-supported programs to digitalize cash payments via mobile phones or to roll out no-frill accounts for a large share of the population may not necessarily lead to use of a wider range of financial services.

Massive rollouts like India’s Pradhan Mantri Jan-Dhan Yojana scheme offer additional cautions—the World Bank finds that 72 percent of accounts opened under the scheme have zero balances (implying dormancy). The



latest Findex data point equally to low usage of accounts, despite strong growth in access to them. Globally, 460 million people have dormant accounts; that is, they have not made a single transaction during the last year. Dormancy and low usage are particularly strong in low-income and lower-middle-income countries.

Hence, the assumption that access leads to inclusion cannot be taken for granted. The linkage has to be understood in detail and lessons from experiences should be integrated into the design of new interventions.

In this context, the increased efforts of the World Bank to launch advisory services, research, and AAA work that is geared toward better understanding reform measures or which type of account best facilitates the access to and usage of a range of services are important. The relevant goal may indeed be providing services to everyone with a productive and beneficial use of them, instead of focusing on “headline numbers.”

Even when assuming that access leads to usage, the broader question remains: Do the poor actually benefit from financial inclusion? The above-referenced literature review and the qualitative beneficiary assessment conducted in the context of this evaluation confirmed that financial inclusion has been less effective in fighting poverty than previously believed. Credit, payments, savings, and insurance do not pull people out

of poverty but can help the poor manage their day-to-day struggles and offer options, especially with regard to education, health, and buffering income shocks. In view of these mixed results, ascertaining the benefits of financial inclusion for the poor through a systematic M&E system becomes important.

The Bank Group has started efforts to develop M&E concepts for the Financial Inclusion Support Framework, focusing on outcome and impact measures of financial inclusion. These are important developments that, once implemented, would have to be complemented by research efforts to better understand under which conditions access to financial services leads to inclusion and to welfare benefits to the poor.

Adopting a rigorous M&E framework as part of a sequenced approach to project implementation provides a sound way forward. Such an approach could focus on clearly delineated and evaluable interventions and incorporate lessons from past and ongoing interventions into the design of new interventions. Having a well-established M&E system in place is of particular importance, as the World Bank Group experiments with new ways to achieve the envisaged Universal Financial Access goal such as rollouts of no-frill accounts or digitalizing government-to-people payments. The World Bank Group will need to closely monitor outcomes to

ensure that financial services are rolled out to the people who can make good use of them—and that these services make their lives better.

Lowering transaction costs—not only initiation costs of, for example, setting up an account—through innovation is important in this context. Delivery models such as mobile or correspondent banking and agent and “branchless” banking and innovations in underlying technology platforms fall in this area, as do initiatives such as India’s use of the universal identification as a satisfaction of the know-your-customer requirement. Advancing these innovations, in partnerships with other agencies, through the suggested “sequenced approach”—where the benefits for the poor in initial interventions are continuously monitored—appears a potential way forward.

The current World Bank Group strategy focuses on 25 priority countries. This may entail an efficient allocation of resources, but it raises questions in light of the universality of the World Bank Group’s declared objective. In any case, the strategy may have to be adjusted going forward, as the remaining financially excluded will be increasingly broadly distributed across many countries.

This suggests that the World Bank Group should clarify its approach to financial inclusion. The Bank Group will also have to decide how it intends

to close the access gap that will remain in 2020. Recent extrapolations conclude that, although current efforts may reach over 1 billion people, allowing for population growth, by 2020 just over 1 billion people may still be unbanked.

How can the World Bank Group’s support help financial services to reach these 1 billion? Will the costs of reaching them be prohibitive or can new technologies and approaches make it achievable? Financial inclusion—if pushed to the very low retail end—is likely to require subsidization, as indicated by recent research. Striking a balance between the costs and benefits of universal inclusion and weighing these against the cost and benefits of other competing priorities will be essential as the World Bank Group provides support to its client countries in achieving the Universal Financial Access goal by 2020 and further financial inclusion goals beyond this.

In this context, the potential of traditional financial sector deepening to lift people out of poverty should not be overlooked. Financial sector deepening—though not directly providing the poor with financial services—strengthens the financial sector so that financial intermediation occurs in an effective and efficient manner. Efficient intermediation helps the private sector prosper, allowing SMEs and larger companies to grow

and expand employment, including for the poor.

### Recommendations

The following recommendations are intended to contribute to the World Bank Group's activities in support of financial inclusion for poor households and microenterprises:

#### **Recommendation 1: Clarify approach.**

The World Bank Group should adopt an evidence-based and comprehensive approach to financial inclusion that aims at enabling access to a range of financial services with benefits for the poor in a sustainable manner. This should be reflected both in broader strategies (such as that for the Finance and Markets Global Practice) and in its detailed business plan. As part of this approach, the conditions and business models under which subsidization is a useful tool to achieve sustainable services should be specified, and consistent, coherent guidance should be provided to staff on when and how to apply subsidy to financial services versus when a focus on markets can suffice. Also critical to this work is how the World Bank Group systematically finds and replicates innovations that lower transactions costs and improve financial inclusion (Recommendation 2).

#### **Recommendation 2: Find and replicate innovative delivery models of financial services to the poor**

**through sequenced and evidence-based approaches.** To deliver sustainable, low-cost services, the World Bank Group and its partners should research, pilot, and scale up innovative business models and approaches to reach underserved (especially rural) clients. Such an approach would focus on delineated and evaluable interventions and ensure a feedback loop in the design of new projects. A key part of this is to ensure that the World Bank Group effectively applies its research and evaluative resources to better understand the extent to which its interventions actually support poor households and microenterprises (as well as other excluded groups), and how best to adapt its interventions to different country conditions.

**Recommendation 3: Strengthen partnerships.** Recognizing the value of partnerships as a central instrument of its financial inclusion work, the World Bank Group should strengthen its partnerships by advocating clear strategies, results frameworks, and M&E arrangements for partnership arrangements it has joined or will decide to join.

**Recommendation 4: Implement new tools in country-based diagnostics and strategies.** In countries with a substantial current or planned engagement in financial inclusion, the World Bank Group should implement an appropriate, holistic, and systematic diagnostic tool and, based

on such diagnostics, develop country-level strategies for financial inclusion to guide its work. Special attention is appropriate for frontier customers and market segments in countries where there is already substantial engagement. These could inform the Systematic Country Diagnostics and

Country Partnership Frameworks. Connected to this, M&E systems should take account of results frameworks established in country financial inclusion strategies and take a practical and cost-effective approach to improving measures of beneficiary impact.

# Management Response

**World Bank Group Management welcomes the constructive analysis and recommendations of the Independent Evaluation Group (IEG) report.** The report provides an important opportunity to strengthen our evidence-based approach to supporting financial inclusion. It notes that support is well aligned with country priorities and that financial inclusion is a clear development priority. The report is especially timely and relevant as the World Bank Group reframes and scales up its interventions and partnerships to reach the Universal Financial Access (UFA) 2020 goal and to respond to increasing country demands for technical, knowledge, and financial support. There is strong coherence between the report recommendations and the current World Bank Group approach to work with partners to scale up a systematic approach at the country level, harnessing technology and innovation to expand access to, and use of, a range of quality financial services.

## World Bank Group Management Comments

**Management broadly concurs with the conclusions and recommendations of this IEG report.** Management responses to and comments on specific recommendations in the report are presented in the Management Action Record table.

**Management agrees that the World Bank Group could apply a systematic approach to financial access and inclusion across more countries than it does at present.** The current approach has been successfully applied in a number of relevant areas, including payments, financial consumer protection, access to financial services (including microfinance), and national financial inclusion strategies. Management will further develop the World Bank Group's "tool kit" for Universal Financial Access and Financial Inclusion, building on the World Bank Group's diagnostic tools, products, and standards/guidance. Management would like to note that, building on previous standard-setting or guidance efforts (e.g., the Principles for International Remittance Services), the World Bank and the Basel Committee for Payments and Market Infrastructures have jointly led a task force of global financial regulators to develop new guidance and recommendations on the payment aspects of financial inclusion.

**With regard to the IEG report's reference to operationalizing the UFA goal,** Management would like to refer to the Framework for Action for reaching this goal, and to the progress that has already made since President Kim announced this goal in October 2013:

- The World Bank has already approved new projects to reach a projected 482 million adults with accounts, and the International Finance Corporation (IFC) has approved new investments to reach a projected 339 million adults with accounts.
- The World Bank Group is now a technical partner for national Financial Inclusion Strategies in 17 of the 25 UFA priority countries (as compared to only 1 country when the UFA goal was launched).
- UFA Country Action Plans have been developed for the UFA priority countries, and new financial inclusion operations are under preparation for 18 of the 25 countries.
- The World Bank Group IDA17 target to support at least 10 low-income countries in achieving their national financial inclusion commitments is proceeding well.
- New guidance for the Payment Aspects of Financial Inclusion has been developed by the World Bank jointly with the Basel Committee for Payments and Market Infrastructures.
- The World Bank and IFC have developed a harmonized methodology for monitoring and reporting on financial access and inclusion activities. A model has been developed to project and track World Bank/IFC contributions toward the UFA goal and to guide the design of World Bank Group projects to target the most important levers for expanding financial access. This model can also be made available to countries and development partners to promote an evidence-based approach to reaching the UFA goal and facilitate setting and tracking national financial access/inclusion targets.

**Management found the IEG report generally useful and relevant, but would like to raise three points that diluted some of the analysis.**

- The IEG report does not sufficiently differentiate microcredit from broader financial inclusion. It also misuses the term *access to finance*, which specifically refers to credit, by applying it to a broader concept of *financial access*, which also covers accounts and other financial services. A prominent example (from the Highlights section) is the suggestion that the UFA goal proposes an expansion of credit, when in fact it proposes an expansion of accounts, precisely because of the concerns raised by the IEG report – the lack of evidence of the impacts of access to credit, and the much stronger evidence of the positive impact of basic savings and payment accounts. Also, in the Strategic Relevance section of the Conclusions and Recommendations, World Bank Group lending volume for financial inclusion is compared with the growth in volume of the microfinance institution “industry”; the concepts are distinct and should not be directly compared.

## MANAGEMENT RESPONSE

- The IEG methodology relies substantially on an analysis of investment lending projects approved in FY06–13. The analysis includes projects conceived over 8 years ago, despite the significant evolution of the World Bank Group's approach to financial inclusion since then. Support is reflected not only in lending volumes, but also in World Bank Group's strong emphasis on systematic reforms and diagnostics, and innovative business models. These elements are relatively under-emphasized in the report. The conclusions with regard to strategic relevance are focused on the growth in volume of World Bank Group lending, but should have also focused on the expansion of support for catalytic enabling environment reforms that are designed to promote innovative approaches, and to unlock the (much greater) levels of private sector investment that are needed.
- None of the financial inclusion projects of the Multilateral Investment Guarantee Agency have been evaluated so far.

### International Finance Corporation Management Comments

Management appreciates IEG's recognition of the investments and advisory projects of the IFC related to financial inclusion for their remarkable private sector development effects and high impact. Management is also pleased that the report acknowledges the strong relevance, leadership role, and high work quality of IFC's engagement in this area.

IFC's mandate is to support the development of sustainable private sector. On the basis of IEG's observation of a longer-than-expected gestation period before IFC microfinance investments become profitable, the report questioned whether our business model has hit its limit. One of the conclusions in the report, backed by IEG's literature review, also points to the likelihood that subsidies will be required to reach the very low retail end of the market. In this regard, we have had promising experiences without having to use subsidies, particularly in South Asia, where poverty levels are extremely high. IFC Management has also been strongly encouraged by rapid progress in rural mobile access boosted by technological advances and cost reductions. Management therefore continues to believe that financial inclusion goals can be met largely without subsidies and that doing so is an important part of the business discipline that we should apply. IFC is working closely with the World Bank to support governments in facilitating an adequate enabling environment.

Regarding IFC's support to microfinance institutions, especially on the contraction in IFC's investment activity in response to the 2008 global economic crises, our own data show that IFC's microfinance investment level through commercial banks and

microfinance institutions did not fall off. In line with IFC strategy in the financial inclusion space, IFC Management is also seeing a strong growth in IFC investments in financial technology and digital financial services.<sup>1</sup>

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<sup>1</sup> “Fintech” and “digital financial services” refer to the use of various forms of technology, specifically: hardware, software, and communications infrastructure, including telephones, mobile phones, and the internet, to originate, process, and fulfil a wide variety of financial services, from payments to loans to investment services. Technology applications are central to customer identification, risk assessment, transaction processing, and fulfilment and to ongoing information management and reporting.



# Management Action Record

IEG Findings and Conclusions	IEG Recommendations	Acceptance by Management	Management Response
<p>At present, the Universal Financial Access Goal 2020 (UFA) and the Financial Inclusion Support Framework (FISF) are key elements of the World Bank Group's engagement with member countries to promote financial inclusion. Although the public commitment to the UFA provides clear and measurable objectives, focusing the World Bank Group's activities on improving access to financial services through transaction accounts, there is limited systematic guidance on how to operationalize this goal into an actionable agenda. The FISF delineates some principles of action, and the preparation of country support programs is under way in a first set of countries; however, there is room for elaboration on the World Bank Group's overall approach to financial inclusion in several dimensions:</p> <p>First, the World Bank Group can make clear where evidence points to clear benefits to the poor, and where evidence is lacking, in light of overall mixed results in the literature on gains to the poor of financial services. The evidence from a broad-based literature review of more than 140 peer-reviewed publications indicates that the expectations of microcredit pulling millions out of poverty have not been fulfilled. While there is a consistent pattern of modestly positive effects of microcredit on the poor, these effects are not</p>	<p><b>Recommendation 1: Clarify approach.</b> The World Bank Group should adopt an evidence-based and comprehensive approach to financial inclusion that aims at enabling access to a range of financial services with benefits for the poor in a sustainable manner. This approach should be reflected both in broader strategies (such as that for the Finance and Markets Global Practice) and in its detailed business plan. As part of this approach, the conditions and business models under which subsidization is a useful tool to achieve sustainable services should be specified, and consistent, coherent guidance should be provided to staff on when and how to apply subsidy to financial services versus when a focus on markets can suffice. Also critical to this work is how</p>	<p>World Bank Group: Agree</p>	<p>The Finance and Markets Global Practice will adopt an evidence-based and comprehensive approach to financial inclusion that aims at enabling access to a range of financial services with benefits for the poor in a sustainable manner.</p> <p>The World Bank Group has for a number of years been using a standardized, comprehensive approach for diagnostics and support for relevant areas of financial inclusion, such as payment systems, financial infrastructure, and financial consumer protection.</p>

<p>transformative. The more limited evidence on noncredit services tends to be more encouraging.</p> <p>Second, a fully elaborated World Bank Group approach should address the need to find a balance between supply-driven approaches for access to finance and <i>enabling</i> actual inclusion. It is widely recognized that universal financial access is not the same thing as universal financial inclusion, which is a much broader concept based on quality, choice, inclusiveness, and range of services available to the poor. True inclusion involves actual use of offered services. There is insufficient evidence to assume that universal access will lead to universal inclusion, especially in light of the high dormancy of accounts newly opened through mass rollouts and low utilization rates of newly opened accounts in low-income and lower-middle-income countries in general. Investing in financial infrastructure, for example through no-frill accounts or transferring G2P payments from cash payments to accounts, may enable access to limited financial services for most of the excluded fairly quickly. Under the right circumstances, this may be self-financing, but as inclusion progresses the excluded ones will increasingly be spread over many countries and many of them will live in the rural areas where such initiatives are likely to incur costs, without providing active or demanded services to many. The relevant goal may be providing services to everyone who can make a productive or beneficial use of them.</p> <p>Third, if pushed to the very low retail end or to mass rollouts aimed at quickly providing financial access to</p>	<p>the World Bank Group systematically finds and replicates innovations that lower transactions costs and improve financial inclusion (Recommendation 2).</p>	<p>The IEG methodology looked back to projects approved between FY06 and FY13, and also focused in more detail on lending/investment projects. The coverage of analysis did not fully reflect the strong emphasis on support to enabling environment reforms and government interventions that lower the costs and risks of providing financial services to all and encourage innovative models. Since FY13 the World Bank Group has expanded its support to over 20 countries in designing or implementing national financial inclusion strategies which go well beyond microcredit or access.</p> <p>Moreover, the programmatic approach being implemented by the World Bank Group</p>
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## MANAGEMENT ACTION RECORD

<p>high number of people, supported interventions may involve subsidization, as do several recent World Bank activities on financial inclusion in the rural space through self-help groups. Any ongoing subsidy requires fiscal sustainability, but also needs to be justified as an effective use of development resources. Currently, however, the World Bank Group lacks systematic guidance to clients and staff providing a consistent and rational basis on when and how subsidies should be used to extend financial services to the poor. As noted in the evaluation, in practice, interventions at times reflect different philosophies and approaches to subsidization of financial services across projects, countries, and practice groups.</p>			<p>for financial access and inclusion includes a strong emphasis on data and diagnostics underpinning reform priorities and actions, and on enabling environment reforms and other measures to encourage investment in innovative models.</p> <p>Management would like to reaffirm that evidence on the impacts of credit versus other financial services has already been taken on board in the design of the World Bank Group's UFA goal (which is for payments and savings accounts) and in the broader programmatic approach to financial inclusion, which is increasingly the norm for World Bank Group country engagement.</p>
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<p>Innovation is still needed to enable the poor to sustainably access a range of financial services. The promise of financial inclusion is that credit, savings, and payment and insurance services help the poor manage their day-to-day lives and offer choices and risk mitigation mechanisms. Yet the evidence to date suggests only modest and mixed benefits of major approaches, emphasizing the need for a sequenced approach toward innovations facilitating financial inclusion.</p> <p>Lowering transaction costs through innovation is recognized as an essential challenge in the context of sustainably reaching the poor and underserved. This evaluation found that financial inclusion faces persistent obstacles in reaching the rural poor. Among promising areas of innovation are delivery models such as mobile, correspondent banking, agent, and “branchless” banking, as well as innovations in underlying technology platforms and initiatives such as universal identification and biometrics to satisfy the know-your-customer requirement. An important way forward is to systematically use a sequenced approach building on comparative advantages of development partners and the World Bank Group to develop, test, and scale up these and other innovations, rigorously monitoring the benefits (and costs) for the poor.</p> <p>Such a sequenced approach focuses on clearly delineated and evaluable interventions, building on lessons from past and ongoing interventions and dynamically feeding these lessons into the design of future projects. Given that only 2 percent of World</p>	<p><b>Recommendation 2: Find and replicate innovative models for delivering financial services to the poor through sequenced and evidence-based approaches.</b></p> <p>To deliver sustainable, low-cost services, the World Bank Group and its partners should research, pilot, and scale up innovative business models and approaches to reach underserved (especially rural) clients. Such an approach would focus on delineated and evaluable interventions and ensure a feedback loop in the design of new projects. A key part of this is to ensure that the World Bank Group effectively applies its research and evaluative resources to better understand the extent to which its interventions actually support poor households and microenterprises (as well as other excluded groups), and how best to adapt its interventions to different country conditions.</p>	<p>World Bank Group: Agree</p>	<p>The World Bank and International Finance Corporation (IFC) systematically identify and support innovative approaches to financial inclusion already. For example: (a) the UFA 2020 conceptual framework identified critical reforms and government actions to drive the expansion of transaction accounts, including through e-money and “digital” delivery mechanisms, and the World Bank Group is orienting its financial inclusion support accordingly; and (b) in early 2015 the World Bank, IFC, and the Consultative Group to Assist the Poor (CGAP) launched the cross-World Bank Group’s “Harnessing Innovation for Financial Inclusion” program,</p>
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## MANAGEMENT ACTION RECORD

<p>Bank Group operations report on beneficiary outcomes, such a feedback loop clearly does not yet exist even within the World Bank Group's own portfolio. The weak evaluative evidence of a clear connection between the World Bank Group's interventions and increased financial inclusion emphasizes the need for a more robust approach to Monitoring and Evaluation (M&amp;E) as part of this sequenced approach.</p>			<p>which will cover over 20 countries.</p> <p>The World Bank and IFC have strengthened reporting and monitoring of financial access/inclusion activities, for example through evaluations conducted by DEC on financial literacy and consumer protection. Management will further explore how to apply a similar approach more systematically to other areas relevant to financial inclusion. Monitoring and evaluation is already central to the global initiatives introduced to strengthen and scale up the World Bank Group's support to financial access/inclusion, including through the FISF and the Harnessing Innovation for Financial Inclusion program.</p>
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			Through the UFA 2020 initiative a reporting model has been developed and is being rolled out in World Bank lending and ASA projects, in close coordination with the IFC (which has a similar model).
The World Bank Group supports policy reform and leverages its country-level impact through a wide range of influential international partnerships, as well as through its policy work, dialogue, and technical assistance. Partnerships clearly extend reach, resources, and influence to promote access to financial services by the poor and microenterprises (and other excluded groups). Organizations like CGAP, the Global Partnership for Financial Inclusion, the Center for Financial Inclusion, and the Alliance for Financial Inclusion have a strong standing with relevant stakeholders and can provide opportunities for knowledge sharing, policy influence, global standard setting, and piloting and disseminating innovative approaches. Partnerships also play a large role in the World Bank Group's goal of universal financial access and longer-term inclusion goals, and can amplify the World Bank Group's leadership on key issues ranging from bank supervision to remittances to digital payments.	<b>Recommendation 3: Strengthen partnerships.</b> Recognizing the value of partnerships as a central instrument of its financial inclusion work, the World Bank Group should strengthen its partnerships by advocating clear strategies, results frameworks, and M&E arrangements for partnership arrangements it has joined or will decide to join.	World Bank Group: Agree	Management continues to work with development partners, bilaterally and through an active Financial Inclusion coordination group, to strengthen and structure joint approaches, including through country coordination mechanisms, and potentially through Memoranda of Understanding where appropriate.  There is a long-standing collaboration in place with international standard setters on several aspects related to

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<p>At the same time, these partnerships bear costs and risks in terms of resources and senior staff time and potentially diluting the World Bank Group’s “branding” and strategic focus. They involve costs, compromise, and coordination that would be ameliorated by clear strategies, accountability, and learning systems of the partner organizations. CGAP has only quite recently developed a clear results framework, and IEG did not come across results frameworks or independent reviews or evaluations of other partnership bodies, beyond a progress report. In this context World Bank staff reported that advocating for such systems is likely to gain more traction in partnerships where the World Bank Group is a major stakeholder, hosts the secretariat, or contributes resources.</p>			<p>financial inclusion, which led to issuing key standards / guidance.</p>
<p>The World Bank Group plays a significant role at the country level in advancing the policy reform needed for financial intermediaries to thrive and better serve the needs of the poor and unbanked. But the World Bank Group’s approach to identify and tackle constraints to financial inclusion is neither sufficiently systematic nor comprehensive.</p> <p>The World Bank Group played an important role in identifying major legal and oversight gaps, and most projects were also executed with good work quality. According to the World Bank’s own self-rating scheme, analytic and advisory work delivers an important and often successful contribution to the policy reform process.</p>	<p><b>Recommendation 4: Implement new tools in country-based diagnostics and strategies.</b> In countries with a substantial current or planned engagement in financial inclusion, the World Bank Group should implement an appropriate, holistic, and systematic diagnostic tool and, based on such diagnostics, develop country-level strategies for financial inclusion to guide its work. Special attention is appropriate for frontier customers and market segments in countries where there is already substantial</p>	<p>World Bank Group: Agree</p>	<p>Management has adopted a systematic and comprehensive approach for new engagements in over 20 countries, linked to national financial inclusion strategies, FISF programs, and Financial Inclusion Programmatic Approaches, as well as for payment systems-related engagements globally. Central to this approach is a focus on data, diagnostics, and monitoring frameworks.</p>

<p>The World Bank Group’s diagnostic work is more comprehensive in some areas than in others. Payment systems, remittances, and financial infrastructure were covered by structured surveys or tool-based diagnostics; in other areas, such as consumer protection and financial literacy, stronger analytical support is under way or planned. However, particularly in areas in which prudential regulations would not be applied, the identification of constraints and priorities was at times not part of a holistic assessment of the adequacy of the various elements of the financial inclusion framework. Given the emergence of new technology as a potential solution, such diagnostics would have to also address issues of stability and consumer protection relating to Mobile Network Operated–led mobile financial services—currently not systematically part of a country assessment. For the rural poor, savings and credit cooperatives often matter, yet the World Bank Group’s country diagnostics pay uneven attention to these important financial inclusion tools. In some country cases, the lack of traction in policy dialogue at the strategic level may have contributed to such an omission in the absence of a coherent national strategy for financial inclusion.</p> <p>One of the root causes for this is the fact that there is no dedicated tool in the World Bank Group’s financial inclusion tool kit designed to provide a comprehensive and systematic assessment of the various aspects of financial inclusion. Therefore it would seem appropriate that the holistic and systematic diagnostic tool for financial inclusion that is currently under development be finalized and implemented. Initiatives to develop a</p>	<p>engagement. Such diagnostics could inform the Systematic Country Diagnostics and Country Partnership Frameworks. Connected to this, M&amp;E systems should take account of results frameworks established in country financial inclusion strategies, and take a practical and cost-effective approach to improving measures of beneficiary impact.</p>		<p>Management will also further strengthen and add to the “tool kit” of products, technical guidance, and diagnostic models relevant to universal financial access and financial inclusion. During the first half of FY16, Management will complete the revision of the Guidance Note for financial inclusion in FSAPs.</p>
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<p>systematic financial inclusion module for the Financial Sector Assessment Program (FSAP), to roll out the FISF, and to elaborate country-level financial inclusion strategies appear to be positive steps.</p> <p>To assess progress in policy reform and in financial inclusion in general, monitoring and evaluating the results of country-level financial inclusion strategies is essential. A vital part of this is tracking beneficiary effects. However, projects most often track only the level of financial intermediation (about 45 percent), that is, the number and volume of loans. About 20 percent of projects track outputs related to the provision of workshops, trainings, reports, and studies. About 7 percent track changes in the enabling environment or other goals related to policy reform work. Only 2 percent report on beneficiary effects such as improvements in welfare or increases in income. In assessing beneficiary effects, the unavailability of baseline data is often a challenge.</p>			
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# Chairperson's Summary: Committee on Development Effectiveness

The Committee on Development Effectiveness welcomed the main findings and recommendations of Financial Inclusion – A Foothold on the Ladder toward Prosperity? – An Evaluation of World Bank Group Support for Financial Inclusion for Low-Income Households and Microenterprises and Management's response. It commends the report's comprehensiveness and the close collaboration between Management and the Independent Evaluation Group (IEG). Members noted the similarities between IEG's recommendations and the existing World Bank Group approach. Members stressed the importance of financial inclusion (FI) to achieving meaningful development outcomes and acknowledged the significant steps the World Bank Group has taken to further national and global progress on the FI agenda. Members remarked that FI goes beyond access alone, suggesting that it is only possible with comprehensive and appropriately targeted interventions and partnerships. They urged Management to expand its interventions to directly benefit the most underserved populations, especially women, and to do more with the World Bank Group's existing innovations. Management clarified that IEG's findings confirm the World Bank Group's progress toward FI, both through projects and AAA work, the latter of which was not covered by the evaluation. Members agreed with the recommendation to scale up the World Bank Group's evidence-based approach, as data suggests that FI has not been as successful in reducing poverty as was once thought.

Because access does not guarantee utilization, the Committee asked Management to pursue innovative delivery models, some of which are already in use, including enhancing consumer protection, financial literacy, and knowledge for meaningful transactions and services. Members supported Management's proposal to broaden financial services, including payment and savings, and possible financial support, to expand the reach of FI. The Committee supported reinforcing strategic partnerships, technology, and diagnostics in addition to implementing new tools to address both access and inclusion. Members agreed that the approach of the institution, including the Consultative Group to Assist the Poor, on financial inclusion could be further strengthened. Members stressed that financial inclusion should embrace all constituencies, particularly women, in an effort to reach the poorest and the most vulnerable, and thus meet the Sustainable Development Goals and reach the Universal Financial Access Goal in 2020.

## **CHAIRPERSON'S SUMMARY: COMMITTEE ON DEVELOPMENT EFFECTIVENESS**

While acknowledging some of the World Bank Group innovations introduced to date, members urged Management to think creatively about what the institution can do differently to promote usage. They supported the significance of internal World Bank Group coordination on the institutional toolkit, of the product mix, of the role of technology, e.g., to scale up digitally enabled financial services. In this respect, they also underlined the importance of partnerships with other stakeholders and welcomed a joint discussion on how to strengthen the results frameworks on these partnerships. Members commented on the World Bank Group use of subsidies as an instrument for expanding financial access to the poor under certain conditions. They agreed on the need for further discussion to reflect on the use of subsidies, their application, opportunity costs and implications.

The Committee noted that evidence illustrates that providing women access to financial services is critical to their empowerment and to development more broadly, adding that they would have liked to have seen a stronger and more explicit representation of gender in the report. Members called for a clearer, more comprehensive and innovative approach in this respect, including in country tools. They welcomed Management's efforts to support innovative approaches to FI and the World Bank Group's role in supporting the design and implementation of national FI strategies.

Alejandro T. Foxley  
CHAIRPERSON

# 1. Do Financial Services Help Fight Poverty?

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## Highlights

- ❖ The poor face tremendous financial challenges and often require access to financial services to meet essential needs, yet they are mostly excluded.
  - ❖ Financial inclusion—the access to and usage of a range of financial services—has the potential to benefit the poor through an array of channels: affordable and reliable payment systems for daily transactions or for remittances; credit or savings to smooth consumption and protect against shocks; and financing to make large investments, for example, for housing or to enhance the productivity of microenterprises.
  - ❖ Over the last 10 years, the microfinance industry grew in terms of numbers—and even more dramatically in terms of assets. The World Bank Group spent about 2–3 percent of its annual commitments on financial inclusion–related projects.
  - ❖ In 2013, the World Bank Group declared universal financial access by the year 2020 to be a goal that is within reach through new technologies, transformative business models, and ambitious reforms. The rationale for World Bank Group support for financial inclusion lies in its ability to improve how markets work by overcoming limitations to market demand and supply so more and better financial services are provided to the poor.
  - ❖ The Independent Evaluation Group reviewed the experience of the World Bank Group with financial inclusion to inform not only the implementation of the World Bank Group’s Universal Financial Access Goal and its longer-term aim for financial inclusion of the world’s poor but also the strategic discussion in and outside the World Bank Group about the role of financial inclusion in the post-2015 development agenda and the ways the World Bank Group can support it.
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Providing the poor with an array of financial services—or trying to “financially include” them—has become a growing focus for policy makers, development partners, and other key stakeholders. It is a means to promote shared prosperity and reduce poverty. Even though many countries have made considerable progress over the last few years, about 2 billion adults worldwide are still “unbanked,” and close to 200 million formal and informal micro, small, and medium-size enterprises in developing economies lack access to affordable financial services and credit.<sup>1</sup> The poor in particular are often excluded from financial services, but at the same time require such services to smooth their volatile (and low) incomes, protect against vulnerabilities, or just facilitate day-to-day transactions.

In 2013, President Jim Yong Kim of the World Bank Group declared universal financial access by the year 2020 an aspirational goal of the World Bank Group, a goal that is “within reach—thanks to new technologies, transformative business models and ambitious reforms” (World Bank 2013).<sup>2</sup> For the World Bank Group, expanding financial inclusion is now understood to be a core mean through which

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financial sector development contributes to its twin goals of ending extreme poverty and promoting shared prosperity with regard to poor households and microentrepreneurs.

In this evaluation, the Independent Evaluation Group (IEG) reviewed the experience of the World Bank Group with financial inclusion during the last six years. The goals of IEG's evaluation are to inform not only the implementation of the World Bank Group's Universal Financial Access Goal, but also to inform the strategic discussion in and outside the World Bank Group about the role of financial inclusion in the post-2015 development agenda and the ways the World Bank Group can support it. With the formation of a new Global Practice Group on Finance and Markets and the general reorientation and reorganization of the World Bank Group to enhance focus on attaining the twin goals, understanding the lessons of recent World Bank Group experience is critical. On the global development agenda, 2015 will be the window through which the development world looks beyond and capitalizes on the momentum generated by the Millennium Development Goals thus far. Even though the Millennium Development Goals did not address financial inclusion per se, the post-2015 development agenda will likely show financial inclusion having a larger role in future global development efforts to combat extreme poverty and boost shared prosperity.<sup>3</sup> This evaluation is hence centrally relevant for both the World Bank Group and the global development community.

The evaluation focuses on financial services for poor households and micro and very small enterprises,<sup>4</sup> in light of the World Bank Group's central goal of fighting poverty—reaffirmed by the 2013 strategy's dual goal of ending extreme poverty and promoting shared prosperity. It analyzes the World Bank Group's interventions considering the needs and constraints of the poor with regard to accessing financial services.

### Why Being Financially Included Matters for the Poor

The poor face enormous financial challenges in meeting essential needs. Poor families are more likely to send their members to faraway cities or even abroad, in the hope that they will send money home—creating the need for transfers (remittances). The income of the poor is not only lower but also more volatile. People who live on an average of \$2 per day often make \$4 one day, \$2 the next, and \$0 the day after, as they rely on a range of often unpredictable jobs and often lack salaried employment; or big earnings may even come only once a season with harvest income (Banerjee and Duflo 2007; Morduch 1998). *Portfolio of the Poor* (Collins and others 2009) found that managing day-to-day cash flow was one of the

three main drivers of financial activities of the poor. Transforming irregular income flows into a dependable resource to meet daily needs poses a central challenge for the poor. Access to formal financial institutions can bring needed reliability to their financial lives: well-regulated formal financial institutions take savings and pay out loans in the amount and at the time promised, show respect to their clients, and are less likely to demand bribes, making their services more dependable and reliable. This may be as important as improving the livelihood of the poor—and the first element (reliability) may pave the way for the second element (prosperity) down the road.

Financial inclusion has the potential to benefit the poor through an array of channels both directly or indirectly. For example, affordable and reliable payment systems have the potential to facilitate day-to-day financial transactions such as the above-mentioned remittances or through credits and savings to smooth consumption. The latter is particularly valuable for poor households as they tend to have unpredictable—or often only seasonal—incomes. Another benefit is protecting against vulnerabilities such as illnesses or unemployment through primary savings or insurance, but also credit and remittances. Loans taken out or savings may be used to pay for child education or health care. A final key benefit can be making investments to, among other things, improve the condition of housing or to enhance the productivity of a very small or microenterprise through savings or credit (Center for Financial Inclusion 2009; Collins and others 2009; Banerjee and Duflo 2007). Though informal services may make up for part of these benefits, they may be unreliable, risky, costly, and unsafe (Roodman 2012; Collins and others 2009). The poor, however, are far more often excluded from formal financial services. Of the 2 billion “unbanked” people, most live in developing countries. Despite considerable progress over the last few years, 46 percent of adults in developing countries are still unbanked, compared with only 6 percent in developed countries (Demirguc-Kunt and others 2015). Among them, the poor are hit the hardest: Of those living on \$2 per day, fully 77 percent lack a bank account. Figure 1.1 shows the gaps in financial inclusion in terms of formal account penetration across the globe. Household income, education, and whether one lives in a rural area are factors that are strongly related to the extent of financial inclusion, even more so in developing countries (World Bank 2014).<sup>5</sup>

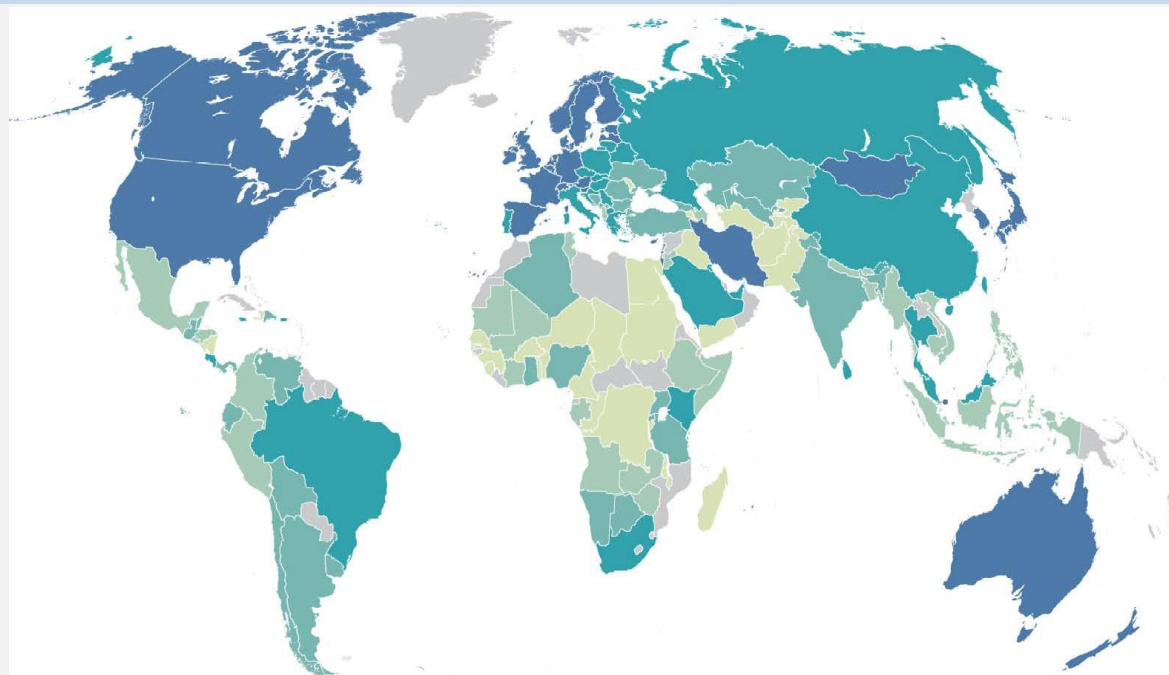
There has been considerable progress in financial inclusion in recent years, but it has been uneven across countries and not necessarily pro-poor or pro-women. Overall, the number of unbanked decreased from 2.5 billion in 2011 to 2.0 billion in 2014, connecting about 700 million to accounts. The difference between the decrease in the number of unbanked (500 million) and the number of those newly connected (70 million) is a result of population growth during these three years. Account

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ownership increased in all Regions but was particularly strong in East Asia and Pacific, South Asia, and Latin American and the Caribbean Regions—in each Region by about 10 percent.

**Figure 1.1. Global Map of the Financially Excluded: Formal Account Penetration**



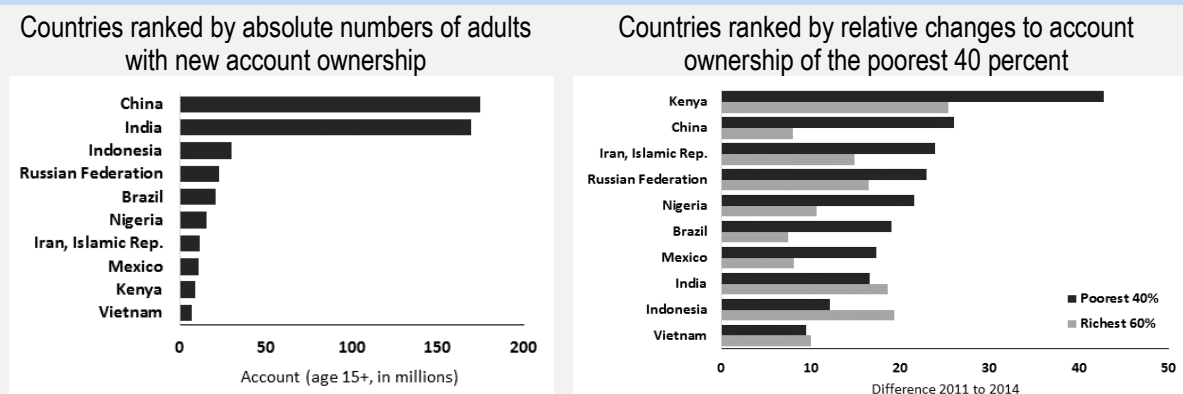
Source: Demircuc-Kunt and others 2015.

Note: Adults with an account (%), 2014: 0–19, 20–39, 40–64, 65–89, 90–100, No data available.

Growth has been more limited in the Middle East, North Africa, and Sub-Saharan African Regions. The gender gap remained at 9 percent; similarly, the youth gap remained constant. China and India provided the most people with new accounts, but it was China that connected the most poor to the financial system. In relative terms, China was only surpassed by Kenya which, globally, was the country with the strongest relative growth in financial inclusion for the poorest 40 percent. Other countries with strong pro-poor financial inclusion progress are the Islamic Republic of Iran, the Russian Federation, Nigeria, Brazil, and Mexico. In India and Indonesia, although absolute numbers of newly connected people are high, their growth benefited either both, the bottom 40 percent and the wealthier 60 percent (as in the case of India) or more the wealthier 60 percent (as in the case in Indonesia) (see figure 1.2).

The challenge going forward will be to gain a better understanding of what drove success in those countries where financial inclusion was pro-poor and pro-women and what policy implication can be derived for the World Bank Group's pursuit of its Universal Financial Access goal by 2010.

**Figure 1.2. Progress in Financial Inclusion 2014**



Source: Findex data from 2014.

## Today's Multidimensional Concept of Financial Inclusion

Today leading policy makers have settled on a broad-based concept of financial inclusion. Financial inclusion encompasses four basic financial services – savings, payments, credit, and insurance.<sup>6</sup> To achieve full inclusion these services should be designed in a manner accessible to traditionally excluded groups, including to the poor, women, minority groups and those difficult to reach, for example, rural dwellers. In addition, provision of these services ought to meet adequate levels of quality, that is, should be affordable, available, and stable and follow minimum standards of consumer protection. Finally, these services should be provided by a range of institutions to allow for choice and competition. Figure 1.3 shows the current concept of financial inclusion, which is based on the recently developed vision of the G20 and the Center for Financial Inclusion (GPFI 2012; Center for Financial Inclusion 2009).

“Financial inclusion” is about offering access to *formal* financial services. All those without a bank account – or access to any other financial services – with a formal financial institution such as a bank, credit union, cooperative, post office, or microfinance institution are among the financially excluded. In practice, there is a continuum of inclusion extending from those who use no financial services to those who use only informal services such as money lenders or family members, to those who use some mix of informal and formal services, and finally to those who exclusively use formal services. Financial inclusion does not only refer to access, but also to the usage and quality of financial services.<sup>7</sup> Even those with access to some formal financial service may be partially excluded by lack of access to other services. It is also important to note that some people are voluntarily excluded from the

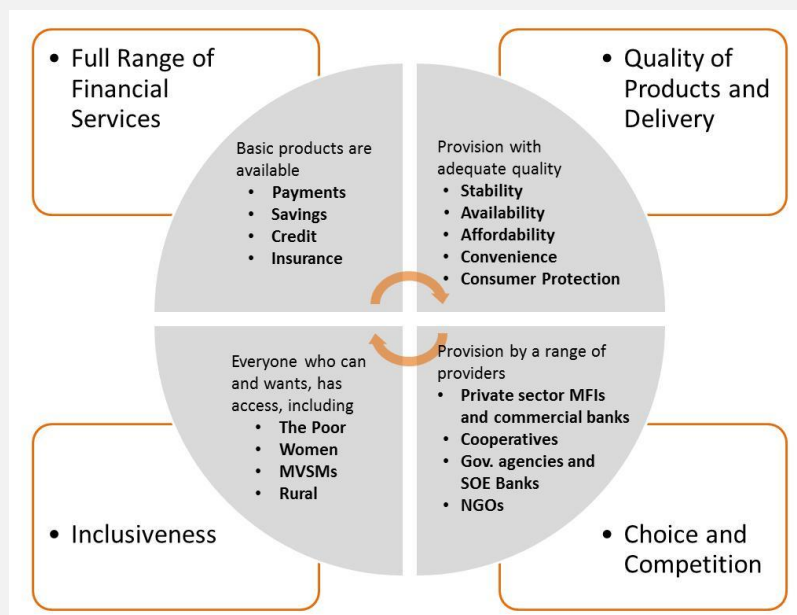


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financial system because they have no rewarding use of it or are content with informal alternatives.

**Figure 1.3. The Four Dimensions of Financial Inclusion**



Source: Based on GPFI (2012).

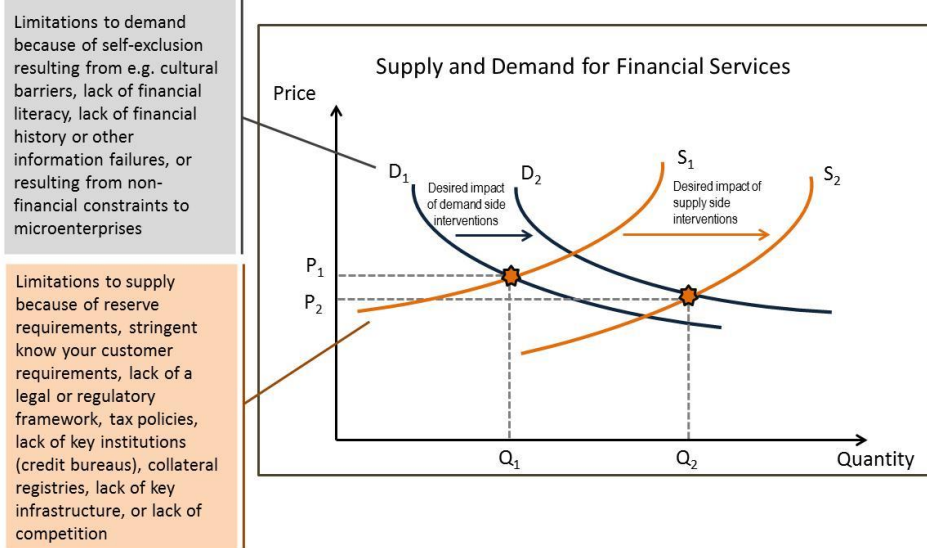
This evaluation adopted this broad-based concept – with a special focus on the poor.<sup>8</sup> The evaluation’s primary attention was on payment, savings, credit, and insurance as the key building blocks of the financial inclusion agenda. Assessment criteria for outcomes, in line with this framework, comprised not only access but also usage and associated quality features and the extent of choice and competition of the provision of financial services. From a supply perspective, it looked at all World Bank Group interventions that foster financial inclusion and hence went beyond formal financial institutions, for example, by also including mobile money systems that are led by a mobile network operator (MNO). From a demand perspective, the evaluation also captured financial literacy and consumer protection, both of which relate crucially to information failures that may suppress market development. The evaluation’s focus was primarily on the poor,<sup>9</sup> given the World Bank Group’s poverty reduction goals, and in this respect applies a somewhat narrower concept.

### Rationale for the World Bank Group’s Interventions

The rationale for World Bank Group support for financial inclusion lies with its ability to improve market mechanisms by overcoming limitations to demand and

supply enabling a more and better financial services provision to the poor. The financially excluded cite specific barriers for not using financial services. For example, barriers include that banks are too far away or that accounts are perceived as too expensive, that potential clients lack the necessary documentation or trust in the bank, or religious reasons (Demirguc-Kunt and Klapper 2013). These barriers can broadly be grouped into supply-side and demand-side factors (Beck and de la Torre 2006).

**Figure 1.4. World Bank Group Interventions and Their Effect on Supply and Demand of Financial Services for the Poor**



Source: Adapted from Beck and de la Torre (2006).

The Bank Group's development interventions can be seen as working to shift the supply and/or demand curves, shown in figure 1.4, to yield more formal services (to more households and micro and very small enterprises), potentially at lower prices.<sup>10</sup> Supply-side interventions would seek to deliver more services at any given price and/or reduce the price of services for a given quantity, shifting the supply curve out from  $S_1$  to  $S_2$ . For example, if International Finance Corporation (IFC) investments facilitate the possibility of microfinance institutions (MFIs) to expand their supply of microcredit, the supply curve would shift out.

If the World Bank's policy consultations with a government led to reforms that made lending in small amounts cheaper or more secure, the supply curve could also shift out. Demand-side interventions seek to increase the quantity of services demanded at a given price. Consumer financial education and entrepreneurship assistance programs provide potential examples in which entrepreneurs or households may, given improved knowledge and opportunity, shift their demand

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from D1 to D2 (figure 1.4). Interventions that remove nonfinancial barriers to successful microentrepreneurship (for example, an improvement in the electricity supply or improvements in macroeconomic stability) could also shift the demand curve for financial services out, although these factors are generally outside the scope of this evaluation. An added benefit of these shifts is the increase in consumer surplus (not shown) to poor households and microentrepreneurs consuming financial services. Interventions that do not shift supply or demand may be seen as lacking a sustainable effect on the market for financial services, and hence on financial inclusion.

Financial institutions that are commercially oriented – or that at least operate on a cost-recovery basis – quote transaction costs and risks as major barriers for providing financial services to the low end of the market. The fixed cost of financial service provision<sup>11</sup> makes provision to low-income segments of the population more difficult, as customers in these segments demand smaller and/or fewer transactions. Dispersed populations in rural areas also make traditional financial service provision through brick-and-mortar branching less commercially viable outside urban centers. In addition, risks might be prohibitively high to reach out to the low end of the market. A large share of households and economic agents in developing countries operate in the informal sector, relying often on volatile income streams with limited or no record of their creditworthiness.

Several of the listed constraints can be seen as market failures. Markets may not provide the data to overcome the information asymmetry between providers and potential borrowers; suppliers of financial services may not know about the potential business opportunity or may not have any incentive to move toward the lower end of the retail business. Instead, they remain in business areas with more reliable margins, such as corporate banking – or, if at all active in the retail end, prefer to serve salaried workers. The size of the low-end market may also provide insufficient incentives for technological innovation, but rather deter first movers – even more so as private sector players would not directly benefit from the social and economic externalities of having the poor financially included.

The World Bank Group plays a role in alleviating these market failures by assisting countries build adequate financial infrastructure, such as credit registries or bureaus or regulatory frameworks and capacity, or by investing in greenfield MFIs that pioneer the provision of financial services in untested and riskier environments, potentially inspiring other investors to follow suit. The Bank Group can also play a role in lowering transaction costs by piloting innovative delivery models, such as mobile or branchless or agent banking or assisting countries in scaling up these

channels. This could help demonstrating that through such new channels, the provision of services at the very low retail end is possible.

Similarly, the World Bank Group can also help overcome government failures. The poor – and in particular those working in the informal sector – often lack the formal documentation necessary for financial transactions. This problem is exacerbated with tighter know-your-customer (KYC) documentation and regulations introduced in the past decade across the globe to fight money laundering and terrorism, in conjunction with lack of comprehensive identification systems in many low-income countries. Prudential regulations may not be proportional with the risks MFIs encounter, preventing them from going downstream, or regulatory gaps may pose too high a risk to open a financial service business. Again, the World Bank Group can play a role in addressing these government failures through policy dialogue, advice, or technical assistance to build a suitable enabling environment for financial inclusion, including fit-for-purpose oversight regimes and codes for operational engagement for nonbank financial institutions, such as cooperatives, which are typically not subject to prudential regulations.

### **The World Bank Group's Operational Engagement: A Snapshot**

Before assessing the World Bank Group financial inclusion agenda at a more detailed level, the highlights of its operational engagement are set out.

Operationally, the World Bank Group has deployed a wide range of services and products, through the World Bank, IFC, and the Multilateral Investment Guarantee Agency (MIGA). IEG identified 885 inclusive finance projects committed between fiscal year (FY)07 and FY13 (an average of 125 projects per year), with a total commitment value of \$9 billion (an average of \$1.3 billion per year; Table 1.1).<sup>12</sup> IFC accounted for the highest share of financial inclusion projects, both by number of projects (65 percent) and commitment value (49 percent). World Bank's lending accounts for 32 percent of total Bank Group projects and 45 percent of commitments, due to larger average project size. MIGA's relative share is only three percent of projects and 6 percent of value (measured by gross exposure; figure 1.4). For this evaluation, IEG identified the World Bank Group's financial inclusion portfolio in a coordinated manner with World Bank Group management; for a detailed methodology on these criteria and the method used, please see appendix A.

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**Table 1.1. Coverage of Evaluation: Inclusive Finance Projects Approved or Committed FY07–13**

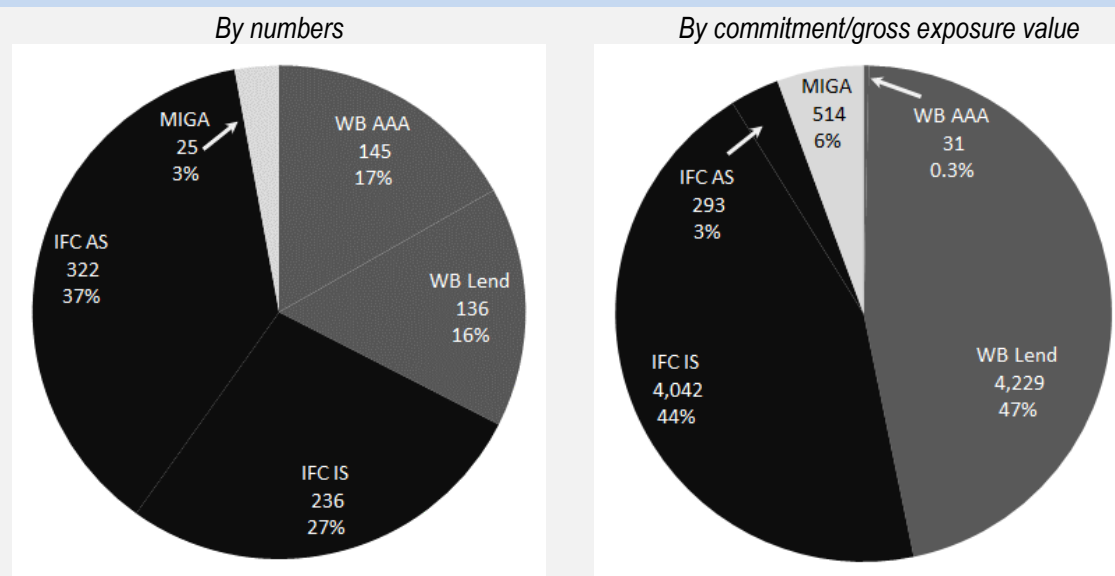
Institution	All projects	Financial inclusion portfolio	% financial inclusion
World Bank lending (IBRD/IDA)	2,275	136	6
World Bank AAA (ESW/TA)	7,152	145	2
IFC investments	2,024	236	12
IFC Advisory Services	1,611	322	21
MIGA guarantees	197	25	13
Total number of projects	13,259	885	7

Source: World Bank database.

Note: AAA = analytic and advisory activities; ESW = economic and sector work; IBRD = International Bank for Reconstruction and Development; IDA = International Development Association; TA = technical assistance.

Throughout the evaluation period, financial inclusion projects, as defined here,<sup>13</sup> accounted for approximately 3 percent of total World Bank Group commitments (Figure 1.5). Again, financial inclusion commitments represented the largest share of IFC's portfolio, with 7 percent of IFC total investment commitments; for MIGA, 4 percent of total gross exposure value issued; and for the World Bank, 2 percent of its total lending commitments. MIGA's financial inclusion gross exposure is driven by two master contracts with the German-based ProCredit Holding Group, through 19 guarantees in 16 projects, for a total of \$287 million, making up 2 percent of the institution's total gross exposure for the period.<sup>14</sup>

**Figure 1.5. World Bank Group Portfolio in Inclusive Finance, Relative Weight, FY07–13**



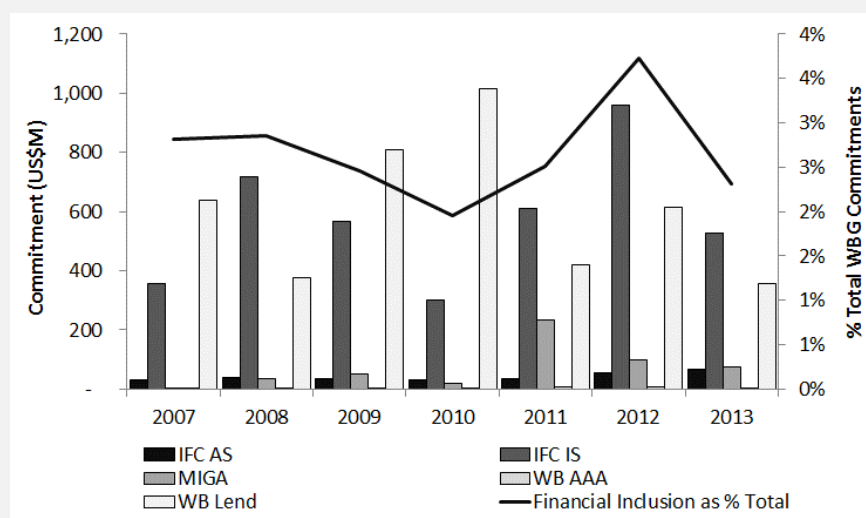
Sources: World Bank Group databases; IEG database.

Note: Volume or commitment for each of the institutions is as follows: World Bank lending = share of financial inclusion components to total International Bank for Reconstruction and Development + International Development Association + GRANT amounts identified using sector and thematic flags and their respective percentages; World Bank AAA = total cumulative cost delivered; IFC investment = total original commitments; IFC advisory = total funds managed by IFC; MIGA = gross exposure. AAA = analytic and advisory activities; AS = advisory services; WB = World Bank.

World Bank commitments to financial inclusion exhibited a marked increase during FY09 and FY10, likely in response to the global economic crisis. However, despite the fact that World Bank lending commitments for financial inclusion were the largest in absolute terms in 2010, their relative share in its portfolio was the lowest, accounting for almost 2 percent of total commitments. By contrast, IFC's investment portfolio in inclusive finance decreased in the aftermath of the crisis by 55 percent, from \$719 million in 2008 to \$321 million in 2010. This potentially reflects the limited opportunities for profitable private financial sector investment during this period.

Then in 2011, IFC commitments nearly doubled and grew by an additional 50 percent in 2012 as international financial markets stabilized, although the rest of the financial inclusion and overall portfolios decreased in terms of commitments (figure 1.6). More details on the World Bank Group's portfolio are presented in subsequent chapters.

**Figure 1.6. World Bank Group Portfolio Supporting Inclusive Finance, Trend FY07–13**



Sources: World Bank Group databases; IEG database.

Notes: AAA = analytic and advisory activities; AS = advisory services; FINC = financial inclusion portfolio; WB = World Bank.

## Is Financial Inclusion an Avenue Toward Prosperity for the Poor? A Literature Review

The factors preventing the poor from accessing financial services and how these services can help them escaping poverty have been extensively—but unevenly—studied. The last decades have seen a rapidly expanding literature that systematically tried to assess the impact of extending access to formal financial services among the poor. Some of these assessments have been undertaken in the

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form of randomized controlled trials, which allow for a proper construction of a counterfactual. In the following, the findings of a broad literature review are summarized,<sup>15</sup> covering systematic reviews, randomized controlled trials, and nonrandomized controlled trials studies from respected sources. Note that while the early literature focused mostly on credit, the more recent literature has expanded toward assessing the impact of increasing access to savings services, microinsurance services, and payment services.

#### CREDIT

The initial expectation of microcredit being able to pull millions out of poverty by providing them with credit has not been fulfilled. There is a consistent pattern of modestly positive, but not transformative, effects of microcredit on the poor. Evidence on the effects of microcredit has been mixed, and the results seem to depend very much on the characteristics and circumstances of borrowers and the purpose of the loans. There is some evidence of an impact on business creation, but this does not necessarily translate into higher consumption or income. Only a small share of business owners benefit through growth (Banerjee, Karlan, and Zinman 2015).

After all, credit might not be the most binding constraint of microentrepreneurs — and most of them never intend to grow. The literature offers a range of explanations why the impact of microcredit is so limited. First, microentrepreneurs might not be credit constrained (Banerjee 2013); or other constraints within the business environment might be more binding, such as bureaucratic “red tape” —for example, getting a license to operate—or simply access to physical infrastructure such as energy (Banerjee, Karlan, and Zinman 2015). Second, microenterprises’ capacity to grow might be limited. Initial returns, achieved through access to credit, might be high (de Mel and others 2008) but rapidly decreasing (Banerjee and Duflo 2007).

The root cause of this is the fact that many microenterprises are set up because of a lack of alternative employment options in the formal sector. There is evidence that such “subsistence entrepreneurs” make up most microenterprises.<sup>16</sup> This indicates that a large share of microenterprise owners may be running their business to make a living while they are looking for a wage job and may not have plans to expand their businesses (Emran, Morshed, and Stiglitz 2007).

A large part of borrowers use credit for consumption rather than investment purposes, as documented, for example, by Johnston and Morduch (2008). About 50 percent of loans given for business creation in rural Mongolia were actually used for household purposes (Attanasio and others 2015). This is in line with evidence

reported by Karlan and Zinman (2010) for the Philippines on diversion of entrepreneurial credit for household purposes.

Overindebtedness can bring substantial harm to the poor and to financial institutions. For the poor, overindebtedness can result in an unsustainable spiral of repayment, with consequent damage to investment in their microbusinesses or to household consumption and welfare. Households that become overindebted may have difficulty reintegrating into financial systems long after their immediate debt problem is resolved. For financial institutions, overindebtedness of clients is a threat to stability and sustainability, and can damage the reputation of service providers. The Andhra Pradesh microfinance crisis (addressed in chapter 4 in detail) shows the dangers of political overreaction when overindebtedness becomes a public concern. An appropriate regulatory and institutional framework, including consumer protection, industry code of conduct, and credit information, can help to avoid overindebtedness and encourage the development of sustainable financial services.

## SAVINGS

Studies assessing the impact of providing access to savings products are, on average, more positive than the impact studies on microcredit. Higher investment among female, though not male entrepreneurs that gain subsidized access to savings account have been documented in rural Kenya (Dupas and Robinson 2013a), for example. In general, literature on savings is not as abundant as for credit; hence, this more positive overall assessment of the impact of savings builds on less robust evidence.

However, the literature also shows the need for very specific products and techniques to overcome constraints of low-income households and microentrepreneurs. Generally people want rewards sooner rather than later. They have the tendency to increasingly choose a smaller-sooner reward over a larger-later reward, that is, they have so-called hyperbolic preferences. This makes saving difficult for most people—and in particular for the poor, who in addition face intrahousehold allocation decisions given the multitude of priorities they need to attend to. Commitment devices have proven to help overcoming these hyperbolic preferences. For example, people using a lockbox with a key increased preventive healthcare spending, whereas clients using the lockbox without a key did not (Dupas and Robinson 2013b). In addition, Malawian cash crop farmers using a commitment savings product increases investment and crop output by 21 percent, with an increase of 11 percent in consumption, while regular savings products have no such effect (Brune and others 2013).



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A systematic review confirmed the need for innovative design. Pande and others concluded that “innovative design of new savings products that increase the supply of savings and increase demand for savings by helping people address behavioral challenges were found to increase income at least in the short run” and can increase income by allowing households to accumulate assets (Pande and others 2012, 1).

#### **MICROINSURANCE AND PAYMENT SYSTEMS**

The evidence on microinsurance suggests positive effects on farmers and entrepreneurs, though limited take-up might limit the benefit of offering such services. Results were mixed from the introduction of weather insurance, for example, in India, where farmers shift toward more rain-sensitive crops that are riskier but also more profitable (Cole, Giné, and Vickery 2013). Index-based drought insurance products showed positive effects in rural Kenya; specifically, they show that insured households are on average 36 percentage points less likely to anticipate drawing down assets and 25 percentage points less likely to anticipate reducing meals on receipt of a payout (Janzen and Carter 2013).

For the poor, managing their risks may matter even more than providing liquidity. To gauge the relative importance of credit and risk constraints, in another study, farmers were randomly assigned to receive cash grants, grants of rainfall insurance, or opportunities to buy rainfall insurance. The authors find not only high demand for rainfall insurance but also larger effects of insurance take-up on agricultural investment than of the cash grants, implying that in this context, risk cost constraints are more binding than resource and liquidity constraints (Karlan and others 2013).

Initial results on the effects of payment systems are quite positive. They show that the use of more effective payment methods can not only reduce costs and connect more people to national and international payment systems, but also allow more effective interpersonal exchange and risk sharing across space and over time. However, research on the impact of expanding digital payment services is still in the early days, as this is a relatively recent product. Several research evaluations are currently ongoing, with results to be expected in the near future. One important aspect will be to gauge whether access to digital payment services increases individuals’ likelihood to participate in the formal economy and increases microenterprises’ investment and profitability.

Global remittances, a special form of payments to a recipient at a distance, typically by migrant workers, have been recognized as an important source of poverty reduction. The volume of official international remittances is estimated to exceed official aid flows by a factor of three (Ratha 2013). Remittances were found to reduce poverty in the developing world: a 10 percent increase in per capita official international

remittances is associated with a 3.5 percent decline in the share of people living in poverty (Adams and Page 2005).

Reducing high transaction costs of remitting money to labor-exporting countries has been suggested as a policy measure by a range of studies. High transaction costs resulting from lack of competition, regulation, or low levels of financial sector performance in labor-exporting countries act as a type of regressive tax on international migrants, who often tend to be poor and to remit small amounts of money with each remittance transaction. Lowering the transactions costs of remittances will help to increase the poverty-reducing impact of international remittances (Adams and Page 2005). A more recent summary of international research indicates that remittances not only improve income for many poor families, but also “are associated with greater human development outcomes across a number of areas such as health, education, and gender equality” (Ratha 2013, 1).

## **GENDER**

The gender dimension is critical to the discussion of financial inclusion, both in terms of access to financial services across males and females and in terms of female empowerment as an important outcome in itself. Females are, on average, less likely to have access to formal financial services than males. At the same time, a large share of self-employment in developing countries is among women and thus in greater need of access to formal financial services (Demirguc-Kunt, Klapper, and Singer 2013). Despite recent progress in financial inclusion rates in general, the gender gap has not narrowed: While the account penetration increased by 13 for both men and women between 2011 and 2014, the gender gap remains a steady 9 percent (Demirguc-Kunt and others 2015).

Beyond the lack of access to formal financial services by women, there are several other reasons why the microfinance movement has focused on women. It has often been argued that credit to female borrowers has more direct impact on household welfare than credit to male borrowers as they care more about children and family. However, there is a trade-off, as documented by Kevane and Wydick (2011); women of childbearing age face greater time constraints due to family commitments and are less likely to expand employment in their microenterprise with credit than male microentrepreneurs or older women.

Another reason is that women are often restricted from access to formal financial services due to intrahousehold restrictions, although this might also imply tailored solutions that protect women against having to share credit or savings within their household. Another supplier-focused argument is that female borrowers constitute less of a credit risk, as they are less mobile than men and often more conservative in

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their investment decision.<sup>17</sup> Women typically have higher repayment rates than men.<sup>18</sup>

There is some evidence on differential effects across gender in terms of microfinance interventions. On the one hand, interventions to increase savings are often more successful for women than for men. On the other hand, some interventions are less successful for women than for men, given intrahousehold and other constraints to women. This implies that such interventions have to take into account context-specific constraints faced by women to be successful.

Financial inclusion can also have a positive impact on female empowerment. However, the evidence reported so far has been rather mixed, which might have to do with products and services not being appropriate to address intrahousehold conflicts. Yoong and others (2012) conclude in their systematic review that there is no conclusive evidence for a positive impact of microcredit on female empowerment.

#### **IMPORTANT POLICY IMPLICATIONS FOR THE WORLD BANK GROUP**

Innovative delivery channels and tailored products can make outreach to low-income and rural population segments commercially viable. The take-up of these products, however, is often below expectations. Differentiating between various financial services is crucial. For credit, there seems no clear-cut case that access to credit has long-term and transformational benefits, at least on average. A large share of loans is for consumption and not entrepreneurial purposes – and, while there is nothing wrong with this, it has different repercussions for both expected micro and macro effects. However, there is some evidence that a certain share of the targeted microentrepreneurial population can benefit quite a lot. A small number of more growth-oriented entrepreneurs and enterprises will use access to finance to expand their businesses. There is thus a need for more tailored and context-specific approaches that takes into account other constraints.

In addition, there are arguments supporting a move up the firm ladder toward small enterprises. Small and medium-size enterprises might have more potential to be transformative and can create jobs. Different groups of borrowers have to be targeted with different techniques (group versus individual lending) and different products, and it is to be expected that different types of institutions will be targeting different sectors and segments of the enterprise population. For example, greater flexibility of loan terms is only consistent with individual and not necessarily with group loans.

Facilitating access to savings products on a broad scale seems more desirable and is important for the World Bank's product mix. It can also have important repercussions for entrepreneurial behavior. Where access to external finance is limited, internal finance becomes more important and constraints to the effective use of internal finance have to be addressed. It is important in this context to take into account behavioral and intrahousehold constraints. Offering formal financial services can help individuals (especially those with weaker decision power in the household, like females) to shift consumption patterns and even invest more in their microbusinesses. Given the World Bank Group's tools, the question arises how it can facilitate access to savings and foster innovative savings products – it is important to facilitate savings among the poor as the literature points out—particularly in the very low end of the retail market where local resources mobilization is likely to be costly; on top, transforming MFIs into deposit-taking institutions requires most sophisticated regulatory frameworks and oversight mechanisms.

The best way to start the entry of the poor into the formal financial system may be with payment services, for a variety of reasons. In many contexts it is also often the most immediate financial service needed by many low-income individuals and households. The importance of global remittances and their effect on a range of developmental outcomes exemplifies this point. In contrast, analysts have been struggling with the question of how to move *beyond* payments to other financial services – a question the World Bank Group also has to answer in light of its Universal Financial Access goal 2020. Current thinking is that payment accounts put the “plumbing in place” through which water can later flow, but a critical question is how to turn on the tap once the pipes are laid. Or is the World Bank Group satisfied with the benefits of only payment services?

There might also be important indirect and systemic effects from financial deepening and liberalization, in addition to direct benefits of access to financial services for the poor. If financial deepening reduces the cost of credit and improves allocation of scarce capital across the economy, this can have an impact on the structure of economy. Although there is no firm evidence that *direct* access to credit is necessarily welfare improving for its recipients, there is some evidence that financial deepening can reduce income inequality and poverty alleviation through indirect channels.

Financial deepening can also contribute to employment growth, especially in developing countries. Financial liberalization and the consequent increase in access-to-credit services can explain the fast gross domestic product per capita growth, rapid poverty reduction and initially increasing but then decreasing income inequality (Pagano and Pica 2011). Underlying these developments are occupational

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shifts from the subsistence sector into the intermediated sector and accompanying changes in wages.

Instead of providing microloans directly to microentrepreneurs in an effort to increase financial inclusion, financial deepening make the overall financial intermediate more effective. This in turn allows the private sector to grow and create jobs. Such salaried jobs are then likely to lift the poor out of poverty – and may ultimately also provide them with bank account. Financial deepening, rather than financial inclusion, has led to decreases in rural poverty, following financial liberalization in 1991 in India (Ayyagari, Beck, and Hoseini 2013). Financial deepening was also found to reduce poverty rates among the self-employed and also supported an interstate migration from rural areas into the tertiary sector in urban areas.

Therefore, microcredit is not necessarily the most important policy alternative to reap the benefits of financial sector reform for poverty alleviation. By changing the structure of the economy and allowing more entry into the labor market by previously unemployed or underemployed segments of the population, *financial deepening* (more efficient financial institutions and markets) helps reduce income inequality and poverty. By doing so, financial deepening can help achieve more inclusive growth and also help overcome spatial inequality in growth benefits.

It is thus important to understand that the effects of financial deepening on employment and poverty alleviation do not necessarily come through the “democratization of credit” but rather a more effective credit allocation. Given the World Bank Group’s Universal Financial Access goal 2020, *has financial inclusion been promoted to the detriment of traditional financial sector deepening, which tends to attract less public attention but may be equally or even more effective in lifting people out of poverty?*

For the poor to benefit directly from financial sector deepening and broadening, it is important to look beyond credit to other financial services that are needed by the poor, such as simple transaction or savings services. Although it should be a goal to achieve access to basic transaction and savings services for as large a share of the population as possible to thus enable them to participate in the modern market economy, the agenda for boosting access to credit should focus on improving the efficiency of this process, replacing access through political connection and wealth with access through competition. Unfortunately, the former kind of access is still too common in many developing countries. By channeling society’s resources to the most credit-worthy enterprises, the financial system can enhance inclusive growth.

There is also a case for looking beyond microfinance institutions to a broader set of financial institutions, including banks and nonbank MNOs. Technology has revolutionized the economics of retail banking, which suggests looking beyond traditional financial institutions to new delivery channels for financial services. As the type of service provided diversifies, tools to assess the level of financial inclusion (such as Findex) are factoring these trends in. To what extent a person having an account with a MNO that is not linked to a bank account is considered “financially included” is still up for debate.

Despite intensive research efforts in the recent two decades, there are still important knowledge gaps. Given the type of research methods applied and the focus of many studies, there is still a considerable area deserving more in-depth assessment, summarized in box 1.1. The gap map presented in box 1.2 discusses the focal areas of existing impact studies and systematic reviews: microcredit has thus far received most of the attention accordingly with many studies reporting on impacts on incomes, health, consumption, and education of the poor. That gap map also obvious makes where gaps in research exist; for example, saving has attracted a lot less research than credit. Payments are even less researched, only lagged by insurance where very few studies exist. Overall, this pattern is also reflected in the summary of the literature review commissioned for this evaluation.

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#### Box 1.1. Financial Inclusion Research Gap Map and Questions Going Forward

IEG’s review of all International Initiative for Impact Evaluation-listed impact evaluations and systematic reviews on financial inclusion indicates that microcredit is fairly well studied; savings more modestly studied; and payments, insurance, financial literacy, and consumer protection represent major gaps in rigorous understanding (see figure B1.1.1).

**The challenge on assessing the impact of financial inclusion will be to reconcile microinterventions and macroimpact.** The first macrolevel assessments of microfinance expansion have been undertaken. This “upward trend” in microfinance evaluation toward the macro mirrors a “downward trend” in the finance-growth literature toward the micro, which started out with aggregate regressions, toward country-level, industry level and ultimately firm-level studies, with identification strategies getting more refined. The micro- and macroliterature on finance and development have developed relatively separate, so bringing them closer together will be a challenge for the future. **Another important area is the role of governments.** Microfinance addresses very specific market failures; to what extent can we rely exclusively on nongovernmental organizations and donors to overcome them? There has been a trend toward the visible hand of government, that is, market-friendly interventions that try to address market failure without creating government failures due to rent seeking, distortions, and inefficiencies. Such

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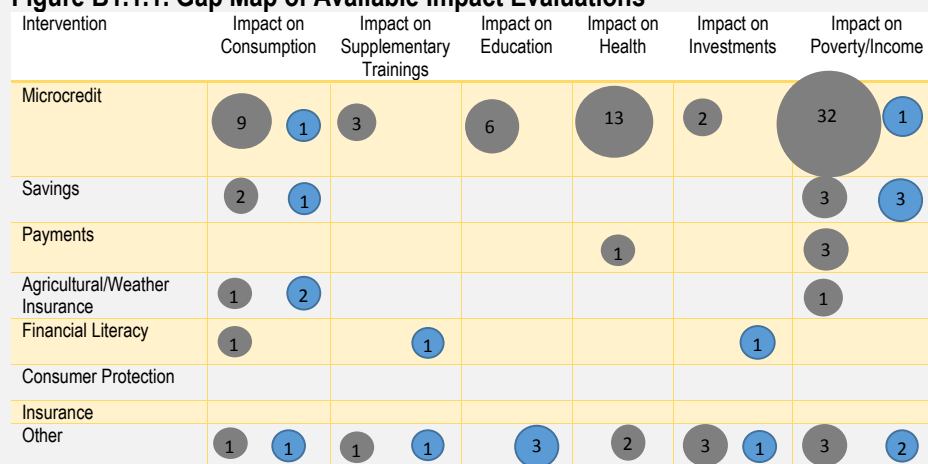
interventions include providing infrastructure platforms and covering fixed costs to overcome first mover and coordination problems.

**Intergenerational effects have not been assessed sufficiently.** Most studies — randomized controlled trials in particular — have a relatively short time horizon, typically of years. As the above-mentioned literature review shows, effects often do not relate directly to enterprise growth, but rather to (i) better education for children as access to financial services, including credit, allows for more educational options; (ii) mitigating risk as funds can be used to finance unforeseen events such as accidents or illnesses without the need to sell down assets; and (iii) access to health care. These benefits may only show up later than in year scope of most studies – likely an entire generation later.

**Studying the enablers that allowed some of the microenterprises to grow.** Credit was successful, albeit only for a minority of entrepreneurs. Generally only a fraction of microentrepreneurs grew and allowed their owners to move up the ladder of prosperity, eventually turning their business into small and medium-size enterprises and employing other people, potentially providing them salaried jobs otherwise not available. The circumstances under which microentrepreneurs tend to be more successful have yet not been studied in sufficient detail.

**Can the provision of activity-tied credit and insurance services hold back transformational changes** by tying households to their current activity? Is it better to provide activity-neutral services, including savings, payments, and consumer credit? This is also still an open question to be discussed.

**Figure B1.1.1. Gap Map of Available Impact Evaluations**



Sources: International Initiative for Impact Evaluation databases on impact evaluation and systematic reviews (<http://www.3ieimpact.org/en/evidence/impact-evaluations/>); Beck 2015; de la Torre, Gozzi, and Schmukler 2007.

Note: Gray circles are impact evaluations and blue circles are systematic reviews; numbers = existing studies.

## Global Industry Trends

One of the best available data sources for analyzing industry trends in financial inclusion is the Microfinance Information Exchange (MIX). MIX<sup>19</sup> receives periodic financial statements and various operational metrics voluntarily from a set of microfinance institutions in developing countries. Particularly in recent years, the quality of MIX data has steadily improved and now captures the vast majority of MFIs, including banks and nonbank MFIs, nongovernmental organizations (NGOs), credit unions and rural banks (Cull and others 2013). However, the use of MIX data comes with a caveat as it may underestimate the efforts of traditional formal banks that may not report to MIX, even though many do.

Other World Bank Group efforts on financial inclusion, for example on policy dialogue and technical assistance, are not centrally tracked and hence cannot be assessed in a comprehensive manner. It is, however, stressed at this point, that large efforts in financial inclusion have been under way in the area of thought leadership and creating commitment by several bodies in the international development arena (see box 1.2). In addition, a broad range of multilateral and bilateral agencies offers assistance on policy and legal issues as well as capacity building. A global overview of these activities, however, is difficult to obtain. The following paragraphs hence summarize an IEG analysis of global trends in microfinance, based on MIX data of the last 10 years.

The MFI industry is made up largely of NGOs and nonbank financial institutions. NGOs account for 31 percent and nonbank financial institutions for 29 percent of all MFIs, followed by credit unions and cooperatives with 17 percent and banks with 10 percent; rural banks account for a very small part. However, the importance of the respective forms of MFIs varies substantially across Region: Africa is unique in the dominance of cooperatives, whereas the East Asia and Pacific, Latin America and the Caribbean, Middle East and North Africa, and South Asia Regions all share a dominance of NGOs. Europe and Central Asia is the only Region where nonbank financial institutions dominate (all in terms of numbers).

The MFI industry grew both in terms of numbers—and even more dramatically in terms of assets. Although the number of MFIs appears to level off, assets grew almost exponentially (figure 1.7). A significant part of the increase in 2010 was due to Harbin Bank (China) entering the MIX data reporting with \$19 billion in assets, by far the largest reporting institution. This also explains the strong growth of MFI assets in the East Asia and Pacific Region in recent years.



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**Box 1.2. Financial Inclusion on the Global Development Agenda**

With the creation of the Consultative Group to Assist the Poor in 1995, the world got its first global partnership of leading organizations seeking to advance financial inclusion. In 1997 the first Global Microcredit Summit took place, and 2005 was the International year of Microfinance. As of 2008 the Alliance for Financial Inclusion, a network of financial policy makers, had aimed to increase access to appropriate financial services among the poor.

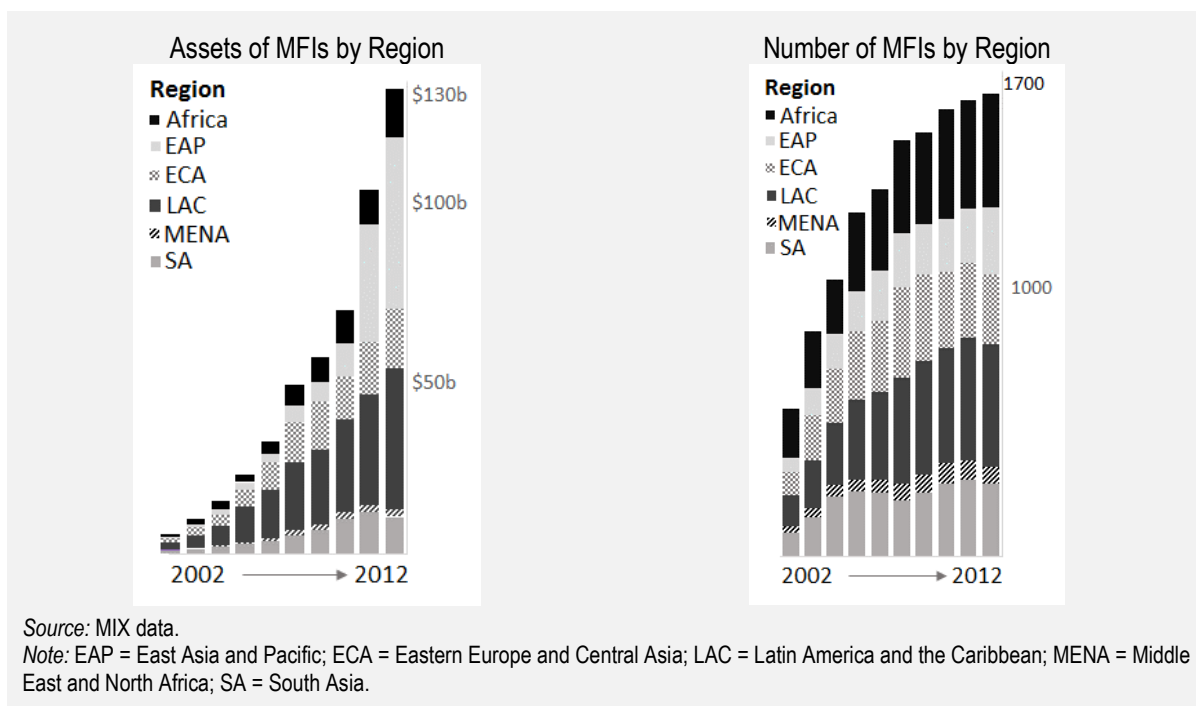
In 2011, the Alliance drafted the Maya Declaration – a measurable set of commitments by developing country governments to expand financial inclusion – which has now been signed by more than 80 countries. The G20 created the Global Partnership for Financial Inclusion in 2010, an inclusive platform for all G20 countries, interested non-G20 countries, and relevant stakeholders to carry forward work on financial inclusion. At their summit in St. Petersburg in September 2013, the G20 leaders endorsed the G20 Financial Inclusion Indicators developed by the Global Partnership for Financial Inclusion to track progress toward financial inclusion. The United Nations designated Queen Maxima of the Netherlands as Special Advocate for Inclusive Finance for Development.

*Source:* IEG staff.

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East Asia and Pacific, together with Latin America and the Caribbean, holds most MFI assets, whereas Africa and South Asia hold the fewest. At the institutional level, the size of assets per MFI reflects somewhat the overall asset distribution by Region, that is, East Asia and Pacific and Latin America and the Caribbean have the largest MFIs (most assets per institution), together with the Middle East and North Africa; Africa has the smallest MFIs. When looking at numbers of MFIs, however, the order is different. Although again Latin America and the Caribbean leads in terms of number of MFIs, it is followed this time by Africa with relatively many – but small – MFIs (figure 1.7), the majority of which are cooperatives.

Figure 1.7. Growth of Microfinance Industry



South Asia, despite having one of the smallest MFI industries, has by far the highest number of borrowers with the smallest average loan size. South Asia has roughly 50 million microcredit borrowers, with Latin America and the Caribbean the next largest at only 20 million and East Asia and Pacific with about 14 million. Most of these 50 million borrowers took out very small loans in South Asia, averaging about \$154, considerably smaller than in Latin America and the Caribbean with an average loan size of \$1,071 and even Europe and Central Asia, where loans are the largest at an average of \$1,862.

In general, there are more borrowers than savers accounted for globally: 96 million versus 79 million, respectively. This partly also reflects the fact that many of MFIs are non-deposit-taking institutions. It may also reflect the fact that deposit taking requires more sophisticated regulatory frameworks than the provision of credit. In addition, credit is a more lucrative business for MFIs and comes with a “built-in” commitment mechanism; that is, borrowers have to pay back. Given the challenge that people—and in particular poor people—face with regard to hyperbolic preference, credit may well have served as a commitment savings device, at an extra cost.

Globally, average loan size grew over time. The average loan size was \$192 in 2002; that grew to \$584 in 2011. This could be explained by a range of factors, including that many MFIs operate with “dynamic incentives,” offering small loan amounts

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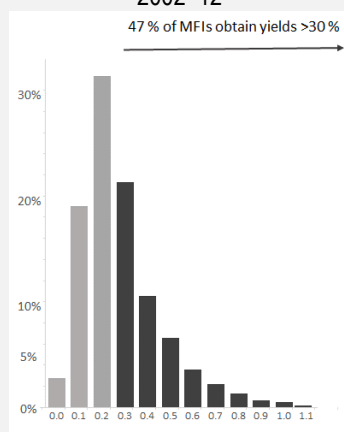
initially and allowing those amounts to grow once the borrower has proven credit worthy and paid back the initial loan. This leads to continuously rising average loan volume. It could also be seen as “mission creep,” where initially the MFIs industry catered (or tried to) to the poor, but with the increasing pressure on self-sustainability, had to grow its average loan size to remain profitable, leaving the poor behind.

Nominal yields, a good proxy for interest rates, exceed 30 percent per year for about half of the MFIs (47 percent). Yields from 20 to 30 percent are found with about a third of MFIs (31 percent) and yields of above 30 percent for about half of all MFIs (47 percent). Only a share of 21 percent had yields of 20 percent or lower (figure 1.8a). Real yields (adjusted for inflation) are distributed in a similar fashion, but by about 10 percent lower.

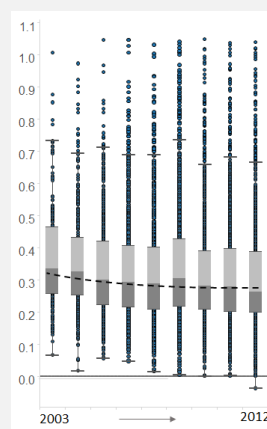
Over the time nominal yields decreased to some extent, from 33 percent to 26 percent (figure 1.8b). This can be attributed to a range of factors, including the global decline in inflation over time and the improved credit quality of the countries, but also the changes in the nature of operations of MFIs, which shifted over time to providing larger loans, as we have seen above. Given the fixed costs associated with origination and supervision, regardless of size, larger loans should provide lower yields and remain profitable.

**Figure 1.8. Microfinance Yields**

(a) Nominal yields of loans across MFIs  
2002–12



(b) Nominal loan yield over time



Source: MIX data.

These global trends form the backdrop against which World Bank Group interventions happened. The Bank Group operated during a time of dramatic growth of the MFI industry. Although the provision of credit dominated, access to

savings accounts has been on the rise. This is particularly promising, as savings tend to have higher welfare enhancing potential than credit. It will be interesting to see to what extent the World Bank Group fosters financial services beyond credit in its financial inclusion agenda.

Further, Bank Group support reaches MFIs markets that are dominated by NGOs, nonbank financial institutions, credit unions, and cooperatives. Not all these are obliged to operate on a self-sustaining manner, shedding particular emphasis on the World Bank Group's stance on "sustainability" in financial inclusion. How well has the World Bank Group balanced the trade-off between targeted and time-bound versus broad-based, open-ended subsidies?

For IFC, this may indicate that it is trying to open shop in countries that thus far were mainly served by NGOs—a challenge to IFC's model of self-sustaining MFIs. And finally, it will be interesting to see the effect of World Bank Group support to MFIs and its impact on average loan size and yields or interest rates, both proxies for reaching the poor and affordability for the poor.<sup>20</sup>

## Evaluation Design

This broad-based concept of financial inclusion together with the rationale for the World Bank Group's engagement forms the basis for this evaluation. In the context of this evaluation, financial inclusion refers therefore to the full range of services (payments, savings, credit, and insurance), to specific quality features of delivery (for example, stability and affordability), to inclusiveness (with special focus on the poor), and to choice (offer of service by a range of institutions). The World Bank Group supports financial inclusion through improvements of market mechanisms by overcoming limitations to demand and supply so more and better financial services are provided to the poor (see figure 1.3).

Figure 1.9 shows these two concepts together, reflecting the supply and demand issues described above and embedding them into the theory of change (or results chain) that this evaluation has used. It links the various World Bank Group interventions with outputs and intended outcomes (embodying the underlying theory of change connecting them). In summary, the World Bank Group deploys its instruments, including lending, investment services, guarantees, advisory services, technical assistance, and analytic work to put in place the enabling environment (see top box under "Outputs" in figure 1.9) for an inclusive finance agenda, as well as to support the operation of bank and nonbank institutions through advisory services, investments, and lines of credit (see bottom box under "Outputs" in figure 1.9).

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These outputs are reflections of the supply- and demand-side issues described above, that is, regulation, competition, financial literacy, and financial infrastructure, such as mobile payment systems. Jointly these outputs are anticipated to improve the way markets work—by shifting supply and demand—and provide financial services to the poor and micro and very small enterprises. Such improved service provisions should ultimately improve the livelihoods of poor people, directly or indirectly, through an array of channels including improved education, health or agriculture, and ultimately strengthen shared prosperity (final outcomes) both directly and due to the role of financial inclusion as an enabler of other development outcomes. All of this is supported by the World Bank Group’s role as convener and leader in financial inclusion, contributing to the knowledge agenda as well as joining policy makers in international forums.

This results chain is based on assumptions, including sufficient macro stability and government commitment and a minimum of institutional and human capacity paired with basic financial infrastructure. In cases where these are not given, the World Bank Group typically can address these either through complementary programs (for example to address macroeconomic and fiscal issues) or through components within financial inclusion projects (for example by building the needed institutional capacity for banking oversight or creating enhanced government commitment).

**Figure 1.9. Theory of Change for World Bank Group Financial Inclusion Interventions**



Source: IEG staff.

Note: L/C = line of credit.

## EVALUATION QUESTIONS

The overarching question that IEG seeks to answer in this evaluation is, Has the World Bank Group been relevant, effective, and efficient in creating better-functioning markets that provide improved access to and quality of financial services to the poor and microenterprises on a sustainable basis, globally and at the country level? This overarching question was addressed with a view to gaining an understanding how successful inclusive finance interventions can be replicated in different country contexts. For more details on the methodology, see appendix C.

- **Relevance.** Has the World Bank Group's support for inclusive finance been relevant to client countries and their poor populations' priority needs, conditions, and readiness for reform?
- **Effectiveness of policy reforms.** Has the World Bank Group been effective in its systemic interventions to create an enabling environment?
- **Effectiveness of direct support to MFIs.** Has the World Bank Group been effective in funding institutions that provide financial services to the poor and microenterprises, including funding through intermediaries or apex institutions? Has the World Bank Group been effective in advising these institutions in improving their performance?
- **Efficiency.** Are World Bank Group interventions in inclusive finance efficient instruments, from both a program and institutional perspective?
- **Work Quality and Coordination – Working as One World Bank Group.** Is the World Bank Group effectively managing factors within its control? Are the three World Bank Group institutions leveraging synergies through adequate coordination and sequencing of interventions?

## SCOPE

This evaluation covers World Bank Group inclusive finance interventions during the FY07–13 period. It covered IFC investments and advisory services; MIGA guarantees; and World Bank guarantees, lending, and nonlending (analytic and advisory activities, including nonlending technical assistance, economic and sector work, and reimbursable technical assistance). For analyzing trends in operations (in terms of volume, number of projects) and design features, this study focused on projects committed, approved, or issued during FY07–13. For the assessment of results, IEG focused on projects that *exited* during FY07–13. That includes projects that were “closed” (for World Bank) or that reached “operational maturity” (for IFC and MIGA) during FY07–13 and were subsequently evaluated (at the project level), hence including projects that were approved during FY07–13 and were already evaluated, but also projects that were approved *prior* to FY07, but evaluated during FY07–13.

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Most (70 percent) of the evaluated interventions are relatively young, that is, approved FY07–13. “Ongoing” projects—those approved FY07–13—that have not yet reached closure or operational maturity, were included to ensure relevance and timeliness of IEG’s conclusion and were analyzed for the purpose of answering questions of design, relevance, and general trends (and, of course, in the context of case studies, as part of the relevant program and context). In country case studies, ongoing projects were considered to assess whether the World Bank Group program addresses strategic priorities at the country level and is hence relevant.

Table 1.2 provides an overview of the World Bank Group projects and interventions covered. The activities of the World Bank’s Development Economics Department and of the Consultative Group to Assist the Poor (CGAP) were not specifically be evaluated, but the team was attuned to apparent gaps in knowledge, research, and advocacy evidenced in the course of the evaluation, and such gaps are pointed out as adequate throughout the report.

The focus of this evaluation is on payments, savings, credit, and insurance. Neighboring concepts of agriculture finance or risk mitigation for the poor through sovereign disaster risk policies were not be subjects of this evaluation, as they are either driven by different context factors, or only indirectly affect the poor, or are geared mainly toward the middle class. Credit to the rural poor, including those to farmers, is, however, covered in this evaluation. Note also that in the area of housing finance, most “affordable mortgage” activities are not oriented to the base of the pyramid or even the bottom 40 percent, so the relevant portfolio of “micromortgage” support is tiny.

**Table 1.2. Coverage of Evaluated Material: Inclusive Finance Projects Approved FY07–13**

<b>Institutions</b>	<b>Financial inclusion portfolio</b>	<b>Evaluated financial inclusion projects</b>	<b>percent with evaluation</b>
World Bank lending (IBRD/IDA)	213	99	45
World Bank AAA (ESW/TA)	142	0	0
IFC investments	274	65	21
IFC Advisory Services	339	91	24
MIGA guarantees	25	0	0
Total number of projects	993	235	24

Sources: World Bank data.

Note: An additional 108 projects evaluated between FY07 and FY13 were identified for the purpose of this evaluation though they were approved prior to FY07. AAA = analytic and advisory activities; ESW = economic and sector work; IDA = International Development Association; TA = technical assistance.

Broad-based macroeconomic or financial sector interventions that only indirectly affect the inclusive finance agenda do not fall within the scope of the evaluation. The success of financial inclusion interventions hinges on a wide variety of factors that

pertain to macroeconomic stability, banking, securities, and insurance market development in general, including the depth and breadth of these markets and factors of governance and transparency. These factors are important, but interventions targeting these other factors were not assessed per se. In addition, factors outside the financial sector may influence opportunities for the poor to make use of financial services to improve their well-being. The primary focus of this evaluation are interventions aimed at strengthening the enabling environment or the provision of financial services to the bottom 40 percent, through funding support, advisory work, or other means.

### **EVALUATION METHODOLOGY**

The methodology to answer the evaluation questions included (i) a review of policy and strategy documents at country and corporation levels; (ii) a portfolio review of World Bank Group projects and activities; and (iii) 15 country reviews, of which 10 were desk reviews based on portfolio data and Country Assistance Strategy Completion Report Reviews and 5 were purposively selected country case studies that included a field mission by IEG evaluation team members; and (iv) a comprehensive literature review.<sup>21</sup>

The approach was nonexperimental, combining qualitative and quantitative methods and drawing on external and internal research data, such as the World Bank's Enterprise Surveys, household survey data where financial inclusion variables have been included and the data of the Microfinance Information Exchange (MIX). Using the MIX data allowed IEG to better understand the practices and performance of microfinance institutions, as well as observe their response to the global financial crisis and longer-term trends over time. Results are presented throughout the report.

At the country level, the coherence of the solutions developed by the World Bank Group was covered through country reviews. IEG carried out these studies to identify drivers of success; assess nonlending and advisory work, including analytic and advisory activities that might have provided diagnostics of the country's financial sector and its inclusiveness or barriers to inclusiveness; and address issues of complementarity, sequencing, and synergies.

A key question as the World Bank Group moves to a new, more-integrated "solutions bank" model (recognizing that this level of integration was not the prevailing model during the evaluation period) is the extent to which critical constraints and opportunities were identified through regional, country-level, or subnational diagnostics, the extent to which activities were aligned to an identified country results framework and to the comparative advantage of respective World



## **CHAPTER 1**

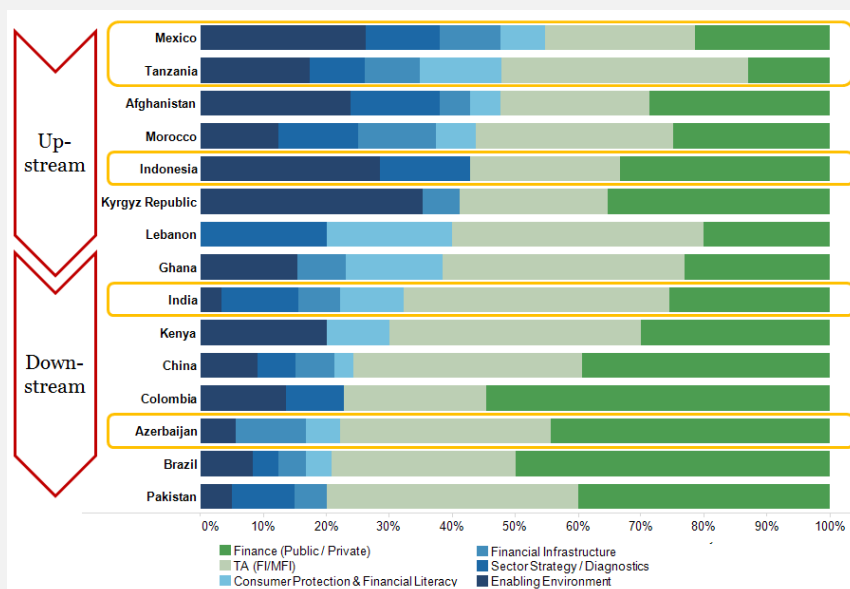
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Bank Group institutions, and the extent to which performance information was used for midcourse correction and learning. Country assistance strategies and Country Assistance Strategy Completion Report Reviews were thus used to assess the question whether the World Bank Group has mobilized the best solutions and personnel in combinations appropriate to country needs.

To this end, IEG conducted 15 desk-based reviews, of which 5 were developed into in-depth country case studies involving field missions which, among other things, allowed gathering information on effects to the beneficiaries. The selection of country cases was first be criteria-driven with subsequent purposive selection of field-based cases. For the selection criteria and method, see appendix C.

The multiple country case studies design allowed answering the evaluation questions for both the “common case” as well as the “critical case.” Credit-focused interventions dominate the entire Bank Group portfolio in financial inclusion. The selected 15 countries represent a cross-section of both credit-dominated portfolios (the common case) – for example, those of Morocco, Lebanon, and Brazil – as well as portfolios with a relatively high share of interventions that aimed at broadening the financial inclusion agenda to also cover payments, savings and insurance (the critical case) – for example, India, Indonesia, Mexico, or Tanzania. These two types of cases allowed investigating the requirements for broadening the financial inclusion agenda as well as success factors. Of these 15 countries, 5 were chosen for additional field studies, based on a purposive selection: Azerbaijan, India, Indonesia, Mexico, and Tanzania.

Figure 1.10. Focus of Bank Group Financial Inclusion Interventions in Selected Country Cases



Source: IEG portfolio analysis at time of selection.

Note: Boxed countries were selected for field-based cases.

The case study design also allowed testing hypotheses for policy-focused interventions and finance-focused interventions. These 15 countries provided an opportunity to learn from portfolios that focus more heavily on policy advice (“upstream” advice) as well as from those that provide mostly “downstream” support, that is, direct support in the form of technical assistance and finance through financial intermediaries. The five field-based case studies were distributed across this spectrum with a slight emphasis on high- to mid-upstream support and one case for which the support is mostly downstream. Such a grouping enabled to test hypotheses in parallel for upstream and downstream countries (Figure 1.10). Contribution analysis was used in field-based country cases to help identify the extent to which World Bank Group interventions actually contributed to the observed development results.

This report is structured to allow understanding the World Bank Group-wide engagement for financial inclusion. Instead of presenting findings in isolated chapters for each Bank Group entity, this report follows the logic of the financial inclusion model. First, for a financial inclusion intervention to be useful to a country, it must be relevant given the country’s development priorities. Hence, it starts with a discussion of the relevance of Bank Group support. Typically, a minimum of an enabling environment must be available for financial inclusion to materialize; hence the report then assesses the World Bank Group’s effectiveness in assisting countries to build up the right policy framework and enabling environment.

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This analysis looks across all institutions engaged in the World Bank Group “upstream” response – that is, in efforts aimed at policy and systemic institutional reform. The analysis revealed that the institutions active in this space are mainly World Bank and to some extent IFC Advisory Services. In chapter 4, the effectiveness of directly supporting MFIs is assessed. This typically involves World Bank lending, IFC advisory and investments. The support directed at MFIs – as opposed to creating the enabling environment for them to operate – is collectively referred to “downstream” support. For IFC investments and advisory services, such downstream interventions are their main activity field. Gender is an important dimension in financial inclusion and findings will be presented throughout the report (box 1.3).

#### Box 1.3. Gender in Financial Inclusion

Despite the current emphasis of microfinance institutions on women, gender differences are still strong when it comes to financial inclusion. Microfinance institutions have a tradition of prioritizing women in their lending portfolios because of early experience in the late 1980s indicating that women are more reliable in paying back than men. Today in Bangladesh, for example, among the two largest microcredit providers, about 97 percent of Grameen borrowers and 92 percent of BRAC (formerly Bangladesh Rural Advancement Committee) borrowers are female. Yet there is a persistent gender gap in the developing world, and even today, in 2015, the gender gap remains unchanged at 9 percent despite progress made overall.

According to the latest Findex data (from 2014), 58 percent of women and 65 percent of men worldwide have an account at a formal financial institution. Looking at only developing countries, the gender gap is wider: 59 percent for men and 50 percent for women. Among adults living below the \$2-a-day poverty line, women are 28 percent less likely than men to have a formal account. In certain Regions (South Asia and the Middle East and North Africa) the financial access gap is significantly higher for women, up to 40 percent.

Evidence from the literature also points to the consequences of relative financial exclusion, for example, women having to pay higher interest rates, being required to collateralize a higher share of their loan, and having shorter-term loans (Bardasi and others 2007). Women are being financially excluded for a wide array of reasons, including unequal legal rights (Almodovar-Retaguís, Kushnir, and Meiland 2013), restrictions on owning assets, and prominence of customary law over constitutional law which, especially in rural areas, predominantly favors men over women (Amin, Bin-Humam, and Iqbal 2013). At the same time, gender-targeted inclusion initiatives can have unintended consequences, which will also be considered.

*Sources:* Demirguc-Kunt and others 2015; Demirguc-Kunt, Klapper, and Singer 2013.

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<sup>1</sup> Based on Global Findex 2014 data as in Demirguc-Kunt and others 2015; 2011 World Bank Findex data; and IFC 2010.

<sup>2</sup> The president's statement especially emphasized electronic payments as an entrée to the financial system. "As early as 2020, such instruments as e-money accounts, along with debit cards and low-cost regular bank accounts, can significantly increase financial access for those who are now excluded." However, he also emphasized the importance of a range of services: "When low-income workers or poor families gain access to basic financial services, they gain a foothold on the first rung of the ladder toward prosperity. Access to savings accounts, credit or remittances can help families afford essential services like water, electricity, housing, education and health care. When firms gain access to financial services such as credit or insurance, they can reduce business risks, expand their firms and create more jobs" (World Bank 2013).

<sup>3</sup> Recognition was given to inclusive finance in milestone reports issued in 2013 by the United Nations Secretary-General and his High-Level Panel of Eminent Persons on the Post-2015 Development Agenda (Source: <http://www.unsgsa.org/priorities/key-initiatives/post-2015-development-agenda>).

<sup>4</sup> Consistent with IFC usage of this term, these include microenterprises of fewer than 5 employees and very small enterprises of fewer than 10 employees.

<sup>5</sup> At the country level, the Global Findex data show sharp disparities in the use of financial services between high-income and developing countries. The share of adults in high-income countries who are "banked" is more than twice that in developing countries. In low-income countries, formal account penetration stands at only 24 percent, compared with 89 percent in high-income countries. Looking more closely at the individual level, data also show significant variations. Wealthier adults tend to make greater use of formal financial services; in developing countries, adults in the highest 20 percent of income earners are more than twice as likely to have an account as those in the lowest 20 percent. Disparities in the use of financial services based on many of these parameters also exist in developed countries, but they are more pronounced in developing countries. In other words, if you live in a developing country, it matters more whether you are poor, have a low level of education, or live in a rural area.

<sup>6</sup> Insurance includes microinsurance. Payments include person-to-person, person-to-business, and government-to-person payments, including international remittances.

<sup>7</sup> It would provide little benefit (and potentially great cost), for example, to try to increase the numbers of those who hold an account with the formal sector if they do not use it. By contrast, focusing only or mainly on access may distort incentives. In this context, the term *formal* for IEG means established under and governed by law, whether or not the law is well-enforced.

<sup>8</sup> In some usage, financial inclusion also includes financial services for SMEs, a topic covered in an earlier IEG evaluation. This evaluation does not include support for SMEs in its scope.

<sup>9</sup> For the methodology used to identify the evaluative portfolio, see appendix A.

<sup>10</sup> Although, this would depend on the interaction of supply and demand.

<sup>11</sup> That is, costs that are independent of the amount of deposit or credit, the number of transactions of a client, or the number of clients served in a branch or by an institution.

<sup>12</sup> An additional 108 financial inclusion projects evaluated between FY07-13 were identified, but these were approved prior to 2007 and are thus not included in table 2 (8 IFC Advisory Services, 32 IFC Investment Services, and 68 World Bank lending). However, they will be included in the evaluated portfolio. The difference in coverage between the committed and evaluated portfolios is clearly represented in the evaluation.

<sup>13</sup> But not including SMEs.

<sup>14</sup> For these master contracts, its subprojects were recorded as a single project for each host country except for Ukraine, Georgia, and Serbia, where each host country had more than one guarantee and thus the collection of guarantees for a host country counted as one project.

<sup>15</sup> Commissioned by IEG and conducted by Professor Thorsten Beck (Beck 2015).

<sup>16</sup> For example, Hsie and Klenow (2009) show that 90 percent of all enterprises in India never grow. de Mel, McKenzie, and Woodruff (2010) show that only 30 percent of microenterprise owners in Sri Lanka have characteristics of large firm owners, whereas 70 percent are similar to wage workers.

<sup>17</sup> For a more in-depth discussion, see Aghion de Armendariz and Morduch 2007.

<sup>18</sup> See for example Beck, Behr, and Güttler (2013) who present evidence from two MFIs in Albania and Bolivia that lend to both men and women.

<sup>19</sup> Formally incorporated in 2002, the Microfinance Information Exchange (MIX) is a nonprofit organization that facilitates collection and exchange of public data designed for microfinance practitioners. MIX receives periodic financial statements and various operational metrics voluntarily from a set of MFIs in developing countries. MIX has been accumulating these annual (and in some cases quarterly) data since at least 1995, providing an important source of information on the size, nature, and performance of the microfinance sector. By 2011, some 1,650 MFIs were reporting data to MIX (compared with 3 in 1995). Typically there is a considerable reporting lag (of up to three years), especially with smaller institutions. Using the MIX data as a key data source for the evaluation helped IEG better understand the practices and performance of MFIs, as well as observe their response to the global financial crisis and longer-term trends over time. It was also a major source in analyzing the strategic relevance of World Bank Group resources allocation, as MIX data provide a sense of the size of the microcredit market in a given country (see chapter 2).

<sup>20</sup> Generally the literature takes the average loan size as a proxy for the extent to which microfinance services reach the poor, that is, assuming the smaller the volumes of, for example, credit the higher the likelihood that such credit reaches the poor.

<sup>21</sup> Commissioned for this study and conducted by Professor Thorsten Beck, Professor of Banking and Finance at Cass Business School in London.

## 2. Relevance of World Bank Group Support

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### Highlights

- ❖ World Bank Group support to financial inclusion grew by 20 percent over the last six years, barely keeping pace with the growth of the microfinance institution (MFI) industry, which grew by 80 percent. Still, the fact that International Finance Corporation (IFC) supports MFIs that jointly issue 39 percent of the global microloan volume underscores IFC's leadership role.
  - ❖ Despite the growth and relative reach of the World Bank Group, its support to financial inclusion is small given the large number of unbanked and the microcredit gap. This requires a strategic allocation of resources, shifting the World Bank Group's scarce resources to where they are needed the most and where they have the highest impact.
  - ❖ The World Bank Group's allocation of its resources devoted to advancing financial inclusion is strategically aligned with countries' needs; that is, they primarily reach countries with low inclusion rates where markets actually reach the poor. This is particularly true for World Bank lending, IFC advisory, and analytic and advisory activities.
  - ❖ IFC's investments also reach countries with very low inclusion rates—which is remarkable, as these markets are often served by MFIs that rely on subsidies. At the country level, World Bank Group support for financial inclusion was relevant in as much as it addressed a clear development priority.
  - ❖ The most common constraint that Bank Group strategies addressed is lack of capacity and financing of financial institutions along with financial infrastructure (credit reporting) and regulations. Consumer protection and financial literacy were, however, almost never addressed, despite their importance for the poor.
  - ❖ The focus of the World Bank Group's inclusive finance support has been on credit and gradually embraced other services—a promising trend given their importance for the poor.
- 

This chapter analyzes the extent to which the World Bank Group's support for financial inclusion has been relevant in the context of its strategic framework and country-level priorities. The intervention logic for World Bank Group support of financial inclusion builds on their potential to address market or government failure, hence allowing an increase in the supply and demand of financial services to low-income households and microenterprises at a lower, or at least affordable, cost and adequate quality. However, local circumstances vary. Geographic dimensions, population density, the extent of "social cohesion," the progress of banking sector reform and the adequateness of its supervision system—to mention just a few factors—may vary across countries. In other words, each country faces particular constraints and developmental challenges requiring a tailor-made financial inclusion agenda and Bank Group support strategy.

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This chapter presents evidence on (i) how financial inclusion fits into the overall strategic framework of the World Bank Group; (ii) the extent to which the World Bank Group interventions matter given the overall magnitude of the issue; (iii) how strategically the World Bank Group deployed its resources; and (iii) how the World Bank Group addressed development priorities in client countries and identified and constraints to the countries' financial inclusion agenda.

### World Bank Group Strategy and Its Universal Financial Access Goal 2020

The World Bank Group's 2007 Financial Sector Strategy set out an agenda and defined a business model for the World Bank Group to engage in financial inclusion. The strategy noted that the development mission of the World Bank Group "leads it to focus on market and institutional infrastructure" – the legal basis, market standards, and systems (including payments). Access to finance "for the underserved" is one of two areas of "special attention through well-defined initiatives." The Consultative Group to Assist the Poor (CGAP) is identified as leading on microfinance, focusing on "sound policies and best practices" with "an increasing emphasis on the regulatory and market development implications of the use of modern technologies (e-banking, phone-banking)." The strategy makes note of the need to use more systematic diagnostics, including Financial Sector Assessment Programs, the Report on the Observance of Standards and Codes, and International Finance Corporation (IFC) microdiagnostics. The plan was to do a Financial Sector Assessment Program stock taking and to develop a set of "consistent diagnostic-based indicators" (World Bank 2007, viii, ix, xi).

The new 2013 Bank Group strategy lays out a role for World Bank Group in financial inclusion. It mentions the priority of access to finance in poor and fragile and conflict-affected (FCS) countries and states that "new products are also likely to emerge to meet the needs of the 2.5 billion people who still do not have access to formal financial services" (World Bank 2013, 9). It recognizes the central role of the private sector in job creation as a means of poverty alleviation. Microenterprises are mentioned only in a box on IFC, noting that IFC's sector focus has shifted to increase the program share of micro, small, and medium-size enterprises (MSMEs). However, financial inclusion is not explicitly mentioned.

In addition, IFC has strongly emphasized financial inclusion (which for it includes SMEs) and microfinance. For example, the *IFC Road Map FY13–15* lists the following as one of five strategic focus areas: "Developing local financial markets through institution-building, the use of innovative financial products and mobilization, focusing on micro, small and medium enterprises." IFC's development goal 3a is to

“increase access to financial services for micro/individual clients.” In declaring its goals, the document emphasizes IFC’s “strong focus” on MSMEs and its continuing to “lead innovation in microfinance” including in technology, products, and policy “to help [financial intermediaries] reach a greater number of people in a more cost-effective way by effectively combining [Investment Services] and [Advisory Services]” (IFC 2012, 2, 16, 20).

In the 2013–15 road map, IFC replaced its development goal of “helping MSMEs increase their revenues” (an outcome or even an impact) and focused on an existing development goal to “increase access to financial services for SMEs clients and micro/individual clients.” A major reason was its difficulty in measuring MSME revenues. IFC plans to continue to increase financial inclusion within the context of the World Bank Group approach to responsible financial inclusion through a range of investment, advisory, and treasury activities, a leading role in the G20 Global Partnership for Financial Inclusion, and leveraging its client network for financial inclusion. IFC’s advice and investment in this area often go hand in hand. The strategy of the Multilateral Investment Guarantee Agency (MIGA) does not enunciate any goals regarding financial inclusion or microfinance, although some of its guarantees have facilitated institutions that provide microfinance among their services.

To accelerate and increase effectiveness of reforms and country-led actions on financial inclusion, the World Bank Group launched the Financial Inclusion Support Framework (FISF) in April 2013. At least 50 countries have set financial inclusion targets and/or made commitments to improve financial inclusion, although far fewer countries have a fully developed FISFs yet. This framework is intended to support these countries both in creating the needed enabling environment through policy and regulatory reforms and in building financial infrastructure development, as well as through measures aimed at funding the expansion of financial services by catalyzing private sector finance, know-how and innovation. Country selection for Bank Group engagement is accordingly based on country commitment, dedicated capacity, and the availability of a lead counterpart and the potential for impact.

Finally, World Bank President Kim lifted financial inclusion to the highest strategic relevance in October 2013 by declaring the World Bank Group’s commitment to achieving universal access to financial services by 2020. The emphasis of this commitment appears to be on extending access to low-income workers and poor families. For details on how the World Bank Group plans to achieve the 2020 goal, see Box 2.1.

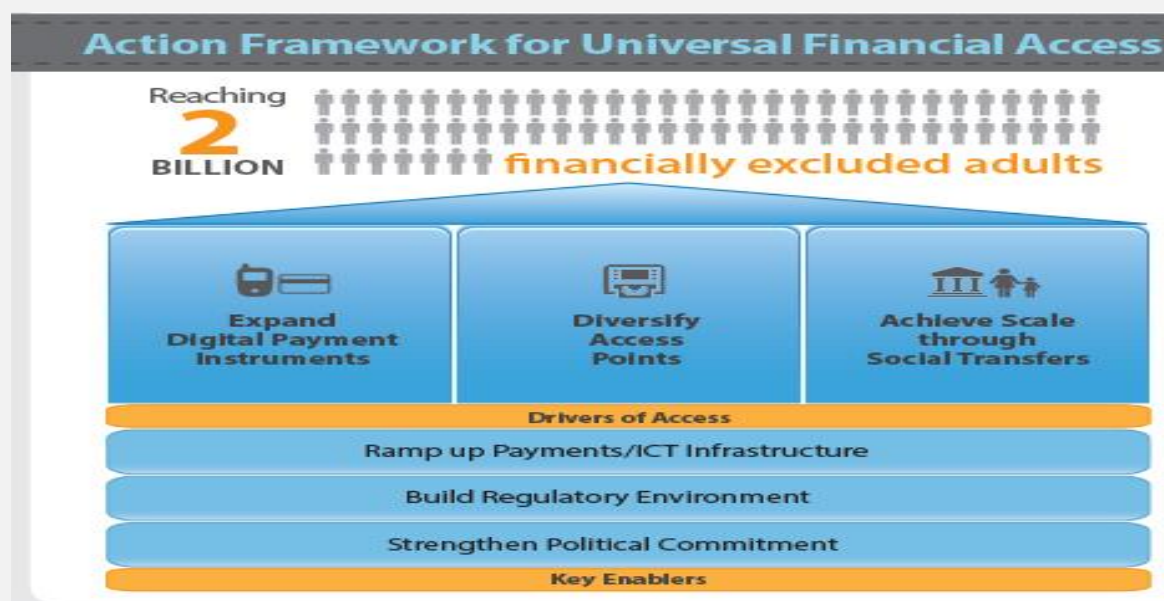


### Box 2.1. World Bank Group's Universal Financial Access Goal is Directly Relevant to Its Financial Inclusion Agenda

Consistent with President Kim's commitment to Universal Financial Access by 2020, the World Bank Group's approach centers on financial access through transaction accounts. These include not only bank-held accounts but also e-money accounts held with banks or other authorized and/or regulated service providers including nonbanks, which can be used to make and receive payments, and to store value. Beyond providing access by introducing these transaction accounts, the World Bank Group focuses on expanding access points, and driving scale and viability through high-volume government programs, such as social transfers, into those transaction accounts. Transaction or deposit accounts are seen by the World Bank Group as the stepping-stone to full financial inclusion, providing a pathway to a broader range of financial services. Advisory services and analytical work is currently being programmed to monitor the transition from access to usage and more broad-based inclusion in client countries.

The Bank Group is focusing its efforts – with development and private sector partners – on 25 countries where 73 percent of all financially excluded people live. India and China have the largest share of unbanked people. Together they account for some 32 percent of them. The rest of the top priority countries include: Arab Republic of Egypt, Bangladesh, Brazil, Colombia, Democratic Republic of Congo, Ethiopia, Indonesia, Kenya, Mexico, Morocco, Mozambique, Myanmar, Nigeria, Pakistan, Peru, Philippines, Rwanda, South Africa, Tanzania, Turkey, Vietnam, Republic of Yemen, and Zambia. The Bank Group is working with these countries to strengthen the key building blocks needed to achieve the access goal, including political and stakeholder commitment, enabling legal and regulatory environment, and bolstering payment systems and information and communication technology infrastructure.

Figure B2.1.1. World Bank Group Action Framework for Universal Financial Access



Source: World Bank 2016.

The Bank Group's public commitment to a specific measurable goal contributed to sustaining and expanding international dialogue to reach consensus and advance the financial inclusion agenda. President Kim's public commitment to universal financial access helped motivate a high level and visible policy dialogue, including with other United Nations agencies, foundations, multilateral development banks, dignitaries, and experts. As a spin-off, these forums triggered further declarations and commitments; for example, by national governments to meet their financial inclusion targets and by foundations, banks, policy makers and financial inclusion alliances to contribute to the global agenda, as was the case at the 2015 World Bank Group/International Monetary Fund Spring Meetings.<sup>1</sup> This is further supported by the World Bank Group's convening power and engagements in partnership and standard-setting bodies, discussed in greater detail in chapter 3.

Despite the World Bank Group's public commitment to the Universal Financial Access goal 2020, there appears to be little guidance on how to operationalize this goal for Bank Group staff. Although the above-mentioned FISH delineates some principles of actions and key building blocks of World Bank Group support, it remains to be seen how this goal will be translated into practice. Such guidance may also define the relative emphasis placed on access to a *range* of financial services and *usage* thereof, that is, actual financial inclusion versus access to basic transaction services, such as receiving government payments electronically.

A focus of "driving up access numbers" runs the risk of ignoring that there is yet limited evidence that demonstrates that the provision of access to financial services leads necessarily to financial inclusion of the poor. Conceptually, the link between access and inclusion (active use) of financial services is clear, but empirically, nonutilization rates in some schemes raise questions. A lot depends on the quality, design and utility of this initial access.

Studies reveal the pros and cons of policy options that are aimed at providing the poor with access to financial services in a fast manner. For example, the promotion of access through government-supported programs to digitalize cash payments via mobile phones or no-frill accounts for a large share of the population may not necessarily lead to inclusion. In Niger, cash transfer via the mobile phone proved that such payment systems could be low-cost ways to deliver cash transfers. Moreover, households receiving mobile transfers had higher diet diversity and children consumed more meals per day, attributed to increased time saving as well as increased intrahousehold bargaining power for women (Aker and others 2013).

However, a later study by the same authors cautions that "[although] these results are promising, they suggest that electronic transfers may not lead to improved

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financial inclusion for all households or in all contexts, as proponents might suggest. Unlike the mobile money ‘revolution’ in Kenya, mobile money registration and usage has not grown substantially in other parts of Sub-Saharan Africa, including Niger” (Aker and others 2014, 29). Another example that is frequently quoted in this context is M-PESA in Kenya. Jack and Suri (2014) found that M-PESA users weathered shocks better than those not using that technology. Despite this encouraging findings, the M-PESA model stands out in as much as the mobile network operator, Safaricom, had a quasi-monopolistic coverage of Kenya and agents were contracted based on exclusivity agreements, that is, they were not allowed to disperse cash for potentially competing service providers. The replicability of M-PESA to date has proved limited.

India, with its massive rollout of the Pradhan Mantri Jan-Dhan Yojana scheme, offers additional cautions—the World Bank finds that 72 percent of accounts opened under the scheme have zero balances (implying dormancy). On a broader basis, the latest Findex data point equally at low usage of accounts, despite strong growth in access to them. Globally, 460 million people have dormant accounts; that is, they have not made a single transaction during the last year (Demirguc-Kunt and others 2015). Dormancy and low usage are particularly strong in low-income and lower-middle-income countries and indicate that “there are millions of accounts, including new ones, that are essentially dormant, and many more that are used for one or a narrow range of purposes” (Kelly and Rhyne 2015, 19). All of these cases exemplify that the link between access and inclusion cannot be assumed—it rather relies on the quality, design, and utility of the initial access and a set of assumptions.

Already the historic approach of trying to lift the poor out of poverty through microcredit built on a set of assumptions—but these proved overly optimistic. The first “wave” of financial inclusion provided the poor with credit, assuming they would invest these funds in productive assets, eventually lifting them out of poverty. However, this model did not work as intended for most. As the preceding literature review showed, the key assumptions that were thought to make this model work, did not materialize. This could be attributed to several explanations, for example, that access to finance was not the binding constraint to start with, or loan recipients did not invest in productive assets but used this funds to smooth consumption and manage their day-to-day finances, or recipients lacked the entrepreneurial skills required. Only a small fraction of recipients were able to develop their microenterprises and thus escape poverty.

One could argue that the international development community, including the World Bank Group, has learned from the experience with microcredit and has turned now to payment systems and savings. However, also the approach of

enabling access of the poor to financial services through digital payment systems also relies on a set of assumptions. These assumptions include (i) sufficient mobile phone network coverage, and if not present, the availability of funds to conduct the needed up-front investment; (ii) the availability of agents to allow users to cash-in and -out because in their local economies cash still prevails; (iii) the required literacy to use mobile phones and associated accounts; and/or (iv) the needs of the poor to use the devices beyond the initial government-mandated cash transfers. As Aker and others put it in the context of their analysis of cashless transfers in Niger:

“This suggests that substantial investment to register clients and agents would be required to establish mobile payment systems. In addition, while program recipient households in our study used mobile money to receive their transfer, they did not use it to receive remittances or to save, two important aspects of financial inclusion. This is potentially related to the limited m-money agent network in the country, a common issue in other West African countries. Like many field experiments, the generalizability of our results may be limited” (Aker and others 2014, 29).

Equally, an approach of digitalizing person-to-person and government-to-person payments or mass rollouts of no-frill accounts relies on a set of assumptions, similar to those above: (i) the availability of these systems, (ii) customer-centric design of these accounts so they are being used beyond the initial transaction they were set up for and—most important—sustainability. Although in some cases digitalizing payments may be self-financing due to efficiency increases and savings from reduced leakage of funds, sustainability needs to be examined carefully.

Even assuming access does lead to inclusion, the question remains to what extent the poor actually benefit. The conclusion of the above presented Independent Evaluation Group (IEG)-commissioned literature review is that microcredit was not transformational in lifting people out of poverty; yet payments, savings and insurance tend to have a higher potential to help the poor manage their day-to-day finance. To some extent these latter services can also lead to investments in education and health care and to business expansion. At least they provide choices that poor people did not have before.<sup>2</sup> The rather limited evidence on benefits points to the importance of continuous monitoring and evaluation of World Bank Group interventions in financial inclusion to ensure support activities actually benefit the poor—an issue that chapter 4 will analyze in greater depth.

The current World Bank Group’s strategy of focusing on 25 priority countries may have to be adjusted going forward, as the remaining population of excluded will increasingly be broadly distributed among many countries. The World Bank Group’s plan implies a focus on 25 “priority countries,” based on the rationale that

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about 73 percent of the unbanked live in these countries. Concentrating on these countries may result in efficient resource allocation as a large number of unbanked potentially benefit through a limited number of interventions in a few countries; however, it is likely not only to pose questions of equity, but also leaves unaddressed the excluded in other countries.

Although China and India may continue to show substantial progress in including people, the still-excluded will come from many countries in all Regions. “It will hence be important that support for efforts to advance inclusion engage with smaller countries that are not in the spotlight,” Kelly and Rhyne (2015, 15) conclude. In addition, as initiatives reach the more proximate populations, many of the remaining excluded poor will live in rural areas, requiring further adaptation of the approach.

Last, the question remains as to whether the Universal Financial Access goal is achievable by 2020 at all. Recent extrapolations from current trends concluded that by 2020 just over one billion people will be unbanked, taking population growth into consideration (Kelly and Rhyne 2015). Will the World Bank Group’s support boost access to such an extent that these 1 billion will still be reached? Have the “low-hanging fruits already been harvested” as large countries have implemented government-mandated mass rolls outs? Will it there be more costly to reach this “last billion” of unbanked?

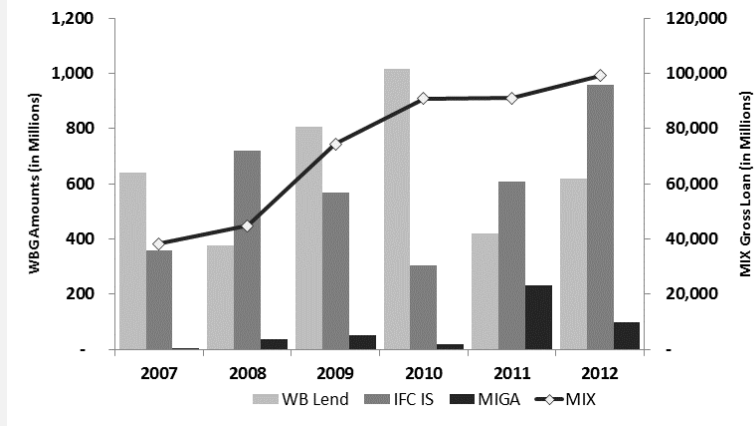
Summing up, the current Bank Group strategy raises a set of questions. It is important going forward to provide a minimum of guidance in setting out the envisaged future state of financial inclusion; the expected benefits for the poor based on evidence; the focal areas of engagement—in particular guidance to find the right balance between focusing on “headline numbers” by pushing for access versus enabling inclusion; and a road map describing how the actual Universal Financial Access goal would be achieved, given the World Bank Group experience in scaling up the relevant approaches. The World Bank Group’s leadership will be important, given that financial inclusion is high on the global development agenda.

### **Given the Magnitude of the Financial Inclusion Gap, Does the Role of the World Bank Group Matter?**

The microfinance industry grew rapidly—and with it World Bank Group support. The microfinance institution (MFI) industry grew significantly in terms of numbers of players and—associated with this—the issuance of loan volume over the last six years (figure 2.1). Based on Microfinance Information Exchange (MIX) data, there were a total of 1,650 MFIs in 2012. This was well above the original three that reported in 1995 and significantly more

than the 526 reporting in 2007, the start of the evaluation period. In terms of volume, the gross issuance of loans by MIX-reporting MFIs increased by 80 percent, from a three-year average during fiscal years (FY)07–09 of \$52 billion to \$94 billion during FY10–12. Bank Group support grew as well, albeit only by 20 percent, from \$1.19 billion to \$1.42 billion.

**Figure 2.1. The Parallel Growth of the Microfinance Industry and World Bank Group Support to Financial Inclusion**

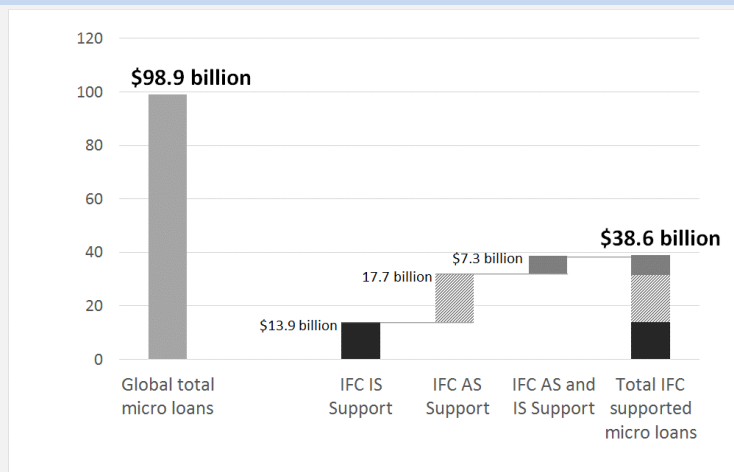


Source: MIX data.

IFC was able to support a significant portion of the MFI industry with its investments and advisory services. IFC supports MFIs through investments in the form of debt or equity, through advisory services to advise, for example, on risk management, market segmentation, upscaling or downscaling, and so forth, or through a combination of both. IFC's investments support MFIs that jointly issue \$13.9 billion of microloans; in addition, IFC advisory supports MFIs that jointly issue an additional \$17.7 billion and the combination of both (IFC investment and advisory) supports MFIs responsible for an additional \$7.3 billion. In total, IFC-supported MFIs issued about \$38.6 billion of microloan, or about 39 percent of the MFI industry (figure 2.2). This is a considerable "reach," demonstrating a clear leadership role of IFC, jointly with the German KfW Bank Group, in funding and advising MFIs.

An important note on attribution though: supporting an MFI through an investment or advice may not necessarily indicate that IFC was responsible for the entire loan volume (or even the major share of the loan volume) that this MFI subsequently issues possible. Hence, the \$38.6 billion are not due to IFC's interventions, but IFC played a role in the institutions that issued them.

Figure 2.2. Microloans Globally versus Microloans Issued by IFC-Supported MFIs

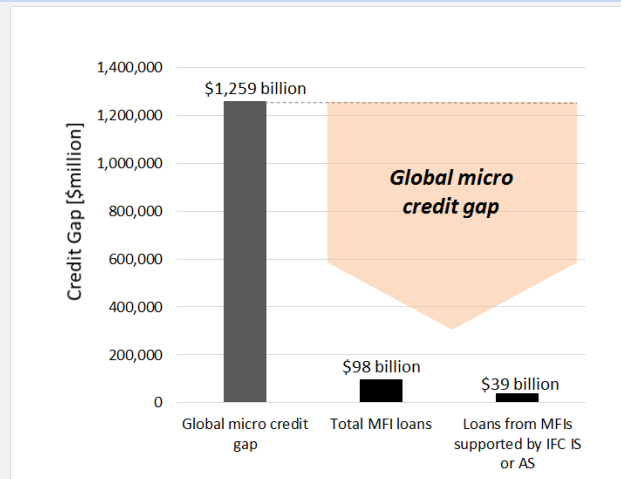


Sources: MIX data.

Despite the growth of Bank Group support to financial inclusion and IFC's reach of MFIs, the World Bank Group support is dwarfed by the magnitude of the yet-to-be accomplished agenda. Globally, as of 2011, 2.5 billion people were unbanked of which the World Bank Group is likely to have reached about 1–2 percent directly. Most of the 2.5 billion unbanked live in developing countries amounting for about 59 percent of adults. Of these, the World Bank Group's IFC has reached about 25 million through deposit accounts and about 23 million through microloans, issued by MFIs that IFC supported.

Despite this growth, the entire MFI industry still only reaches about 20 percent of its potential market among the 2.5 billion unbanked and is meeting only 8 percent of the IFC-estimated \$1.3 trillion microloan credit gap. Collectively, all MIX-reporting MFIs reach about 72 million of clients—a tiny fraction compared with 2.5 billion of unbanked. Collectively, these MFIs issue a gross loan volume of \$98 billion<sup>3</sup>—again a small fraction of the actual credit gap: IFC and McKinsey estimated the global credit gap for microenterprises to amount to \$1,259 billion.<sup>4</sup> Of the total loan amount issued, the share of microloans that was issued by IFC-supported MFIs amount to \$38.6 billion or 8 percent (figure 2.3). In a similar vein, the global MFI industry is estimated at about \$600 billion, of which IFC accounts for about \$3 billion of cumulative investments and \$1.45 billion in currently outstanding commitments. Hence, despite the fact the World Bank Group support grew in line with the MFI industry, it appears rather small overall.

**Figure 2.3. Global Microcredit Gap versus Microloan Industry versus IFC-Supported Microloans**



Source: IFC 2012.

Note: AS = Advisory Services; IS = Investment Services.

In summary, the volume of Bank Group support is small given the large number of unbanked and the demand for microfinance – calling for a selective and strategic engagement. Regardless of which measure one takes, Bank Group support appears small compared with the industry size, even though? IFC is among the top lenders in this sector.<sup>5</sup> Bank Group support appears even smaller when compared to the demand, that is, the number of unbanked and the microcredit gap. This indicates that Bank Group support cannot fix the problem through its volume (and it may not even be desirable), but rather by establishing the foundation for better-functioning markets, creating new MFI markets (for example, through greenfield operations) or expanding them. This requires a strategic allocation of resources, shifting its scarce resources where they are needed the most and where they can be expected to have the highest impact either in terms of creating new markets or scaling up existing markets.

But World Bank Group support extends beyond funding of MFIs. The Bank Group is active “upstream,” that is, in creating an enabling environments for financial inclusion. A full 30 percent of Bank Group activities aim to create the enabling environment for financial inclusion by assisting countries in diagnosing financial inclusion constraints and developing national financial inclusion strategies and policies (12 percent), adequate legislation and regulation (14 percent) and the needed financial infrastructure (10 percent), such as payment systems and credit registers or bureaus. Such activities are typically supported by either the World Bank and, to a limited extent, also by IFC Advisory Services. In addition, the



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convening power and thought leadership, although difficult to capture in a formal program, are another relevant aspect of World Bank Group engagement (chapter 3).

The following sections therefore assess to what extent World Bank Group resources have been allocated in a strategic manner, including upstream and downstream work. It will then analyze in how far the World Bank Group's agenda has reflected the needs of the poor, that is, has responded to their specific constraints; followed by an assessment of Bank Group's capability to address specific country needs.

### **The World Bank Group's Strategic Resources Deployment to Financial Inclusion**

Given its limited resources, the World Bank Group has to allocate them where they are needed the most and are likely to result in a high development impact. One way of measuring the need for such support is by looking at country characteristics with regard to financial inclusion, that is, its "financial inclusiveness." Four types of measures have been chosen by IEG as proxies of a country's financial inclusiveness and hence as an indication for its relative need for financial inclusion support. Each of these measures can be measured objectively using Findex and MIX data. See table 2.1 for details.

- Prevalence and share of the unbanked relative to the country's population
- Capacity of the MFI market to reach the poor, that is, its "depth"
- Funding gap for microloans relative to the country's gross domestic product (GDP)
- Penetration of the MFI market relative to the size of the country

Based on these inclusiveness measures, the universe of client countries was analyzed and divided into quartiles. Such a division yielded four discrete categories depending on the level of inclusion, called lowest-, low-, middle-, and high-inclusion countries.<sup>6</sup> For example, according to figure 2.4, about one-quarter or 24 percent of all client countries fall into the category of lowest inclusion when using the measure, "Number of people who do not hold an account according to Findex in a given country."

Comparing these 24 percent to the 49 percent of World Bank Group support (in terms of number of projects) provided to this category of countries indicates that the World Bank Group strongly support these lowest-inclusion countries. The relative resources allocation in terms of number of World Bank Group financial inclusion projects is (with 49 percent of its portfolio) significantly higher for these lowest-inclusion countries than for any other category. As only 24 percent of countries fall

into this category, the allocation is disproportionately high—which illustrates the strong emphasis on lowest-inclusion countries.

**Table 2.1. Financial Inclusiveness Measures**

Measure	Numerical value	Comment
Prevalence and share of the unbanked	<ul style="list-style-type: none"> <li>Prevalence in terms of the absolute number of people who do not hold an account according to Findex in a given country</li> <li>Share of people who do not hold an account according to Findex over entire population</li> <li>Share of people who do not hold an account at the bottom of the pyramid (BoP, lower 40 percent) over entire population</li> </ul>	The first measure (number of unbanked) emphasizes relatively strong, larger countries, for example, India and China. The third measure, involving the number of unbanked at the BoP, reflects better the target population of this evaluation.
Capacity to reach the poor, that is, “depth” of MFI market	<ul style="list-style-type: none"> <li>Average loan size according to MIX data in client country, GDP</li> </ul>	The average loan size is quoted in the literature is a proxy for the extent to which an MFI markets actually reach the poor, assuming that smaller loan size indicates better reach of the poor.
Funding gap	<ul style="list-style-type: none"> <li>\$ billions of funding gap of very small, micro, and informal enterprises in the respective client country, according to IFC / McKinsey (IFC 2010)</li> </ul>	This relies on IFC’s own calculation and has not been subject to IEG validation, even though the data model has been assessed for its soundness.
Penetration of the MFI market	<ul style="list-style-type: none"> <li>Aggregated gross loan volume (\$ billions) of MIX-reporting MFIs in the respective client country / GDP</li> <li>Share (in percent) of borrowers according to MIX data/total population of client country</li> </ul>	Both measures indicate in how far the MFI markets have developed. One caveat, however, needs to be noted: MIX data may not be entirely representative of the entire MFI market.

Sources: IEG database; Findex data; MIX data; IFC (2010).

Note: BoP = bottom of the pyramid.

To assess how far the relative share of Bank Group’s volume was adequate for the country, the gross loan portfolio of the country’s MFI industry was taken as a benchmark. In total, 1,650 MFIs report to MIX; MIX data provide a detailed breakdown of the respective MFI industry per country. The volume (\$ billions) of gross loans outstanding in a respective country can be taken as an indication for the size of the MFI industry in that country and hence its status of development. Comparing the relative share (in percent) of World Bank Group allocation of volume toward a specific category of countries with the gross loan volume of the MFI industry provides an indication of appropriateness. For example, according to the graph in figure 2.4a, all MFIs together hold 43 percent of the gross loan volume in the “lowest” inclusion countries. These are countries where only 0.4–15 percent of the population are banked. The World Bank Group allocated a full 72 percent of its volume there. This indicates that the World Bank Group gears volume disproportionately toward these lowest-inclusion countries.

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1. Overall, World Bank Group support targets countries most in need of its support, that is, low-inclusion countries. Looking across *all* different financial inclusiveness measures presented in table 2.1, World Bank Group has synchronized its financial inclusion support with country needs; or in other words, the World Bank Group has geared its support toward countries that (i) have a high number of unbanked and also relatively high shares of unbanked, including when looking at the bottom of the pyramid; (ii) suffer from the highest microloan credit gaps; (iii) have a relatively low MFI market penetration, that is, countries where the MFI market is as yet relatively underdeveloped and small compared with the countries' GDP and population size; and (iv) where the MFI industry caters to the poor, that is, where the average loan size is relatively small.

2. Figure 2.4 shows the distribution of World Bank Group support in relation to the above define measures, that is, the prevalence of the unbanked at the country level, the capacity of the MFI market to reach the poor, and the size of the funding gap for microloans (relative to the country's GDP); for sake of simplicity the charts visualizing the fourth measure, that is the penetration of the MFI market relative to the size of the country, is not displayed, but exhibit a similar pattern of World Bank Group support.

- *Prevalence of the unbanked relative to the country's population.* World Bank Group's portfolio is strongly geared toward lowest- and low-inclusion countries. Although about half of the countries of countries belong to the category of lowest and low inclusion countries (25 and 28 percent, respectively), a full 70 percent of Bank Group interventions take place in these two categories of countries. In volume, the emphasis is even stronger: 83 percent of World Bank Group volume (\$) flows there (figure 2.4a).
- *Capacity of the MFI market to reach the poor, that is, its "depth."* Equally pronounced as above, World Bank Group support reaches countries where MFI markets are likely to work for the poor, as evidenced by the average loan size of the respective MFIs. About half of the countries fall into the categories having the "smallest" and "small" loans while 60 percent of interventions and 80 percent of Bank Group volume flows into these countries (figure 2.4b).
- *Funding gap for microloans relative to the country's GDP.* With regard to the size of the microloan funding gap, Bank Group support is somewhat in sync, but it does not emphasize those countries with the relative largest funding gap. As can be seen in figure 2.4c, interventions and associated volume (\$) is somewhat more evenly spread across all four categories

Looking at the relative emphasis of the various World Bank Group institutions and instruments reveals that World Bank lending, IFC advisory and analytic and advisory activities (AAA) have the strongest focus on reaching the lowest and low inclusion countries. Taking again the share of the unbanked in client countries as a

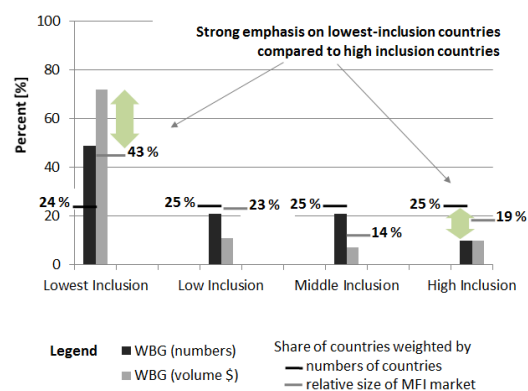
measure, World Bank lending overemphasis countries with the lowest inclusion rates: 67 percent of its interventions take place in this category of countries which represent 57 percent of countries. For IFC advisory, 61 percent of their projects take place in this category; and 60 percent of AAA work takes place in these countries. The resources allotted to the other categories that is, low, middle and higher inclusion countries, is generally commensurate with their prevalence. Figure 2.5 shows the strategic resources allocation of World Bank lending and IFC Advisory Services.

The allocation of IFC investments generally is commensurate with country needs — and when looking at volume invested, IFC exhibits a strong emphasis on countries with the lowest inclusion rate. Fifty-six percent of IFC investments take place in lowest-inclusion countries, commensurate with the relative share of 57 percent of these lowest-inclusion countries (figure 2.6). The demand-driven nature of IFC's business helps explain this pattern; that is, it cannot create investment itself but needs sponsors to go along with. With regard to investment volume (\$), however, IFC does emphasize the lowest-inclusion countries. IFC provides more funds to lowest-inclusion countries than the MFI market itself does: 46 percent of IFC investments (\$) flow into lowest-inclusion countries while about 42 percent of the gross loans of the MIX MFI market are issued in these countries.

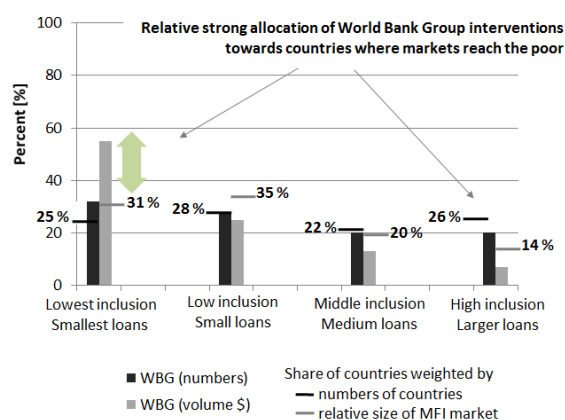
IFC investments can be considered pioneering as they occur in countries where otherwise commercially oriented financial services providers shy away. Although IFC's investment allocation is only about 4 percent above of the MIX volume, it needs to be noted that the MIX market data contain a high number of MFIs that are not aiming at full financial self-sustainability. A fair share of the MFI markets is composed of NGOs with 31 percent of the total market; banks only make up 10 percent of the MFI market.<sup>7</sup>

**Figure 2.4. Client Countries' Financial Inclusiveness and World Bank Group Support**

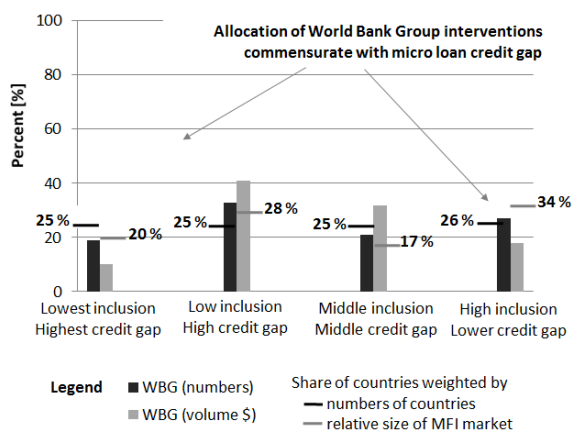
(a) Countries grouped by prevalence of unbanked versus World Bank Group support<sup>a</sup>



(b) Countries grouped by extent to which MFI markets reach the poor (average loan size) versus World Bank Group support<sup>a</sup>



(c) Countries Grouped by their Funding Gap of Microloans versus World Bank Group Support<sup>a</sup>



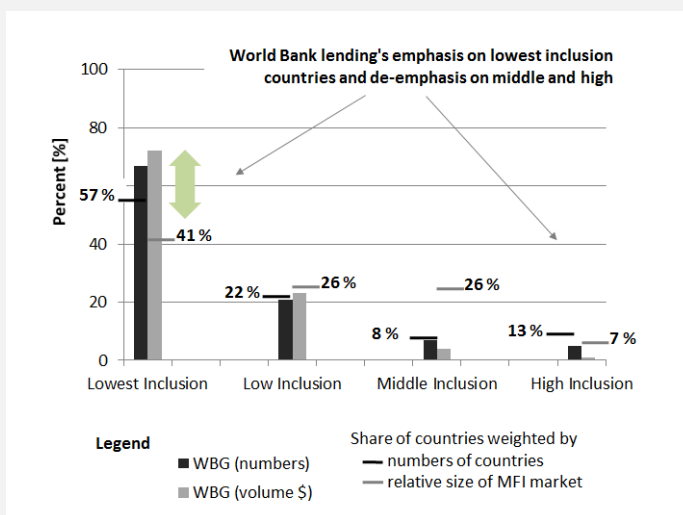
Sources: Findex data; MIX data; IEG database.

a. Data on country-level inclusiveness were transformed using the natural log

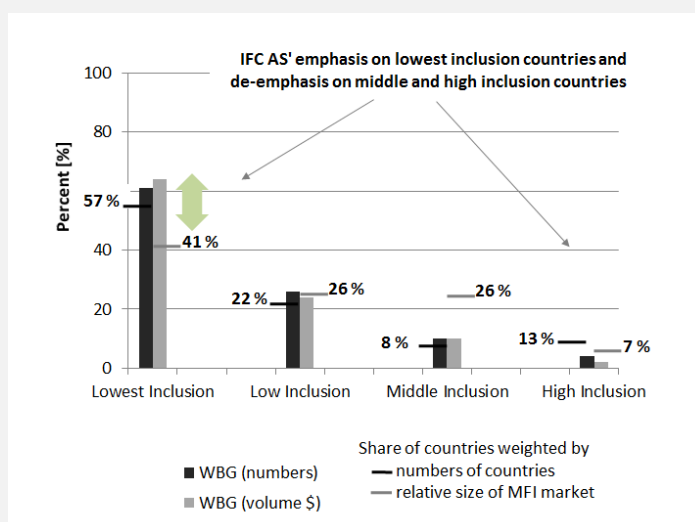
Note: WBG = World Bank Group.

**Figure 2.5. World Bank Lending and IFC Advisory versus Client Countries' Financial Inclusiveness**

(a) World Bank Lending across lowest-, low-, middle- and high-inclusion countries



(b) IFC Advisory Services across lowest-, low-, middle-, and high-inclusion countries

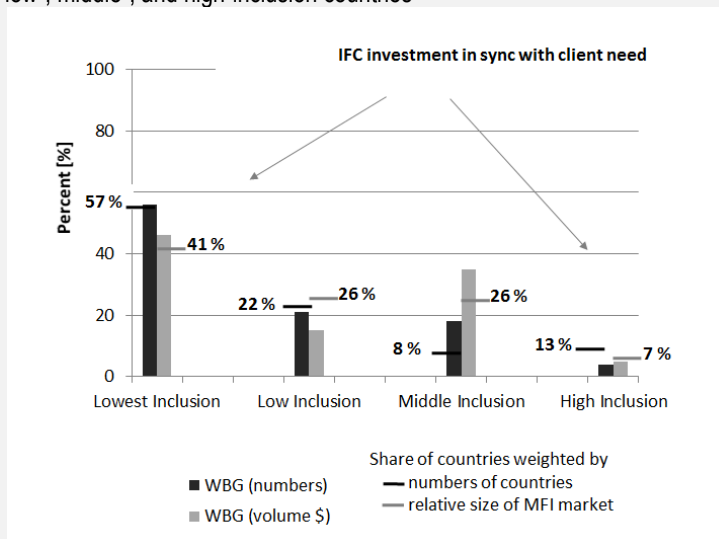


Sources: Findex data; MIX data; IEG database.

Note: AS = Advisory Services; WBG = World Bank Group.

**Figure 2.6. IFC Investment versus Client Countries' Financial Inclusiveness**

IFC IS across lowest-, low-, middle-, and high-inclusion countries



Sources: Findex data; MIX data; IEG database.

In contrast to banks, NGOs tend to receive subsidies through below-market-priced funding and so find it easier to open shop in areas where start-up costs are relatively high. Hence, having 56 percent of IFC investment and 46 percent of its volume (\$) flowing into lowest-inclusion countries can be seen as a sign of high relevance of IFC's MFI support.

MIGA's resources allocation is difficult to assess due to the low number of financial inclusion guarantee projects. MIGA has supported 21 financial inclusion projects through guarantees during the evaluation period. Of these, 12 belong to one MIGA project in support of ProCredit. MIGA's guarantees reach lowest-inclusion countries to some extent, but to a lesser extent than the World Bank and IFC projects. By contrast, MIGA's guarantees are quite frequent in middle-inclusion countries, in particular when looking at guarantee volume: 43 percent of its gross issuances are in middle-inclusion countries, even though these countries only absorb 26 percent of the MFI market globally. In terms of number of projects, the emphasis on middle-inclusion countries is similar, with 19 percent of MIGA projects in these category of countries even though this category only comprises 8 percent of countries globally.

In conclusion, the World Bank Group's allocation of resources devoted to advancing financial inclusion is strategically well aligned with countries' needs, that is, they reach primarily countries with very low inclusion rates. World Bank lending, IFC advisory, and AAA strongly emphasize the lowest-inclusion countries, indicating a high level of relevance. IFC's investments are also well in sync with client countries' needs, but exhibit less of an overemphasis on lowest-inclusion countries. Given that

these markets are typically dominated by NGOs, IFC's presence in these countries is pioneering as IFC aims at establishing self-sustaining microfinance providers.

Following the analysis of strategic resources allocation, the next few paragraphs will analyze the extent to which governments have identified financial inclusion as a priority and how well the World Bank Group has responded to their needs. Subsequently, the next section will also take a look at the beneficiaries and assess the needs for financial services of low-income households and microenterprises, the focus of this evaluation.

## Addressing Country Priorities and Financial Inclusion Constraints

### COUNTRY-LEVEL PRIORITIES AND CONSTRAINTS

Financial inclusion was identified by most country strategies as a priority, albeit not explicitly. Across all 15 countries analyzed in-depth, financial inclusion is mentioned as a priority in the respective country strategy documents during the evaluation period. However, the term *financial inclusion* was hardly used in the country strategy documents; instead, *access to finance* or support to *rural finance* were some of the phrases used, implicitly emphasizing the financial inclusion aspect of the financial sector interventions.

While a prominent issue throughout, only about half of the countries described financial inclusion as a "binding constraint" to growth or poverty reduction in general. About half of the 15 countries evaluated mentioned financial exclusion or the "lack of access to finance" as a binding constraint to growth and poverty reduction (Ghana, Indonesia, Kenya, Pakistan, and Tanzania), and out of these five, four explicitly mentioned "lack of access to finance" as a binding constraint to at least growth and poverty reduction (and also include investment climate and doing business).

For Indonesia, the Country Partnership Strategy FY09–12 specifically states that "inadequate access to financial services for SMEs and poorer households" was a major obstacle to improving investment climate (World Bank and IFC 2008, 95). Limited access to finance is seen as an obstacle to poverty and growth by way of it being linked to the strategies and core engagements supporting investment climate.

Similarly in Pakistan, financial exclusion, or the lack of access to finance, is identified as a constraint to growth and private sector development. Likewise, for Ghana financial exclusion is explicitly described as a constraint to growth and MSME development but not to poverty reduction. However, given the country's growing inequality, promoting broad-based growth will be closely linked with poverty



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reduction, in particular when discussing constraints to broad-based growth in rural areas (where poverty and inequality are more prevalent).

The overall timing of country-level support was generally in sync with global trends. The general timeline about which financial inclusion emerged as an issue in the country documents is between 2000 and 2007. The emergence of financial inclusion in country strategies hence roughly coincides with the general global trend. This finding from the country case studies is further corroborated by portfolio data: as we have seen above, the growth of Bank Group support was largely synchronized with the overall growth of the MFI industry over the last ten years.

The Bank Group's support to financial inclusion broadened over the last ten years, in parallel to the global perception that financial inclusion is a multifaceted endeavor. Throughout the 15 case studies, World Bank Group had a significant emphasis on microfinance during early 2000s, which implies an emphasis on financial inclusion in the countries in question. However, toward 2010, the focus on financial inclusion evolved to include also other themes such as financial literacy, consumer protection, and financial infrastructure interventions.

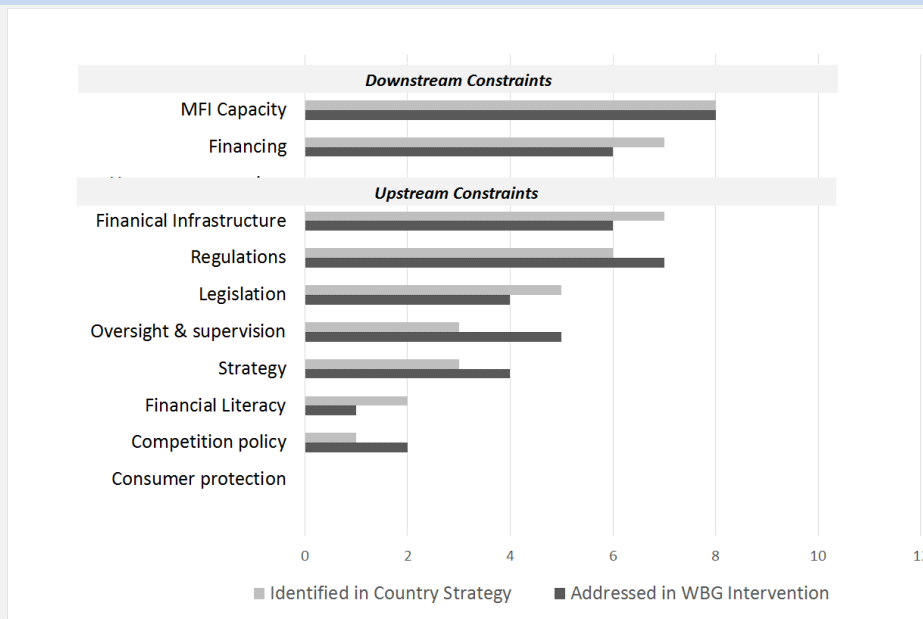
Typically, financial inclusion was pursued under the "growth" pillar. Across all country cases, except for Indonesia, every country has had financial inclusion listed under pillars for growth in the country strategy documents. Financial inclusion had been under different pillars for different time periods, roughly between 2000 and 2014. The shift in financial inclusion being under different pillars also reflects on the transition in the World Bank Group's approach toward this area for different country contexts. Countries such as Azerbaijan, Kyrgyz Republic, and Tanzania maintained financial inclusion under their growth pillars throughout the different country assistance strategy periods spanning years 2003 to 2015. China, India, and Pakistan showed a shift from the growth pillar to "inclusion" or "inclusive development" pillar for their respective country strategies. For Ghana, financial inclusion was listed under the growth pillar in FY04–08 period, shifting to "private sector competitiveness" for the FY08–12 country assistance strategy. Finally, country strategies of Kenya and Mexico showed a transition from poverty reduction from 2004, to "growth" about 2010 for the incorporation of financial inclusion.

Country-specific constraints may impede the implementation of a country's financial inclusion agenda. Identifying financial inclusion as a priority is an important expression of country commitment, but in itself it is not enough. For a country-specific financial inclusion agenda to take root, a set of preconditions needs to be met. This include an adequate regulatory and supervisory regime of both deposit and non-deposit-taking institutions, consumer protection laws of particular

importance as the poor generally lack higher education, sector management capacity and capacity at the MFI level; all of these should be embedded in a country's financial inclusion strategy.

The most common constraints identified in World Bank Group strategies were the lack of capacity at the level of the financial institution, that is, lack of MFI capacity, and lack of finance. These constraints were identified in eight countries and refer to capacity to adapt to regulatory changes, to develop MFI strategies, and to engage in product development, technological upgrading or risk management. The Bank Group responded in most cases with adequate interventions to mitigate this downstream constraint—in both cases led by IFC, indicating the relevant role of advisory services and investments. The second-most common constraints were lack of financial infrastructure and regulatory deficiencies. Both of these constraints are “upstream,” as they relate to the enabling environment, identified in 7 and 6 of 15 case study countries, respectively. For both constraints, the World Bank put measures in place to mitigate them (Figure 2.7).

**Figure 2.7. Financial Inclusion Constraints in Country Strategies**



Sources: IEG country assistance strategies and country partnership strategies; IEG.

Note: N = 15 countries. downstream = measures directed toward MFIs; upstream = measures aimed at improving the policy framework.

Credit reporting, an important component of a country's financial infrastructure, was increasingly addressed as a constraint after the 2008 global economic crisis. A general trend observed is that the country strategy documents emphasize MFI capacity constraints during the 2000s (mostly 2008). However, after the 2008 crisis, financial infrastructure (pertaining to capturing and reporting credit information)

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has increasingly been identified as a significant constraint to financial inclusion, and to the improvement of financial sector in general. This increased attention to credit reporting is possibly an outcome of the financial crisis, following which the World Bank Groups interventions, focused on more expansive and accurate credit reporting. Further example from country cases are presented in box 2.2.

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#### Box 2.2. Constraints to Financial Inclusion: Country Examples

MFI capacity was a leading constraint in Kenya. The lack of capacity points toward a profound lack of capacity of institutions when it comes to adapting to regulatory changes to gain access to finance through commercial banks; this suggests a need for informal institutions to “graduate” to formal status to achieve financial inclusion objectives. Another key area of lack of MFI capacity in Kenya was risk management.

In Pakistan, the identified capacity constraints indicated a lack of adequate products and services, technology, and staff trainings. Inadequate coverage through private credit registries hindered the process of acquiring credit information in Pakistan and therefore the provision of credit and other financial services for the already underserved segments.

Constraints pertaining to MFIs capacity in Tanzania were associated with the lack of financial products (including loans and deposits), outreach to the target beneficiaries (in line with financial inclusion objectives of outstanding loan portfolios), inadequate staff skill of banking regulators who would contribute to regulatory oversight and payment systems, and general financial institutions and MFI constraints.

*Source:* IEG country case studies.

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The Bank Group was consistent in identifying constraint and subsequently also addressing them. Across most countries, once constraints were identified in a country strategy, they were also addressed through Bank Group interventions, which indicates an internal consistency of Bank Group country-level engagement.

Consumer protection and financial literacy were rarely identified as a constraint – despite their importance in regard to the poor. Financial literacy was only identified in two countries and followed up on in one; while the lack of financial literacy has been identified as a significant barrier on the demand side, fighting the lack of financial literacy through development interventions poses a challenges (box 2.3). In light of this, financial literacy interventions are likely to remain a matter of trial and error. Consumer protection did not at all appear on the radar screen of constraints. This may relate to the fact that financial inclusion was initially more concerned with the provision of microcredit, paying less attention to the enabling environment in which this happened. However, the notion of financial inclusion changed, at least after a series of repayment crises 2008 and 2009 in Bosnia and Herzegovina, Morocco, and Nicaragua and 2010 in India (Andhra Pradesh), which underscored the need for consumer abuse by service providers to be checked and consumers be

educated. The latter would help, among other things, keeping overindebtedness at reasonable levels, an issue discussed in the next section.

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**Box 2.3. The Challenge of Fighting Financial Literacy**

Lack of knowledge is an important barrier. There have been attempts at increasing financial literacy, most of them with frustratingly limited results. The outreach effort by Cole, Sampson and Zia (2011) also involved a free two-hour financial education program. Unlike the subsidy to open an account, financial education had no effect on the likelihood to open an account. A similar study in western India finds that financial literacy courses for female microentrepreneurs had no impact on their savings behavior (Field and others 2010). Bruhn, Ibarra, and McKenzie (2014) analyze attendance and effects of a large-scale financial education program in Mexico City and find that monetary incentives is what is most likely to convince individuals to attend.

Attending training results in a 9 percentage point increase in financial knowledge, and a 9 percentage point increase in some self-reported measures of saving, but it had no impact on borrowing behavior. Overall, the authors conclude, however, that most individuals make the right benefit-cost choice when deciding not to attend. On a more positive note, Berg and Zia (2013) find that including examples of responsible and irresponsible financial behavior in soap operas in South Africa can improve financial behavior of viewers, including lower incidence of overindebtedness and gambling. Bruhn and others (2013) report the results of a comprehensive financial education program spanning six states, 868 schools, and approximately 20,000 high school students in Brazil through a randomized controlled trial. The program increased students' financial knowledge, led to a modest increase in saving for purchases, a better likelihood of financial planning, and greater participation in household financial decisions by students. The authors also find significant "trickle-up" impacts on parents' behavior.

In summary, the studies on financial literacy show a very limited effect of such attempts on financial behavior, including savings behavior. There seems more promise in fine-tuning financial literacy attempts to teachable moments, that is, trying to reach out to individuals when they are in the process of making financial decisions. Similarly, reaching out to younger population segments, who are easier to influence seems promising.

Source: Beck (2015).

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**AVOIDING OVERINDEBTEDNESS**

Too much credit can also be a bad thing. Knowing how much credit a country's MFI clientele can absorb is critical for microfinance policy makers and practitioners. Improving access to financial services while ensuring that its clients remain protected from the risks related to over-borrowing is essential (PlaNet Rating 2013). For the poor, overindebtedness can result in an unsustainable spiral of repayment, with consequent damage to investment in their microbusinesses or to household consumption and welfare, as presented in the literature review in chapter 1. It is

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hence essential to understand to what extent client countries have reached levels of market saturation—and are hence at risk of overindebtedness—and as to whether World Bank Group takes this market saturation into consideration in its strategic resources allocation.

Overindebtedness of microfinance clients is perceived as a risk facing the industry (CSFI 2014). Accordingly, overindebtedness is widely seen to be symptomatic of wider problems in the industry: surplus lending capacity, a lack of professionalism within MFIs, and an emphasis on growth and profit at the expense of prudence. Overindebtedness is linked to a range of risk factors, including credit risk; the (in)ability of microfinance providers to manage the lending process; the lack of credit information of MFI clients; the level of competition, in particular the rapid growth in lending capacity created by abundant funding and new entrants; potential weaknesses in consumer protection regulations and political interferences. The fact that consumer protection is rarely identified as a constraint, as pointed out above, is hence particularly worrisome.

Taking the Microfinance Index for Market Outreach and Saturation (MIMOSA) score, about 18 percent of countries warrant a careful evaluation of potential overindebtedness. This MIMOSA score ranks countries from 1 to 5. A score of 1 implies significant underdevelopment of formal credit use; markets scoring 2 or 3 generally show a normal level of development in the use of formal credit; and countries scoring 4 or 5 are either approaching their credit capacity threshold or have crossed it altogether and thus require a strong emphasis on preventing overindebtedness (PlaNet Rating 2013). About 6 percent of countries are at risk of overindebtedness (that is, are rated 5) and about 13 percent warrant a detailed analysis of market stability factors—including evaluation of levels of overindebtedness (that is, are rated 4).

The lack of safeguards against multiple borrowing and lack of credit information played a major role in one of the most prominent cases of overindebtedness, the Andhra Pradesh microfinance crisis (Box 2.4). Similar reports have also been published on Tanzania, where prevalence of multiple borrowing was very high, underscoring the need for efficient credit information systems.<sup>8</sup>

Broadly speaking, World Bank Group strategic resource allocation to client countries reflects market saturation. Taking the MIMOSA as an indicator, World Bank Group's activities are commensurate with level of saturation. Countries at risk of overindebtedness receive relative limited finance from the World Bank Group, commensurate with their limited ability to absorb more credit volume. Countries rated 5 on the MIMOSA score receive commensurate support in numbers of projects:

jointly such countries represent seven percent of all countries, but receive 9 percent of all Bank Group support; however, only 4 percent of IFC's investments and 3 percent of the World Bank's finance flows into these countries, reflecting well these countries' limited credit capacity. Only AAA work can be found more often in countries at risk, that is, those rated 5. Thirteen percent of all financial inclusion AAA work can be found in these countries even though they represent only 7 percent of all countries. This indicates that the World Bank Group – intentionally or unintentionally – provides the support these countries needs rather than flooding them with funding which they could not absorb safely.

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**Box 2.4. The Andhra Pradesh Microfinance Crisis and Crisis Response**

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**The Andhra Pradesh crisis.** By 2010, two major systems of finance for poor people coexisted in Andhra Pradesh: there were roughly 6 million borrowers from microfinance programs and 19 million borrowers through a linkage program for rural self-help groups that channeled commercial bank finance. In late 2010, Andhra Pradesh state authorities reacted to claimed abuses and breakneck growth of the microfinance industry, which included overlending, inadequate consumer information and protection, and abusive collection practices. Although abuses clearly occurred, the degree to which abusive practices were widespread and the connection of such practices to an alleged 72 suicides remains hotly debated. The crackdown took the form of state legislation that was so restrictive that no MFIs found it possible to operate or to collect most outstanding loans. The ordinance and regulations eliminated MFIs as competition to the self-help group system as a means of providing finance to the poor.

**Crisis Response.** The Andhra Pradesh microfinance crisis, deeply shocked the microfinance industry and India's central bank – the Reserve Bank of India (RBI), stimulating both to remedial action. The RBI took several key steps to address the liquidity crisis in the microfinance sector, including encouraging banks and development finance institutions to re-start lending to MFIs, and granting certain relaxations with regard to the restructuring of bank loans to MFIs. The RBI also set up the Malegam Subcommittee, whose report in January 2011, formed the basis for subsequent RBI regulations of nonbank financial companies (NBFCs) MFIs, including limits on interest rates, margins, fees, and loan tenors, as well as capital adequacy and provisioning requirements, the mandating the establishment of credit bureaus and the monitoring of MFI's conduct. The microfinance industry strengthened its nascent professional association for nonbank financial institutions, the Microfinance Institutions Network, into a viable self-regulatory body recognized by RBI. Through the Microfinance Institutions Network, nonbank financial institutions introduced a code of conduct for all NBFCs, and a credit information scheme (now adopted by multiple private credit bureaus) covering all NBFC loans. RBI, after initially introducing a fairly strict set of regulations for NBFCs to restore faith in the industry, has recently begun vetting drafts of more viable long-term regulations and has introduced regulations allowing for small banks which can take deposits and payments banks as new instruments for financial services. The World Bank

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Group, which had been working to support the development of MFIs and encourage responsible finance, provided significant formal and informal support.

*Source:* IEG country case studies.

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#### PRIORITIES AND CONSTRAINTS OF HOUSEHOLDS AND MICROENTERPRISES

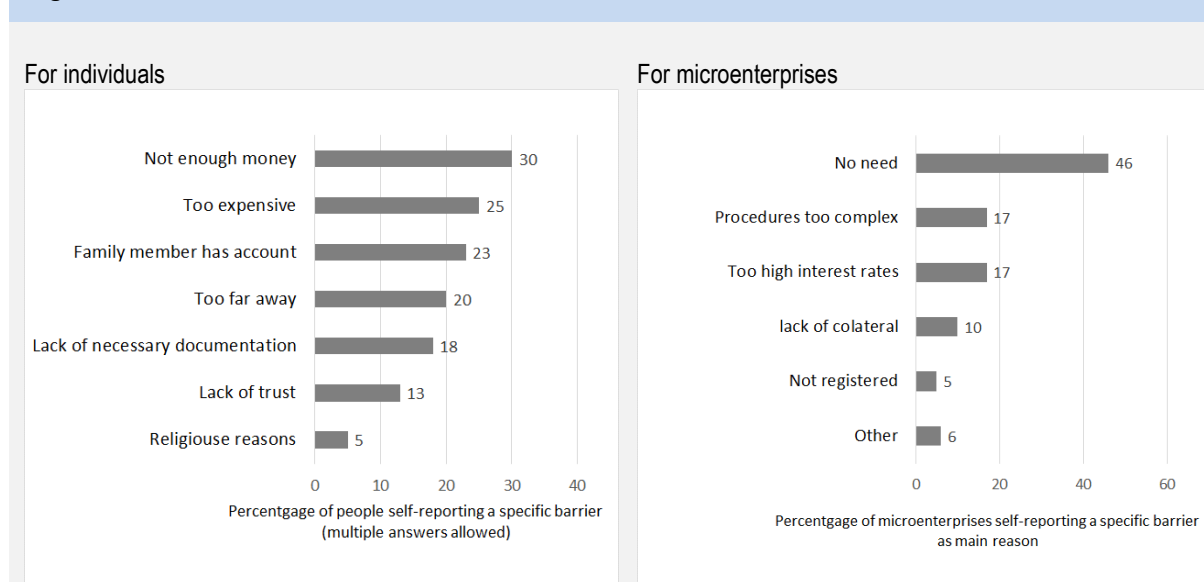
To assess to what extent financial inclusion is also a concern for the people in client countries, IEG analyzed the results of a large-scale enterprise survey and Findex data on individual constraints. The enterprise survey provided access to responses of 4,246 informal enterprises of a survey conducted by the World Bank from 2003. The survey covered 16 countries in the Sub-Saharan Africa and Latin America and the Caribbean Regions. Though not representative for the globe, the results are intended to provide a flavor of constraints to financial inclusion among a large sample of microentrepreneurs. Note that firms in the informal sector are on average micro-sized and relatively younger (Farazi 2014); about 80 percent of total MSMEs are informal today (IFC 2012).

Lack of access to finance is a top priority for microenterprises—underscoring its high importance to client countries' governments. The enterprise survey asked respondents to evaluate the severity of obstacles that firm faced. The most severe constraints were access to electricity, followed closely by access to finance. Access to land, crime, and civil disorder followed as lesser constraints. When it came to identifying their single biggest constraint, more firms identified access to finance, regardless of size of the enterprise. These IEG findings are corroborated also by the literature that indicated that access to finance is the single biggest obstacle (Farazi 2014).

High interest rates, collateral requirements, and procedural complexity are the key deterrents for microentrepreneurs. In the overall population of enterprises, 67 percent are “unbanked,” that is, have neither a bank account nor a loan from a formal financial institution; while 33 percent were banked. Only 9.8 percent had a loan, although larger firms (above 5 employees) had loans twice as often. Of the 90.1 percent that did not have a loan, 46 percent said they did not need one. The remaining 43.5 percent who indicated they needed a loan, but did not have one, were deterred mainly by high interest rates, collateral requirements and procedural complexity. Complexity of the application being more of a concern than the price and collateral requirement for informal firms can be due to the fact that these firms tend to lack documentation and other required legal papers needed for a loan application.<sup>9</sup>

Similar to microenterprises, individuals also quote lack of funds, costs, distance and lack of documents to comply with the procedural requirements as the key factors for not having an account. Globally, the most frequently cited reason for not having a formal account is lack of money. The next most commonly cited reasons for not having an account are that banks or accounts are too expensive and that another family member already has one. (Demirguc-Kunt and Klapper 2013). Figure 2.8 juxtaposes constraints of individuals and of microenterprises—indicating that both suffer from a set of very similar constraints. This is not surprising because at the onset of an entrepreneurial activity, there is often little difference between individuals and microenterprises. Assets move back and forth and savings are likely joint; microenterprises frequently try first as individuals to get consumer loans due to lack of collateral or formal credit references.

**Figure 2.8. Constraints to Financial Inclusion**



Sources: IEG, based on enterprise survey data; Demirguc-Kunt and Klapper 2013.

Defining target beneficiaries and assessing their specific priorities and constraints is hence important for financial inclusion projects. Constraints to financial inclusion deserve to be analyzed in detail—and are likely to show the way for policy interventions for the World Bank Group. Given the varying extent to which financial inclusion is a priority and the wide range of reasons why low-income people and microenterprises do not have access to finance, a detailed assessment of the target group's needs and constraints is essential.

Box 2.5 outlines selected solutions that could help overcome some of these identified constraints and corresponding interventions are likely to contribute to World Bank Groups endeavor in reaching its Universal Financial Access goal 2020. To assess



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how far the World Bank Group has tailored its interventions to the priorities and constraints of the people in client countries, IEG summarizes in the following section to what extent the World Bank Group has actually identified specific target groups and assessed their needs.

Across the portfolio, most projects identified target beneficiaries – albeit, most lacked a definition. Most project beneficiaries are low-income households and families, microenterprises and very small firms, and those “underserved” by the financial system. In the majority of cases, while these beneficiary types were identified in project documents, they were often not defined. For example in the case of IFC’s Investment in Advans Ghana, the MSME sector was described as mainly informal but includes about 70 percent of the population and contributes about 40 percent of the country’s GDP. Nor were beneficiaries defined by IFC’s standard definition—as in Kenya’s MSME Competitiveness Project, a joint International Development Association–IFC project that adopted IFC’s standard definition and referred to its target group as including not only micro (1–9 employees) and small (10–49 employees), but also medium-sized firms, as this segment plays a critical role in employment generation and market linkages. This trend is consistent across the World Bank Group institutions (approximately 7 percent of IFC Investment Services and Advisory Services versus approximately 12 percent of World Bank Lending and AAA).

#### Box 2.5. Overcoming Constraints: Examples

**Overcoming distance through branchless banking.** When looking at data on constraints in detail, distance from a bank is a much greater barrier in rural areas. Technological and other innovations that help overcome the barrier of physical distance could potentially increase the share of adults with a formal account by up to 23 percentage points in Sub-Saharan Africa and 14 percentage points in South Asia. At the same time, people in Sub-Saharan Africa use mobile phones more often for conducting business than in Latin America and the Caribbean (73 percent versus 42 percent) which points at mobile applications for the provision of financial services as potential solution, at least in Sub-Saharan Africa, where population density is scarce and usage of mobile phone high. In a similar vein, agent banking models help overcome the high operational costs of traditional banks in sparsely populated areas and hence help provide financial services where distances are a constraint.

**Making procedures easier through risk-based know-your-customer (KYC) requirements.** Another example, as we have seen above, is that procedural requirements deter many microentrepreneurs from opening an account; similarly, documentation requirements for opening an account tend to exclude workers in the rural or informal sector more often, as they are less likely to have wage slips or formal proof of residence. In Sub-Saharan Africa documentation requirements potentially reduce the share of adults

with an account by up to 23 percentage points. In this context, reviewing a countries KYC requirements will be essential as it would allow introducing a tiered system where KYC requirements are a function of the risks involved that is, allowing for low KYC requirements for low transaction accounts.

**Enabling cheap access through no-frill low transaction accounts.** One of the most commonly cited reasons for not having an account are that banks or accounts are too expensive. Given that poor people often require accounts for rather simple transactions of low volume, fostering the introduction of cheap no-frill accounts is likely to enable financial inclusion for many poor people – in particular when coupled with risk-based KYC requirements, that is, no-frill accounts that can be opened easier and with reduced documentation requirements as these types of accounts are for low-volume transactions only, hence not the target of anti-money laundering regulations.

*Source: Demirguc-Kunt and Klapper (2013).*

In addition, about one-third of projects focus on women and rural areas. Though women are clients of many of the institutions supported in the World Bank Group financial inclusion projects (about 68 percent of MFI clients are women), they are mentioned as project beneficiaries explicitly in approximately 30 percent of projects. This trend holds true across the World Bank lending (35 percent) and IFC investment and advisory portfolios (30 and 31 percent, respectively). Of those projects that mention women beneficiaries, a minority of projects provide an in-depth description of this target population. An exception to this may be observed in IFC's investment and advisory linked project with Exim Bank Tanzania, where a definition of "women entrepreneurs" is included in the project's Legal Agreement. Rural beneficiaries are identified in 30 percent of project documents, though the share of rural projects varies across institutions. Projects with rural beneficiaries account for over 40 percent of the World Bank lending portfolio compared to 32 and 30 percent for IFC investment and advisory projects, respectively. Interestingly, gender and rural area are targeted in one-third of financial inclusion projects in both projects that focus on microenterprises or on households.

A minority of projects identified urban areas as their primary target market, mentioning rural expansion as a future objective. Although most of the remaining portfolio remains mostly undefined in terms of geographic targeting (by focusing on both urban and rural), a minority of projects identified urban areas as its focal outreach area. These projects, however, often contained language that implied a future move toward rural and more underserved areas. For example, IFC's linked investment and advisory project with Tameer Bank in Pakistan identified its target market as "urban, self-employed small businesses with combined aggregate annual household incomes of Rs18,000 (\$300 equivalent)"; the institution aimed to expand to peri-urban and rural areas in the future, "if feasible." Similarly in Tanzania, IFC's linked investment and advisory project would begin operations in Dar es Salaam

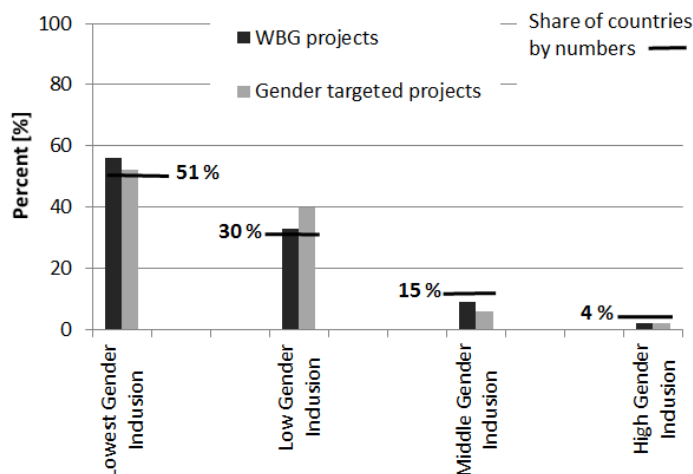
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and focus on the urban clientele of MSMEs but aimed to “rapidly” expand its branch network to other cities in Tanzania and to serve rural and semirural clients through microbranches, mobile bank operations, and cooperation with savings and credit cooperatives.

Gender was often identified as important project dimension when countries exhibited low inclusion rates for women. About half of the world’s countries have very low financial inclusion rates for women. In these lowest-inclusion countries, 56 percent of World Bank Group projects are located and 52 percent identified gender as dimension. Similar with low-inclusion countries: these capture 30 percent of countries, 33 percent of projects, and 40 percent of gender-focused projects. This indicate that the focus on gender is well in sync with the needs, that is, where women are mostly excluded (figure 2.9). Likewise, rural areas were specified as focal areas when the rural population was largely excluded from financial services. While the data and corresponding figure are not reproduced here, they look similar to the analysis of rural aspects.

**Figure 2.8. Identification of Gender Is in Sync with the Gender Gap**



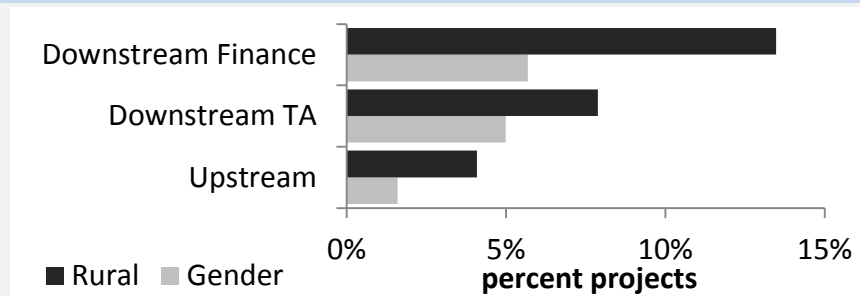
Source: Findex data.

However, financial inclusion projects frequently fail to spell out the constraints specific to these beneficiaries. Project documents often mention constraints to financial inclusion in client countries but often fail to spell out how these constraints affect the project’s beneficiary groups. Figure 2.10 indicates differences between identifying gender- and rural-specific constraints. Rural constraints are presented more often in project documents than gender-specific constraints. Another pattern that can be seen from project data is the fact that downstream finance and

downstream technical assistance constraints are more often identified for both the rural and urban subsets than are upstream constraints. This is likely because upstream constraints are often seen as “systemic” and thus affect all beneficiaries, both direct and indirect.

However, there are cases when these constraints are explicitly defined, such as in the World Bank’s Rural Financial Services project in Ghana, which describes the country’s oversight capacity as “overextended,” given that the World Bank of Ghana has the “statutory mandate to monitor rural bank operations (as is the case for other, mostly urban based, commercial banks). However, this task is made very difficult by the large number, isolation and wide geographic distribution of the 111 rural banks. As a result, poorly performing banks (that actually need) do not often receive the intense supervision required and some banks may not be supervised in a given financial year” (World Bank 2000, 7–8).

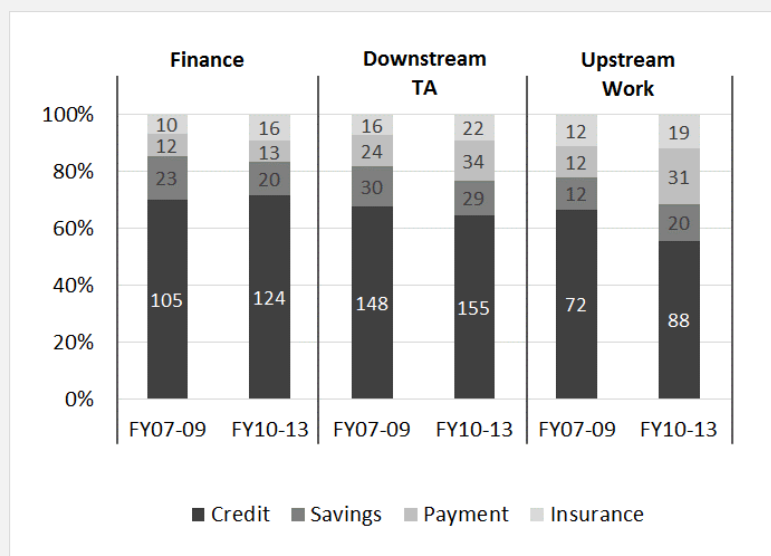
**Figure 2.9. Identification of Gender- and Rural-Specific Constraints in Project Documents**



Sources: World Bank Group databases; IEG database.

Although in earlier years the World Bank Group’s inclusive finance support has relied mainly on credit-related interventions, it has gradually embraced other services, such as payments and savings, which are known to have higher potential to improve the lives of the poor. With a growing realization that poor households and small firms need broader financial services than just credit, the original focus on credit provision during the early days of the financial inclusion agenda gradually gave way to a more comprehensive concept that also included savings, and later payments and insurance. The World Bank Group was no exception to this general trend (Figure 2.10. World Bank Group Support by Type of Financial Services. Across all its instruments, finance, downstream technical assistance and upstream policy support work, credit aspects originally dominate. Although downstream technical assistance addressed noncredit aspects slightly more often than finance, during the last three years upstream policy support exhibited gradual shift toward payment systems, insurance and savings.

Figure 2.10. World Bank Group Support by Type of Financial Services



Source: IEG database.  
Note: TA = technical assistance

The focus on credit has simple reasons. Credit is easier to regulate than deposit taking (savings); credit also requires discipline; that is, the client is compelled to repay at regular intervals (while most schemes do not compel savers to make regular deposits). By contrast, mobilizing local client savings is not cheap, because of high mobilization and transaction costs. From an MFI point of view, paradoxically, it may be cheaper to provide poor people with credit than to take care of their savings, and internal incentives may encourage the greater financing required by credit projects. However, an increased mobilization of savings in the local currency would also make MFIs more impervious to foreign exchange fluctuations, reduce their need for hedging, or reduce the foreign exchange risk passed on to customers. Finally, it may also make financial markets less vulnerable, as international funders tend to withdraw funding to frontier markets during crises.

## Conclusion

Financial inclusion has been lifted to the highest strategic importance by President Kim by declaring its commitment to Universal Financial Access by 2020. Over the last six years (FY07–13), World Bank Group support to financial inclusion grew by about 20 percent – however, that was outpaced by the growth of the MFI industry, which grew by 80 percent during the same period. The fact that IFC supported (either through investments or advisory services) MFIs that jointly make up 39 percent of the global microloan volume demonstrates IFC’s leadership role.

But despite the growth and relative reach of World Bank Group, its support to financial inclusion is small given the large number of unbanked and the microcredit gap. Under these circumstances it is imperative that the World Bank Group strategically allocates its resources, shifting them toward where they are needed the most and where they can be expected to have the highest impact either in terms of creating new markets or scaling up existing markets. While in earlier years the World Bank Group's inclusive finance support relied mainly on credit-related interventions, it has gradually embraced other services, such as payments and savings which are known to have higher potential to improve the lives of the poor.

Globally, the World Bank Group's allocation of resources devoted to advancing financial inclusion are strategically well aligned with countries' needs, that is, they reach primarily countries with low inclusion rates and where markets actually reach the poor. In particular, World Bank lending, IFC advisory, and AAA are strongly geared toward the lowest-inclusion countries. Also IFC's investments are well in sync with client countries' needs. Given the self-sustaining nature of IFC investments, the presence in lowest- and low-inclusion countries is remarkable, as these countries are typically served by MFIs that rely on subsidies, such as NGOs. Overindebtedness of microfinance clients is perceived as a risk facing the industry. But IEG found that, broadly speaking, the allocation of World Bank Group strategic resources to client countries reflects market saturation, improving markets at risk of overindebtedness with AAA work rather than with funding. At the country level, World Bank Group support for financial inclusion was relevant in as much as it addressed a clear development priority. The most common constraint that Bank Group strategies addressed are lack of capacity and financing of financial institutions along with financial infrastructure (credit reporting) and regulations. Other important constraints, such as consumer protection and financial literacy, however, have almost never been addressed.

Across the portfolio, most projects identified target beneficiaries, such as microenterprises, albeit most lacked a definition of what these projects understand under a microenterprise. This is important as project may end up supporting larger companies under the heading of microfinance. Of those projects that mention women beneficiaries, a minority provide an in-depth description of this target population. However, financial inclusion projects fail to spell out the constraints specific to these beneficiaries.

The Bank Group's public commitment to a specific measurable goal contributed to sustaining and expanding an international dialogue to reach consensus and advance the financial inclusion agenda. However, despite its public commitment to the Universal Financial Access goal 2020, there appears to be only limited guidance on

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how to operationalize this goal. The Bank Group's current approach delineates principles of actions and key building blocks, but it remains to be seen how this goal will be translated into practice. Conceptually, the link between access and inclusion (active use) of financial services is clear, but empirically, nonutilization rates in some schemes raise questions.

A lot depends on the quality, design and utility of this initial access. For example, the promotion of access through government-supported programs to digitalize cash payments via mobile phones or to roll out no-frill accounts for a large share of the population, may not necessarily lead to inclusion. High dormancy rates and low usage of newly opened accounts offer additional caution, in particular in countries that implemented mass rollout programs, but also in low-income and lower-middle-income countries in general. The current World Bank Group's strategy of focusing on 25 priority countries may also have to be adjusted going forward as the remaining excluded will increasingly be broadly distributed among many countries. To what extent and how those who remain excluded by 2020 (according to recent extrapolations about one billion of people) will be integrated in the formal financial system is another question the World Bank Group's strategy to financial inclusion leaves unanswered.

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<sup>1</sup> <http://www.worldbank.org/en/news/press-release/2015/04/17/world-bank-group-coalition-partners-make-commitments-accelerate-universal-financial-access>

<sup>2</sup> For example, see Ashraf, Karlan, and Yin 2010; Bruhn and Love 2014; Bruhn and others 2013; Burgess and Pande 2005; Karlan and Zinman 2010.

<sup>3</sup> According to MIX data 2012.

<sup>4</sup> In the relevant loan segment, according to IFC and McKinsey data (IFC 2010), classified as "very small," "micro," and "informal."

<sup>5</sup> With KfW expected to decrease its ambitions, IFC is even expected to move up to number 1.

<sup>6</sup> Most data distributions show "positive skewness," that is, they are skewed to the lower end (left end) because many countries have a very low level of inclusion according to these measures. Therefore, data were transformed using the natural log. As a result, countries on the left (including those on the left in figure 2.3) have actually *very* low inclusion rate.

<sup>7</sup> IEG's analysis of MIX data showed that the relative share of the various legal forms of MFIs (nongovernment organizations, nonbank financial institutions, credit unions, and so forth) is about the same in lowest-, low-, middle-, and high-inclusion countries.

<sup>8</sup> More than 70 percent of the 250 microfinance clients had at least two loans from different MFIs at the same time. In addition, about 16 percent had also borrowed from individual lenders. Major reasons for multiple borrowing were insufficient loans from MFIs, loan recycling, and family obligations. More than 70 percent of the respondents had problems in loan repayment because of multiple pending loans. The study found that education level and number of dependents of the respondent significantly influenced the number of loan contracts. To control the incidences of multiple borrowing, the study recommends that MFIs should devise a way of sharing clients' loan

information. In addition, MFIs should provide adequate loans so as to avoid the practice of clients to reapply to other MFIs to meet their requirements. Some form of training should also be provided to help clients distinguish between business and family matters (Mpogole and others 2012).

<sup>9</sup> Having a loan is associated with higher employment growth rate than a microenterprise without a loan. Using data from the enterprise survey, IEG sought to example employment growth, that is, increase in employees since the creation of the firm, controlling for firm age), using a series of explanatory variables. The controls for firm characteristics, initial size, age, sector, and a range of other factors, captured in dummy variables. Other things being equal, an informal enterprise having a loan is associated with an 8.1 percent higher employment growth rate than a microenterprise without a loan. Older firms appear to grow faster, but this is due to the fact that firms that exited are no longer surveyed; in other words, only the survivors are surveyed, resulting in a bias.



### 3. Policy Reforms that Support Financial Inclusion

#### *Highlights*

- ❖ The World Bank Group has been able to substantially increase its impact in advancing the policy agenda for financial inclusion through its global partnerships.
- ❖ Partnerships clearly extend the reach, resources, and influence to promote access to financial services by the poor and microenterprises. Partnerships require resources, can dilute the voice of the World Bank Group, inhibit “branding” or taking credit, and may sometimes pursue goals not squarely aligned within the World Bank Group’s own strategy.
- ❖ With regard to the World Bank Group’s country-level engagement on policy reform, the approach currently taken to identify and tackle constraints to financial inclusion is not sufficiently systematic nor comprehensive.
- ❖ International Finance Corporation advisory interventions that foster the establishment of important elements of an enabling environment are relevant and often crucial. Such projects frequently benefited from high-quality analytical work and stakeholder assessments and were often executed in sound collaboration across the World Bank Group.
- ❖ The lack of an adequate monitoring and evaluation system made attribution of success to International Finance Corporation interventions difficult.

Financial inclusion requires an appropriate policy framework and regulatory environment. To make financial inclusion happen, country governments need commitment, strategies, and tools. Although this is needed for any sector reform effort, it applies even more so for financial inclusion. Financial inclusion “pushes the boundaries” of traditional banking inasmuch as it tries to reach out to the low end of the retail market. This brings along a wide range of challenges both for the public sector providing the regulatory environment (for example, in terms of installing effective supervision and oversight mechanisms or establishing prudential as well as nonprudential norms for the various service providers) and for the private sector as investors face very small transactions amounts making business merely sustainable in many cases.

This chapter discusses the World Bank Group support to policy reforms, through both international partnerships and through its country-level engagement to create adequate regulatory frameworks. The Bank Group substantially contributes to global knowledge, standards and policy norms. International partnerships are important means to nourish government commitment, developing strategies and

sharing knowledge and innovative approaches. These are often important precursors or inputs to client countries' financial inclusion agendas.

The World Bank Group has played a vital role in a range of international partnerships, using its convening power and expertise to advance the financial inclusion agenda. Often these efforts go unnoticed as they are not framed in an official program. Hence this evaluation tries to shed light on the role and effectiveness the World Bank Group had in this space. This chapter further analyses the role and effectiveness the World Bank Group played in shaping the enabling environment – and here in particular the regulatory environment – in client countries through its lending and advisory and analytic and advisory activities (AAA) work.

### **Financial Inclusion through Global Partnerships**

The World Bank Group uses partnerships as a central instrument for implementing its financial inclusion work. At the 2015 Spring Meetings, President Kim stated that, to promote financial access, “The World Bank Group’s role is to convene and energize a coalition of partners – and also to step up our work” (World Bank 2015). Some of these are the direct partnerships formed with governments of low and middle-income countries, organizations and businesses in the context of country strategy, programs and projects. Others can be specific partnerships with a major international donor, such as the Partnership for Financial Inclusion, which the International Finance Corporation (IFC) has forged with MasterCard to develop agent banking and mobile financial services in Sub-Saharan Africa.

A second important example of a specific partnership is in the arena of knowledge generation and sharing, and provides a resource used extensively in this evaluation. The Global Findex provides an important set of indicators for 148 countries on financial inclusion based on information collected in partnership with Gallup World Poll, designed and overseen by the World Bank Development Research Group, and funded by the Bill and Melinda Gates Foundation.

Beyond this, the World Bank Group uses a number of international and global partnerships through which it plays a role in expanding financial inclusion through knowledge generation and sharing, standard setting, policy guidance, piloting, and sharing innovative approaches and a host of other initiatives. Partnerships are a key means to extend reach and presence, and very senior IFC and World Bank staff are deeply involved in several of them. They can be a means to transmit knowledge World Bank Group has gained through its own experience and research or gain

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knowledge through research, piloting and consultation. Although the Independent Evaluation Group (IEG) cannot evaluate these partnerships because they lack adequate results frameworks and evidence, it is clear that these partnerships form an essential part of the World Bank Group's efforts both to promote Universal Financial Access by 2020 and longer-term aims to achieve universal financial inclusion. Partnerships they require resources and senior staff of the World Bank Group, can inhibit or dilute its own "branding," and may at times pursue goals or methods not squarely aligned the World Bank Group's own strategy. However, it is clear the World Bank Group values partnerships and that they can mobilize tremendous resources and commitment, and help contribute to or complement the World Bank Group's own programs and projects and supplement its capacity.

#### **CONSULTATIVE GROUP TO ASSIST THE POOR**

With the creation of the Consultative Group to Assist the Poor (CGAP) in 1995, the world got its first global partnership of leading organizations seeking to advance financial inclusion of the poor. Its activities, aimed to find innovative solutions to address barriers to financial inclusion, include high-level advocacy, research and knowledge sharing on client demand, support for product and business model innovation, policy advice, and guidelines and standards for donor effectiveness. Much of its activity is focused on generating and sharing open knowledge, open data, and related practical insights of a public good nature and private and public experimentations that demonstrate viable product and business model innovations.

CGAP is currently a partnership of 34 leading organizations. Its Council of Governors is chaired by the World Bank and comprises of members who finance its core program with unrestricted funds. The World Bank also acts as financial administrator of trust funds it established to support CGAP activities. Its executive committee advises the Council of Governors and is currently composed of representatives of the World Bank, the Japanese International Cooperation Agency, the European Investment Bank, the Norwegian Agency for Development Cooperation (NORAD), International Fund for Agricultural Development, the MasterCard Foundation, and two microfinance institutions (MFIs)—M-KOPA and Absa.

Hosted at the World Bank headquarters, CGAP's early work focused on microcredit, informed strongly by the experience of the Grameen Bank in Bangladesh. Later, CGAP came to emphasize multiple financial services, including mobile payments. CGAP often works in close partnership with World Bank Group institutions and staff, undertaking work that is complementary or collaborative or piloting for potential scale up. In the 2007 Financial Sector Strategy, the World Bank identified CGAP as leading on microfinance, focusing on "sound policies and best practices"

with “an increasing emphasis on the regulatory and market development implications of the use of modern technologies (e-banking, phone-banking)” (World Bank 2007, ix). CGAP also provides a platform for knowledge sharing and convening that is used extensively by the World Bank Group. Both the World Bank and IFC have had periods of close partnership on aspects of financial inclusion and now, in the drive for universal access by 2020, the collaboration appears even tighter.

This evaluation offers an evaluation summary of recent and past reviews and assessment of CGAP. Although CGAP has not to date been rigorously evaluated,<sup>1</sup> there has been a range of reviews and assessments that tried to gauge the role CGAP plays at the global level. A 2008 IEG review found that although its achievements were “impressive,” “weaknesses in CGAP’s monitoring and reporting system” made it hard to evaluate its contribution to alleviating poverty. The review further praised its collaboration with World Bank Group, but cautioned against too close a relationship, “which could generate perceptions of unfairness and inequity on the part of other CGAP members” (IEG 2008a, xiii, xiv, xviii).

IEG’s 2011 independent assessment of the World Bank’s involvement in global and regional partnership programs finds that CGAP has become “a powerful and pivotal force in the microfinance field, playing a critical role in helping build inclusive financial systems by providing advisory services, developing and setting standards, and advancing knowledge, training and capacity building.” However, CGAP lacks a “well-articulated theory of change to indicate how each program’s strategies and priority activities were expected to lead to the achievement of the program’s objectives,” its monitoring and evaluation (M&E) system is “not well designed,” and data on achievement of outcomes is not systematically collected. Nonetheless, IEG notes progress under way to strengthen M&E and the development of a “results-management system” (IEG 2011, 34, 32, 27, 29).

The April 2012 Ayani-Universalia external mid-term review of CGAP also notes its major achievements and apparent impact. Specifically, it identifies a high relevance as a “valuable and recognized brand in the field of financial inclusion.” It finds CGAP “very effective in realizing its overall objective to create and share practically relevant knowledge to advance access to financial services for the poor.” It also commends its general program design. However, the evaluation suggests a need for a more rigorous focus and framework by which to evaluate its impact: “[CGAP should] articulate the theory of change of the overall program . . . review and revise . . . the results framework to ensure that it reflects the program logic [and] develop a formal [M&E] process and indicators to guide an overall assessment of

CGAP's planned/actual cumulative performance over time" (Ayani and Universalis 2012, viii, ii, vi).

In its 2014–18 Strategic Directions document (CGAP 2013), CGAP aims to rectify this by defining a results framework that measures progress against defined objectives in terms of access and use of financial services by the poor globally, achievement of CGAP's strategic objectives, and CGAP's organizational performance. The most recent impact evaluation team work on partnerships which also covered CGAP again underscores these points (box 3.2). This evaluation found that CGAP has only quite recently developed a clear results framework. IEG did not come across results frameworks or independent reviews or evaluations of other partnership bodies, beyond a progress report.

### Box 3.1. Findings from Recent IEG Evaluation of Partnerships

IEG, in its work on partnerships and trust funds, has found four common challenges related to selectivity, oversight, linkages to country operations, and results frameworks:

**Selectivity:** Most donors allocate funds from a fixed envelope for total official aid; trust funds have not increased the size of that envelope. As earmarked pots of money with separate approval and allocation processes, trust funds tend to increase transaction costs for client countries and for the World Bank and to impose parallel budgeting and approval processes. That is why the World Bank needs to be selective in what trust funds and what governing procedures it agrees to.

- **Oversight:** Evaluations have found weaknesses in governance and transparency in many partnership programs, as well as frictions and conflicts of interest from the multiplicity of roles that the World Bank typically performs in partnerships. Yet the World Bank has no routine oversight and tracking of partnerships and of how it engages in them.
- **Links to country programs:** The World Bank is uniquely placed to help client countries benefit from global programs. However, there are often missed opportunities at the intersection of the World Bank's participation in global programs and its country engagements. There are no explicit agreements on division of labor between the World Bank and some major global health programs.
- **Results are often unknown:** Although there has been progress in recent years, many partnerships that IEG has reviewed lacked clear goals and indicators. It is often hard to attribute results to specific partnerships let alone assess results across the portfolio.

IEG has recommended ways to help the World Bank address these challenges via internal reforms to ensure selectivity, routine corporate oversight, and policies and standards about partnership governance, engagement strategies for individual programs, empowerment of staff serving on partnership boards, and results frameworks.

Source: IEG 2015.

### **G20 GLOBAL PARTNERSHIP FOR FINANCIAL INCLUSION**

In 2010, the G20 created the Global Partnership for Financial Inclusion (GPFI), an inclusive platform for all G20 countries, interested non-G20 countries, and relevant stakeholders for peer learning, knowledge sharing, policy advocacy, and coordination. It is also the main implementing mechanism for the G20 Financial Inclusion Action Plan, updated in 2014. GPFI began with three implementing partners – the Alliance for Financial Inclusion (AFI), CGAP, and IFC – and later gained the World Bank, the Organisation for Economic Co-operation and Development, the Better Than Cash Alliance, and International Fund for Agricultural Development as additional implementing partners. Queen Maxima, the United Nations Secretary-General’s Special Advocate for Financial Inclusion, is the honorary patron of the GPFI. The GPFI began with three working groups: Financial Inclusion Principles and Engagement with the Standard-Setting Bodies, Small and Medium-Size Enterprises Finance, and Data and Measurement. It can create others as it deems needed. GPFI has been able to organize as a global consultative mechanism and to mobilize funding for key initiatives, including technical support for implementation of the G20 Principles for Financial Inclusion. World Bank experts suggest that GPFI provides an excellent platform for the World Bank Group knowledge and policy contributions to achieve greater influence and a high-level audience within the G20 and beyond (see box 3.1).

A key destination of this funding recently has been Financial Inclusion Support Framework (FISF), a program jointly financed by the Netherlands, the Bill and Melinda Gates Foundation, and the World Bank Group. The FISF is a country-based program financing technical assistance, data and capacity building to assist leaders in national financial inclusion to achieve country-level commitments and targets. It covers such areas as small and medium-size enterprise (SME) finance (not a focal point of this evaluation), financial consumer protection, financial literacy, payments systems, digital payments, and remittances. Rwanda, Indonesia, and Mozambique were early FISF program participants. In 2014, GPFI members created a subgroup on Markets and Payment Systems to promote the use of payment systems for financial inclusion.

### **ALLIANCE FOR FINANCIAL INCLUSION**

The AFI is a global knowledge-sharing network exclusively for financial inclusion policymakers from 90 developing and emerging countries. Its partners include IFC, CGAP, the G20/GPFI, and the Bill and Melinda Gates Foundation. Although AFI offers several types of support for financial sector leaders and regulators, it is especially known as the shepherd of the Maya Declaration, a set of “measurable commitments” that financial institution policy makers can use to establish a national strategy. Under the Maya Declaration, commitments are made in four areas aligned to the G20 Principles for Innovative Financial Inclusion:

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- Create an enabling environment to harness new technology that increases access and lowers costs of financial services
- Implement a proportional framework that advances synergies in financial inclusion, integrity, and stability
- Integrate consumer protection and empowerment as a key pillar of financial inclusion
- Use data for informed policymaking and tracking results.

The AFI comprises 54 institutions representing more than 60 nations with Maya Declaration commitments (as of January 2015). World Bank experts regard the work of AFI as a vital step toward detailed country strategies for financial inclusion, by raising the consciousness and commitment of financial regulatory leaders (often central bank governors or finance ministers) and political leaders. The Maya Declaration is also seen as an appropriate precursor to the FISF. AFI provides resources, peer review, support for M&E, and international conferences in support of its members from 90 developing and emerging countries, including an annual global policy forum. The World Bank Group and G20 both work closely with AFI.

#### CENTER FOR FINANCIAL INCLUSION

The Center for Financial Inclusion, based at the microfinance NGO Accion, is an action-oriented think tank aiming to achieve full global financial inclusion, which is defined as a state where “everyone who can use them has access to a full suite of quality financial services, provided at affordable prices, in a convenient manner, with respect and dignity.” IFC, Citi Foundation, MasterCard Foundation, Visa, the Ford Foundation, the Inter-American Development Bank, and KfW number among its partners. In its vision, these services should be delivered by a range of providers, in a stable, competitive market to financially capable clients. Among its programs are the following:

- *Financial Inclusion 2020* is a research and advocacy project to deepen the shared understanding of what financial inclusion is, where the gaps are and the road map to achieve it. Through extensive consultation, this program establishes recommendations to move financial inclusion forward, with the year 2020 representing an aspirational target to galvanize thought and action. In this initiative, CGAP leads a working group on “addressing customer needs,” and IFC leads a group on credit reporting which, among other things, has brought a higher profile to the principles established by a World Bank task force on credit reporting.
- *The Smart Campaign* aims to embed client protection in the DNA of the microfinance industry. This campaign offers a certification program financial

service providers to provide the tools and resources they need to deliver transparent, respectful, and prudent financial services to all clients. This includes transparency in pricing and terms of services, safeguards against overlending, and providing appropriate services to client needs. Among its sponsors are IFC, the U.S. Agency for International Development (USAID), IDB Inter-American Development Bank's Multilateral Investment Fund, Credit Suisse, Deutsche Bank, the Ford Foundation, and the Small Industries Development Bank of India. This last organization works with the Smart Campaign under its "Responsible Microfinance" initiative to educate MFIs on client protection principles, conduct client protection assessments and to build capacity and strengthening client protection for assisted MFIs.

#### **MICROFINANCE INFORMATION EXCHANGE MARKET**

The Microfinance Information Exchange (MIX) Market has become the premier source of public information on MFIs and their financial and social performance. It collects data from over 2000 MFIs, validates and standardizes it, and provides access to data, analysis, and market intelligence both as a public good and as a membership service. Partners in the MIX market include CGAP (itself a partnership), as well as the Bill and Melinda Gates Foundation, the MasterCard Foundation, the International Fund for Agricultural Development, the Dell Foundation, Citi Foundation and U.K. Aid. The MIX Financial Inclusion Lab publicly provides country-level data on microfinance services for 19 countries so far. MIX data are the most comprehensive and detailed data on MFIs available, and (as can be seen in this evaluation) provides a far higher level of understanding of industry characteristics and trends than would otherwise be available.

#### **THE GLOBAL BANKING ALLIANCE FOR WOMEN**

The Global Banking Alliance for Women is an international consortium of financial institutions and other organizations whose mission is to accelerate the growth of women in business and women's wealth creation, while also benefiting member financial institutions worldwide. It is especially focused on the SMEs, falling somewhat outside the scope of this work. Nonetheless, some of its work is focused more broadly on gender access to finance issues, including generating gender disaggregated data on financial exclusion. Members include IFC, World Bank, CGAP, Citi Foundation, the G20 and GPFI, the Gates Foundation, the Omidyar Network, and UNCDF.

#### **WORLD BANK GROUP INFLUENCE ON STANDARD-SETTING BODIES THROUGH GPFI**

The World Bank Group has been able to have a strong impact on global standard-setting bodies through its partnerships with CGAP and the GPFI (through the



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Regulations and Standard-Setting Bodies subgroup). This work engages with six global standard-setting bodies:

- Financial Action Task Force
- Basel Committee on Banking Supervision
- Committee on Payments and Market Infrastructures
- International Association of Insurance Supervisors
- International Association of Deposit Insurers
- International Organization of Securities Commissions (since 2013).

According to knowledgeable informants, in 2009 and 2010, global standard-setting bodies, influenced by the recent global financial crisis, were focused on restoring and safeguarding stability and integrity, without explicitly considering the potential impact on the poor. The Bank Group and its partners in financial inclusion responded. For example, under the mantle of GPFI, CGAP mobilized both its own expertise and that of “six relevant World Bank technical units” to produce the 2011 white paper: *Global Standard-Setting Bodies and Financial Inclusion for the Poor: Toward Proportionate Standards and Guidance*. This white paper became a broadly accepted reference in efforts to shape global standards in financial supervision to encourage financial inclusion. Through ongoing follow-up, utilizing these partnerships, the work has allowed standard-setting bodies to “own” financial inclusion, making it their own objective. Two concrete results have been:

- The Financial Action Task Force, which is responsible for know your customer (KYC) and related safeguards, acknowledged the risks of financial exclusion in terms of undocumented financial transactions. It accepted a tiered (proportional) system for KYC, applying reduced scrutiny to simple accounts that imposed lower risk.
- The Basel Committee on Banking Supervision has evolved its core principles over time to strengthen proportional principles. Over time, through long-term engagement of CGAP (with the endorsement and input of GPFI and engagement of World Bank experts), IEG learned that most of the recommendations of the 2011 White Paper (now being updated) were accepted by the standard-setting bodies.

### PARTNERSHIPS AS PLATFORMS FOR WORK ON REMITTANCES

The World Bank has exercised intellectual leadership on the topic of global remittances for many years, and in more recent times, has also leveraged global partnerships and platforms to move an agenda. Research presented in chapter 1 indicates that remittances not only improve income for many poor families, but also “are associated with greater human development outcomes across a number of areas

such as health, education, and gender equality” (Ratha 2013, 1). Reducing remittance costs has been one of the focal areas of World Bank’s engagement.

Through the Group of Eight, the World Bank assumed leadership of a Global Working Group on Remittances, authorized in 2007 and created in 2009. This body has worked to generate consensus on lowering the cost of remittances by generating a common foundation of data and knowledge, and by promoting the 5 × 5 objective to reduce the global average cost of remittances by 5 percentage points in 5 years “through enhanced information, transparency, competition and cooperation with partners” (G8 2009, 49). Approved by the G8 and G20 in 2009 and tracked through the Remittances Price Worldwide database hosted by the World Bank, this initiative is credited with stimulating global and country-level reforms that have significantly reduced the weighted average cost of remittances, resulting in tens of billions of dollars of savings to migrant workers and their families.

### Country-Level Engagement for Policy and Sector Reform

This section assesses how well the World Bank Group has helped client countries establish and strengthen the enabling environment for financial inclusion. The assessment is based on a portfolio of Bank Group financial inclusions interventions, desk reviews of five country cases, and five in-depth country cases that included visits to the country and discussions with staff, country authorities and other stakeholders.

For financial intermediaries to thrive and better serve the needs of the poor and unbanked, an enabling environment has to be in place (box 3.2). Such environments must be built in a way that fosters sustainable financial inclusion, delivering a range of quality and affordable financial services that meet the needs of underserved sectors (for example, the poor, women, micro, very small, and medium-size enterprises [MSMEs], and rural areas). Even then there are likely to be potential clients at the very bottom of the pyramid that may not be reachable in a financial self-sustainable manner (that is, covering the economic cost of funding) without the support of at least temporary subsidies.

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**Box 3.2. Elements of a Financial Inclusion–Enabling Environment**

**An adequate framework of proportional regulation and effective supervision** of financial services providers that targets the low end of the market and which are allowed to mobilize deposits is in place. Such a framework should seek to ensure intermediaries’ soundness and the protection of small depositors.<sup>a</sup> When numerous intermediaries are subject to oversight that could overly stretch the supervisor’s resources, an appropriate,

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risk-based, tiered architecture of oversight is in place supporting the effective discharge of responsibilities. Rules and regulations are in place that provide for the transformation of non-deposit-taking financial intermediaries into authorized deposit-taking institutions subject to meeting requirements. Such a framework should help underpin the trust of users of formal financial intermediaries and the evolution of the industry serving the financial needs of the unbanked without overburdening intermediaries with compliance costs that drastically cuts outreach.<sup>b</sup>

**Comprehensive, nonfragmented, reliable, and timely credit information** on borrowers is made available by credit registries/bureaus and is used in credit allocation decisions, including by MFIs. Such services are provided by properly licensed and regulated entities underpinned in legislation providing for borrowers rights. The use of such information in credit decisions along with financially literate consumers can help lessen the risks of overindebtedness and the soundness of intermediaries as incentives for timely repayment of credits are strengthened.

**Simplified, risk-calibrated procedures for account openings**, transactions size, and balances holdings are in place helping overcome identification constraints while safeguarding the integrity (anti-money laundering and combating the financing of terrorism) of the system; and/or national identifications are made available and affordable. Many of the unbanked face challenges in proving their identity and proof of income.

*Source:* IEG staff.

a. Proportional refers to the balancing of risks and benefits against the costs of regulation and supervision. See CGAP (2011).

b. Thirteen percent of Global Findex survey respondents who do not have an account at a formal financial institution identify lack of trust as a reason; see World Bank 2014.

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## NATURE AND EVOLUTION OF WORLD BANK GROUP SUPPORT TO POLICY REFORM

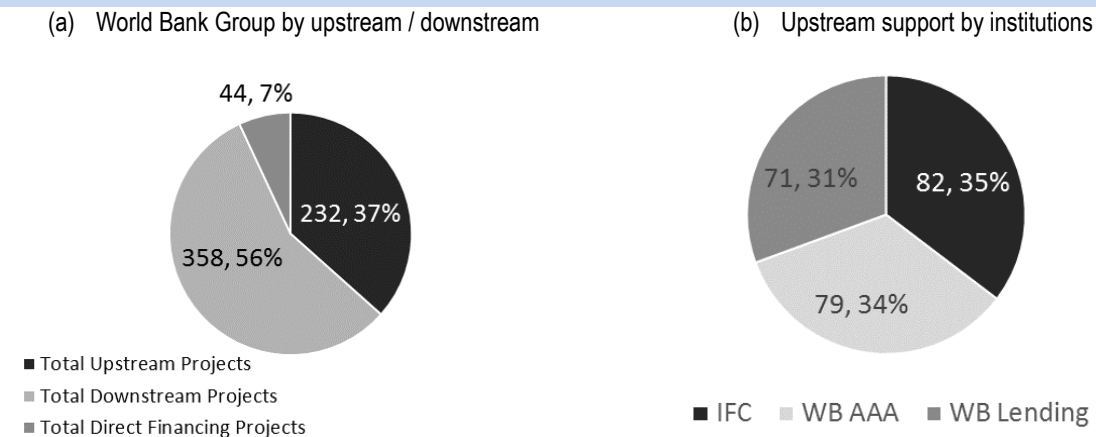
World Bank Group country interventions in financial inclusion have various components. They typically entail components aimed at building or improving the enabling environment, that is, “upstream” components; components that provide financing for on-lending through MFIs, guarantees for such funding, or advice to MFIs, that is, “downstream” components; or a mix of both. This section focuses on projects that have at least one “upstream” component (see box 3.2).

Of the total of 634 financial inclusion interventions of the World Bank Group, about one-third or 232 were upstream support during the period of evaluation—fiscal years (FY)07–13. Upstream interventions are provided by both the World Bank and IFC with two-thirds of the total number of interventions delivered by the former. The World Bank upstream interventions were delivered in roughly equal proportion through lending instruments and AAA. It is not unusual for AAA interventions to be delivered in parallel with lending or preceding lending operations, for example providing advice to authorities on legal and regulatory matters that subsequently are considered in the context of Development Policy Loans.

IFC upstream interventions were delivered through its advisory services. These interventions (IFC Advisory Services) are usually delivered in the context of related investment interventions as a way to establish or strengthen a regulatory framework (for example, when investing in a greenfield MFI and the country lacks a regulatory and oversight framework for this type of intermediaries). Figure 3.1 breaks down the entire World Bank Group financial inclusion portfolio and by institution.

World Bank Group's support to policy reforms focuses on diagnostics and regulatory, legal, and financial literacy issues. In broad terms, the World Bank tends to provide policy advice and technical assistance pertaining to the *broader* financial system (for example, strengthening of banking oversight, reform of the credit cooperative sector), whereas IFC's advisory services tend to have a *narrower* sectoral focus (for example, MFIs) but on many occasions with applications that go well beyond microfinance (for example, credit bureaus). With this distinction of focus in mind, both entities have been active in the provision of interventions with regulatory, legal, oversight, and financial literacy focus. IFC has been quite important in the area of financial infrastructure and financial literacy-related interventions, whereas the World Bank has been active in undertaking sectoral diagnostic work (and advising on the formulation of financial inclusion strategies) in a number of countries. Competition policy and consumer protection issues are rarely addressed (figure 3.2).

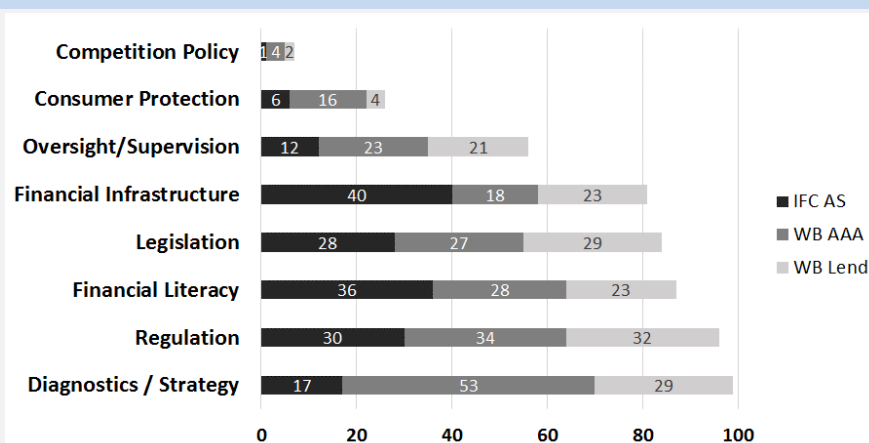
**Figure 3.1. Bank Group Support for Policy Reform for Financial Inclusion**



Sources: IEG portfolio analysis.

Note: The total number of interventions reported above in graph (a) exceeds the total number of upstream interventions as a particular Bank Group intervention may have multiple components and hence may appear more than once in the classification of constraints. The portfolio review classified upstream interventions in country operations by the financial inclusion constraints that were dealt with: Diagnostic and Policy; Legislation; Regulation; Oversight and Supervision; Competition Policy; Financial Infrastructure; Consumer Protection; and Financial Literacy. For example, an intervention could have addressed changes in the laws and regulations governing MFIs, and in their supervisory practices therefore the intervention would be classified under each of the three categories. It is also noted that legislation, regulation, or oversight may refer to MFIs, savings and credit cooperatives, mobile banking, credit bureaus, or other financial service institutions. Thus the total number of interventions reported in figure 3.2 for the areas covered exceeds by a considerable margin the total number of upstream interventions identified in the portfolio review.

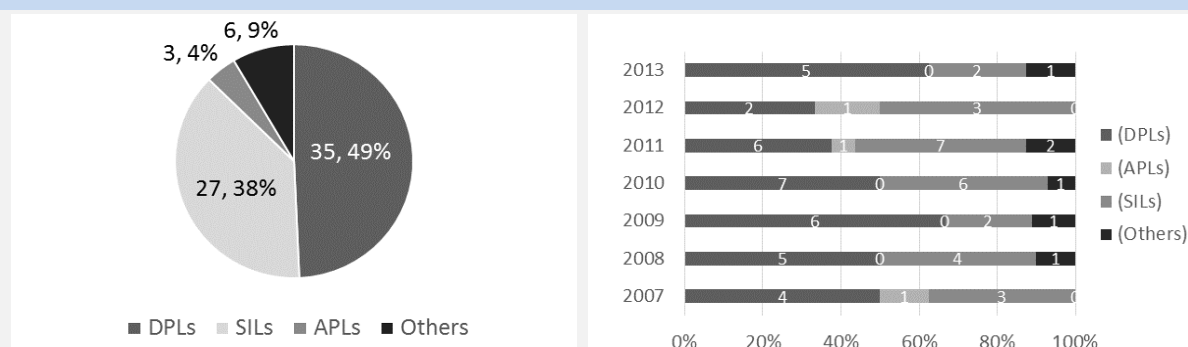
Figure 3.2. Focus Areas of World Bank Group Policy Reform Interventions, FY07–13



Source: IEG portfolio analysis.

On the World Bank side, lending with upstream components was delivered primarily through Development Policy Loans and Sector Investments Loans, averaging about 8–10 projects per year (figure 3.3). The choice of instruments in part reflected the expected length of supported reforms and focus area. Among these operations, Development Policy Loans account for half of the number of operations, experiencing a surge in the context of the global financial crisis. Interventions aiming at structural reforms of long gestation (for example, reform of the credit cooperative sector and its oversight in Mexico) and where it is important to monitor progress over time were implemented under a series of investment loans with sufficient maturity, and when necessary extension of deadlines, to keep policy dialogue and reforms moving even at a slower than anticipated pace.

Figure 3.3. World Bank Lending Interventions by Instrument FY07–13



Source: IEG portfolio analysis.

Note: APL = adaptable program loan; DPL = development policy loan; SIL = sector investment loan.

In addition to lending, the World Bank also provides policy reform support through AAA. Overall, financial inclusion-related AAA represent just over 2 percent of the World Bank's AAA portfolio or 11 percent of Financial and Private Sector Development AAA activities in both number and volume. This AAA support focuses mainly on upstream issues (80 percent) and almost doubled in recent years, FY10–13, compared with FY07–09. Interestingly, the share of non-credited-focused AAA increased as well, amounting to 41 percent recently. The single most important field of activities is informing government policy (25 percent), including providing strategic advice, followed by stimulating public debate and raising awareness (18 percent). An area of particular strong analytical support has been payment systems, remittances, and financial infrastructure; for the future, the World Bank is planning to expand its support through a global program on consumer protection and financial literacy.

Many upstream interventions tended to address several areas at the same time and be tailored to country circumstances. For example, an IFC advisory service in Ghana in the area of credit bureaus approved in FY10 aimed at strengthening the effectiveness of the country's credit reporting system – part of its financial infrastructure. Legislation underpinning the credit reporting industry had been enacted in 2007 with World Bank support, but implementation was not as effective as envisioned, failing to fully realize the benefits of credit information systems. Only informal mechanisms for information reporting (by intermediaries) and sharing (among credit bureaus) were being used, resulting in a fragmented system with incomplete information. Further industry oversight had not been well established, reflecting the lack of Central Bank experience in this area. There was insufficient education of financial services intermediaries and the public on the new credit information system and on how to use credit information in the credit decision process.

The IFC Advisory Services intervention sought to establish a code of conduct to govern relationships among bureaus and creditors and to facilitate its acceptance; strengthen the capacity of the Central Bank to oversee credit bureaus; and to support the credit bureaus and the Central Bank to promote public education on the role and importance of credit bureaus and consumer protection. In the case of an IFC intervention in the Lao People's Democratic Republic on credit bureaus, an overhaul of the sector was required, starting with the need to establish regulations for electronic credit information reporting, the creation of such a system and the training of central bank staff to operate the new system and of the industry to introduce the system and its uses.

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IFC upstream interventions are generally linked to downstream advisory and investment interventions, which are sometimes beneficial but at times have raised the perception of conflict of interest. A successful example of upstream advisory occurred in Liberia. There, IFC had supported the establishment of a commercial greenfield MFI in Liberia in 2007, but there was no legal and regulatory framework in place that would help underpin operations involving this type of intermediary. The IFC Advisory Services intervention sought to help the Central Bank review existing banking law and its applicability to MFI activities, draft legislation and implementing regulations as needed, and build capacity to oversee a new (for the country) type of financial intermediary, while transferring best practice in the oversight of banking and microfinance activities. This timely engagement with the Central Bank was credited with building the authorities' confidence and laying down an appropriate oversight framework that also helped in the process of accepting the MFI's license application.

However, there have been other cases (for example, mobile banking in Indonesia) in which the authorities viewed the advisory services advice as being tainted by potential conflict of interest and they therefore decided to rely on the World Bank for advice on regulatory matters. In other cases, IFC, using its convening capacity, sought to influence regulation of mobile banking and credit bureaus (China).

The World Bank Group country engagement on establishing an enabling environment for financial inclusion has evolved over time. The desk reviews and country case studies show a pattern of engagement that typically started with broad reforms of the financial sector and later on moved more focus in particular areas. This evolution is reflected on how financial inclusion has been couched in country assistance strategy and country partnership strategy documents. Typically, country assistance strategies or country partnership strategies covering the earlier years of analysis (that is, FY06) did not include specific references to financial inclusion or inclusive finance but, rather, financial sector issues were discussed in the context of broad financial sector reform and development (deepening) under the economic growth pillar. In more recent years (for example, 2000), references started to be become more specific about fostering access to finance to underserved sectors including SMEs, the poor, and rural areas. Such references are presented variously under poverty alleviation and economic growth pillars. Finally, more specific references to financial inclusion started to appear more recently (approximately FY10-FY11) under the inclusive growth pillar.

Initial reforms sought to help put in place the broad conditions for financial sector stabilization and deepening and in some cases establish very basic financial sector infrastructures. Such conditions refer to, among other things, the regulation and

oversight of the banking (more broadly financial) system and its stability, the rule of law, basic payment system infrastructure, and the soundness of key financial sector intermediaries. In a country like Ghana, constraints were identified at the level of the banking and financial system regarding prudential regulations and oversight, and financial infrastructure. In other countries like Mexico and India, there were important problems with (absent or inadequate) regulation and oversight and the soundness or governance of whole segments of the financial system (the savings and credit cooperatives [SACCOs] sectors and other types of MFIs).

In Indonesia, for example, the interventions sought to buttress financial sector stability in the aftermath of regional financial crises and then institutional reforms of MFIs followed by the broad reform of the rural and microfinance sectors. In other countries, the reforms supported the privatization or restructuring of state-owned banks (for example, Tanzania). In Azerbaijan, early interventions sought to help put in place the very basic infrastructure for the operation of a financial system, namely a payment system, accounting standards, collateral rules and law enforcement that would lay the foundations for the overhaul of credit systems, including in rural areas, later on. These types of interventions were expected to foster deeper financial systems which research has found supports economic growth and in turn employment generation.

The more focused engagements that appeared later on sought to address specific constraints impinging on financial inclusion but typically centered on the access-to-credit dimension of financial inclusion. For example, in Azerbaijan and China the absence of centralized and/or deficiencies in credit bureaus and the undue reliance on collateral were seen as impediments to access to finance for MSMEs. Similarly, in the case of the Kyrgyz Republic, recent documents identify the need to build a credit information infrastructure and a modern moveable collateral registry to support access to credit to SMEs, and the transformation of the postal office into a deposit-taking financial intermediary with broad geographic coverage. In India, overcoming deficiencies in microfinance credit information systems and achieving adherence to a Code of Responsible Finance were seen as important actions to foster recovery and growth of the microfinance industry.

In Ghana, interventions sought to strengthen the operations of a credit bureau that had been established under the aegis of a law the World Bank Group had supported a few years earlier. In Indonesia, a very important AAA report identified personal identification requirements and lack of collateral as major constraints and, reflecting the country's adherence to the Maya Declaration, the need to develop branchless banking including mobile services.



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#### RELEVANCE OF POLICY REFORM SUPPORT

World Bank Group interventions that aim at creating or improving an adequate enabling environment for financial inclusion, that is, “upstream” interventions, take place in countries that have low inclusion rates. Roughly two-thirds of the countries are low-inclusion countries (see chapter 2 for classification), and about 64 percent of Bank Group upstream interventions occur in these countries. Looking more closely at the various components of upstream work, the percentage of upstream interventions with regulatory, oversight, and legal content rises to just below 70 percent of the respective totals to countries in the first quartile. A somewhat similar pattern, albeit at a much lower scale (in the range of 20–30 percent) emerges for countries in the second quartile, and finally relatively fewer resources are allocated to countries in the third quartile.

A closer look at the World Bank Group’s identification of upstream constraints to financial inclusion in the country cases and desk reviews reveals a mixed picture, with certain areas receiving scant attention. World Bank interventions have identified shortcomings in (or the total absence of) oversight of certain types of financial intermediaries (for example, SACCOs, credit unions) that cater to lower-income segments of the population and frequently operate in rural areas. Country examples include Azerbaijan, China, India, Mexico, and Tanzania, among others. In turn, IFC has identified a few cases where there was no regulatory and oversight framework for MFIs, or the one in place presented severe deficiencies including with regard to prudential treatment of microfinance activities and the capacity of the supervisor to oversee those intermediaries.

Constraints have also been identified with regard to the adequacy of the regulatory architecture to oversee a large number of intermediaries given the limited resources and capacity of the supervisor (for example, Ghana, Tanzania). Several IFC Advisory Services interventions have also identified shortcomings in credit registries and credit bureaus and their legal and regulatory frameworks (for example, Azerbaijan, China, and India) and less frequently in the oversight framework for mobile banking (for example, Indonesia). However, very rarely, if at all, have they identified legal/regulatory constraints associated with branchless (correspondent) banking or with KYC requirements or the extent of competition (or lack thereof) in the provision of financial services to the poor.

Also rarely mentioned are concerns over consumer protection legislation, regulation, practices, and oversight, although adoption of microfinance industry code of conduct has been identified as an issue of focus in a few IFC interventions (for example, in Pakistan and India). Financial literacy is rarely identified as constraint,

but the review found a few countries where it has been a focus (for example, Ghana).

Some of the gaps in constraint identification appear puzzling, given the state of financial inclusion and country characteristics. One such case is Azerbaijan. The Global Findex survey reported that only 15 percent of adults held formal institutional accounts and the rate was much lower in rural areas. Further, close to half the population live in rural areas which are scarcely (if at all) served by banks.<sup>2</sup> It is surprising that in this context there is no discussion of the potential role of branchless banking (bank agents and mobile banking) as a means to increase access, particularly in rural areas. Nor was there any discussion of whether the enabling regulation was in place to support the development of such delivery channels.

Similarly, in the case of Tanzania, where only 30 percent of the population (most of whom live in rural areas) live within 5 kilometers of an access point, there is no comprehensive discussion of the enabling environment for branchless banking which inter alia could help overcome the low density of access points to financial services in rural areas and “bypass” the strict requirement to branch opening. Although there are four mobile network operators (MNOs) offering e-transfers through a nonexclusive network of agents, there is no explicit regulatory framework setting standards for a broader range of products and services (for example, savings, deposits) or providing for the oversight and linkage to payment system infrastructure that would provide stronger underpinnings to the system. However, it is worth noting that, through IFC efforts financed by the Partnership for Financial Inclusion, operators are seeking to achieve system interoperability.

IEG also found several country cases where constraints to financial inclusion had been identified and tackled by the countries on their own and/or with the support of other developmental partners. For example, in the case of Mexico, where informality reaches up to half the labor force, ways needed to be found to allow for opening accounts at various access channels (banking agent, mobile, branch) that would also preserve the integrity of the financial system. A risk-based four-tier system of accounts was developed with a requirement increasing levels of information risk-calibrated to the volume and range of transactions allowed and the channel used to open the account.<sup>3</sup> In Azerbaijan, although the World Bank had identified the lack of a centralized credit bureau and collateral requirements as constraints to foster access to credit to MSMEs, efforts to overcome shortcomings were carried forward by USAID.

However, there are a few country cases where World Bank Group documents report on identified constraints but have no indication of subsequent (timely) interventions

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and, as a result, an imbalance between upstream and downstream interventions can emerge. It is not clear what the reasons may be for a lack of timely follow-up. It is possible that the countries themselves have tackled those constraints without the need of World Bank Group support, but this has not been documented in World Bank Group reports. Perhaps those constraints have not been addressed yet, but that should be noted, too.

For example, in the case of China, World Bank Group documents had identified shortcomings in the capacity of regional governments tasked with oversight responsibility over private MFIs (called microcredit companies) operating in rural areas, but it is unclear that the diagnostic was shared with the authorities or that regional government oversight capacity was subsequently strengthened. This country is an example where most of the World Bank Group interventions were downstream, with a limited set of upstream AAA interventions.

In India, during the initial stages of engagement on financial inclusion covered in the evaluation, the World Bank Group did not identify the absence of an appropriate oversight framework for MFIs as a key constraint and made only limited efforts to push for the development of sustainable financial intermediaries and prudent financial inclusion. For example, the World Bank had encouraged responsible finance through its project with the Small Industries Development Bank of India through voluntary standards. When troubles surfaced in certain states, the regulatory reaction of the State of Andhra Pradesh drastically curtailed the activities of MFIs. A more proactive and timely engagement on the World Bank Group's part might have limited the impact of latent troubles early on and thus avoid the adoption of draconian regulations later.

In Tanzania, SACCOs are subject to a prudential framework but one which is not effectively enforced owing to limited capacity and resources of the overseer and limited capacity of intermediaries to comply with prudential requirements including reporting. There are some 5,800 SACCOs in Tanzania, but it is not clear how sound that system is and what its outreach effectively is because there are no reliable data. At the same time the authorities are seeking to develop stable sources (for example, deposit mobilization) to fund credit; thus, it would seem critical that an updated systematic review of constraints impacting the SACCOs sector (for example, adequacy of regulatory standards, of the architecture of oversight given overseer capacity constraints and risks posed by the intermediaries, and capacities of SACCOs) and the fleshing out of options to address them be undertaken.

By contrast, World Bank support in neighboring Kenya was more successful in creating a viable regulatory environment for SACCOs. The Financial Sector

Deepening Trust, which is supported by the World Bank and other donors, has been credited with having supported the passage of a law and supportive reforms to establish a regulatory framework for SACCOs for improving the regulatory framework for microfinance, and for supporting microfinance institutions through grants.

In most of the country cases reviewed, no government financial inclusion strategy was explicitly laid out or discussed in Bank Group country documents. It would seem reasonable that a systematic identification of constraints would inform the formulation of strategies to which the World Bank could have contributed. Absent such an organizing device, it appears that the financial inclusion constraints identification work has proceed in an unsystematic way. An illustration of this are instances in which IFC in the context of investment services is supporting the setting up of credit bureaus, mobile banking investments, and greenfield MFIs to fill particular immediate gaps in the enabling environment, but there is not comprehensive effort to identify and tackle all relevant constraints impacting the enabling environment.

One exception appears to be Indonesia, where an influential World Bank Group AAA report and the authorities' adherence to the Maya Declaration in 2012 helped lead to the formulation of the National Financial Inclusion Strategy, which identified the establishment of an enabling environment for branchless banking, credit reporting, and no-frills accounts as important components. The World Bank is supporting a growing number of countries to establish such strategies, but this is a very recent phenomenon.

There are country cases where different governmental entities have put forward financial inclusion initiatives, but they appear fragmented and without clear prioritization (for example, India). It does not appear that the World Bank Group or authorities are making systematic use of the Global Findex findings on the reasons survey respondents give for not having a formal financial account to identify priority reforms to expand financial inclusion. At a broader level, formulating an explicit financial inclusion strategy could also help coalesce the political commitment of key stakeholders while likely providing a forum for the World Bank Group to both coordinate (across internal units) and to engage strategically at the highest policy level.

There does not seem to have been any explicit coordination in the endeavor of identifying upstream constraints among the governments, World Bank Group, and other development partners. In countries with strong institutional development and capacities, it seems that such tasks are primarily the remit of the government, which

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takes the initiative and coordinates efforts, with the World Bank playing a supporting/consultative role at times.

For example, in Mexico, identifying the challenges of informality and KYC requirements were tackled by the government interfacing with the relevant standard setter (the Financial Action Task Force) and consulting with experts in the field of banking correspondents. In the case of India, the government drives the financial inclusion agenda and the roles different developmental partners play in support of it. In general, it is not clear what arrangement is in place to ensure that such an endeavor is carry forward in a systematic and comprehensive way, which leaves room for gaps to emerge and duplication of efforts to occur. Once again, the formulation of an explicit financial inclusion strategy would seem to offer an opportunity to tackle the issue. The new instrument of the FISE, aimed to develop a national approach to expand financial inclusion through enabling the achievement of country commitments and targets, may offer a more systematic approach.

In some cases, there were opportunities missed to productively collaborate across World Bank Group entities. For example, when IFC takes an investment position or provides advisory services to a company, it is not always clear whether it takes as given the regulatory framework or an assessment of its adequacy is considered. For example, in Pakistan, IFC appears to have been successful in helping establish a credit bureau for MFIs, but it is not clear whether there had been an analysis by the World Bank or IFC (or another independent entity) of the adequacy of the legal and regulatory framework for that activity.

At the same time, there are cases (for example, India) where IFC used its advisory work and convening power to push the adoption of industry standards for credit reporting by nonbank financial companies. Although such an IFC action could certainly be beneficial for the sector and consumers, it run the risks that it may be perceived as tinted by conflict of interest. In those cases, it would seem that if the World Bank were to be engaged in providing advice on the matter, it could be better received by country authorities.

Strong analytical pieces on the state of financial inclusion in the country including the identification of constraints can set the stage for productive policy dialogue with the authorities and key stakeholders for several years. In the case of Indonesia, a World Bank AAA report “Improving Access to Financial Services in Indonesia” (World Bank 2010) is considered to have played an important role in shaping the national financial inclusion strategy and agenda of the government. Drawing on a dedicated survey, the report identified constraints—documentation requirements and lack of collateral—from the perspective of (potential) consumers, quantified

access gaps in financial products (savings accounts) and services both from the demand and supply side. Some results surprised the authorities (for example, only half the population have access to financial services notwithstanding having one of world largest microfinance banks, Bank Rakyat Indonesia's Unit Desa system) triggering reexamination of the approaches hitherto taken to financial inclusion.

In India, the AAA report "India – Scaling-Up Access to Finance for India's Rural Poor" (World Bank 2004) and the activities surrounding it (including workshops with high-ranking government officials) were strongly influential in stimulating a heightened attention and activity in delivering financial services to the poor, rural citizens, and women. It built on a survey of rural households and background papers, conferring the World Bank significant stature, visibility, and credibility with the government. It laid the analytical foundations for subsequent World Bank engagements with the government in areas ranging from self-help groups and their linkages to commercial banks to microfinance to crop microinsurance but was not followed up with a similarly comprehensive or influential analytic work since.

In principle, the joint World Bank-International Monetary Fund Financial Sector Assessment Program (FSAP) provides an analytic vehicle for a stock taking of the state of financial inclusion in member countries, the identification of constraints, and the formulation of recommendations. In practice this has rarely been the case, as the treatment was not comprehensive, based on a standard and recognized framework, and/or sufficiently detailed and data-driven to mobilize relevant parties to action (box 3.3).

### **Box 3.3. FSAP and Its Application to Financial Inclusion**

The evaluation finds that discussion of financial inclusion-enabling environment issues vary greatly in terms of coverage and depth of treatment in the desk review and country study cases. In 8 of 10 cases covered in-depth in this evaluation, there is an accompanying technical note focusing on such issues in detail, which provides background and analysis presented in the FSAP's missions' Aide Memoires (not made public) and Financial Sector Assessment reports (public).<sup>a</sup>

Coverage ranges from quite limited treatment of the issues in the cases of Indonesia (2009) and Pakistan (2010) – where perhaps concerns over financial system stability trumped other considerations – to fairly comprehensive discussions in the case of Kyrgyz Republic (2013) and Ghana (2011). In the case of the former, the FSAP focused on oversight of MFIs, access to finance and certain infrastructure issues and notably aspects of consumer protection and financial literacy in light of cases of serious abuse by MFIs. In the case of the latter, it covered legal and regulatory frameworks, market infrastructure, the gaps in effective oversight of credit unions, and the scope for regulatory arbitrage. In other cases, the treatment is fairly narrow, for example in India where the technical note

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focuses exclusively on three ongoing initiatives of the BRI. In other cases, the coverage is fairly comprehensive, but important gaps appear in the analysis. In Kenya (2010), the FSAP had a fairly comprehensive discussion relevant to country circumstances (for example, challenges implementing recently enacted legislation on credit bureaus, SACCOs, and MFIs) but with some important gaps in coverage, for example, no discussion of the regulatory challenges associated with agent exclusivity and competition in mobile payment services. Similarly, in the case of China, the treatment is fairly comprehensive on a range of issues (for example, the shift to commercially oriented provision of services, mobile banking in rural areas), but there is little discussion of the adequacy of the oversight framework for nonbank financial institutions, particularly relevant in light of the role of local governments in that regard.

In most cases, the recommendations regarding the enabling environment appear to be clearly driven by the need to overcome identified constraints but the degree of specificity varied. For example, in the case of the Kyrgyz Republic, emphasis is given to the need to develop the role of financial agents and mobile banking and to the supporting regulatory environment to overcome barriers to financial inclusion associated with the geography and low population density in rural areas. In the case of Mexico, FSAP Update recommendations focused on the need to develop an effective exit mechanism to help bring the ongoing restructuring of financial cooperatives framework and the need to adjust branchless banking pricing policies to help realize the opportunities for financial services delivery innovation that the regulatory framework creates room for. But in other cases it is not that clearly apparent the strength of the case made in the reports put forward for some of the recommendations (for example, in India regarding the call for passage of the MFI law). There are also cases where the discussion and recommendations are couched at the broader level of the financial system like in Azerbaijan (2004) reflecting the need to put in place some basic infrastructure (for example, accounting, financial reporting) and oversight frameworks (for example, nonbank financial institutions – MFIs and credit unions), but at the same time pointing to areas for development later on (for example, payment infrastructure in rural areas).

Overall, there is a need to develop a comprehensive and systematic assessment tool that covers all elements of the enabling environment. No doubt there are country circumstances where it would not be appropriate to engage in such systematic assessment, for example, when there are clear signs that the stability of the financial system is in peril and hence relevant focus would be in avoiding falling into crisis or ensuring adequate preparation for it. In most other cases and where the indicators for financial inclusion show significant deficiencies, provision should be made under the FSAP (perhaps under its developmental module) to undertake such assessment in particular drawing on demand-side survey findings that now cover an ever growing number of countries (Global Findex). Such assessments should among other things tackle adequacy of regulation of intermediaries catering to the bottom-of-the-pyramid, branchless banking (agent or mobile), KYC regulations, infrastructure (credit information and payment system), and consumer protection/literacy from the perspective of financial inclusion. Many of these issues are already covered in FSAPs so the challenges is to systematically draw the implications of those assessments for financial inclusion in a

sharper way. At the same time, financial inclusion implications should be borne in mind when putting forward recommendations in those other areas.

*Source:* IEG staff.

a. The 80 percent frequency in technical notes for FSAPs found in the sample of countries reviewed in this IEG evaluation exceeds the about 60 percent country coverage found by the Finance and Markets Global Practice. They looked at all FSAPs that have been undertaken since the inception of the program through 2013.

## **RESULTS AND DRIVERS OF SUCCESS AND FAILURE**

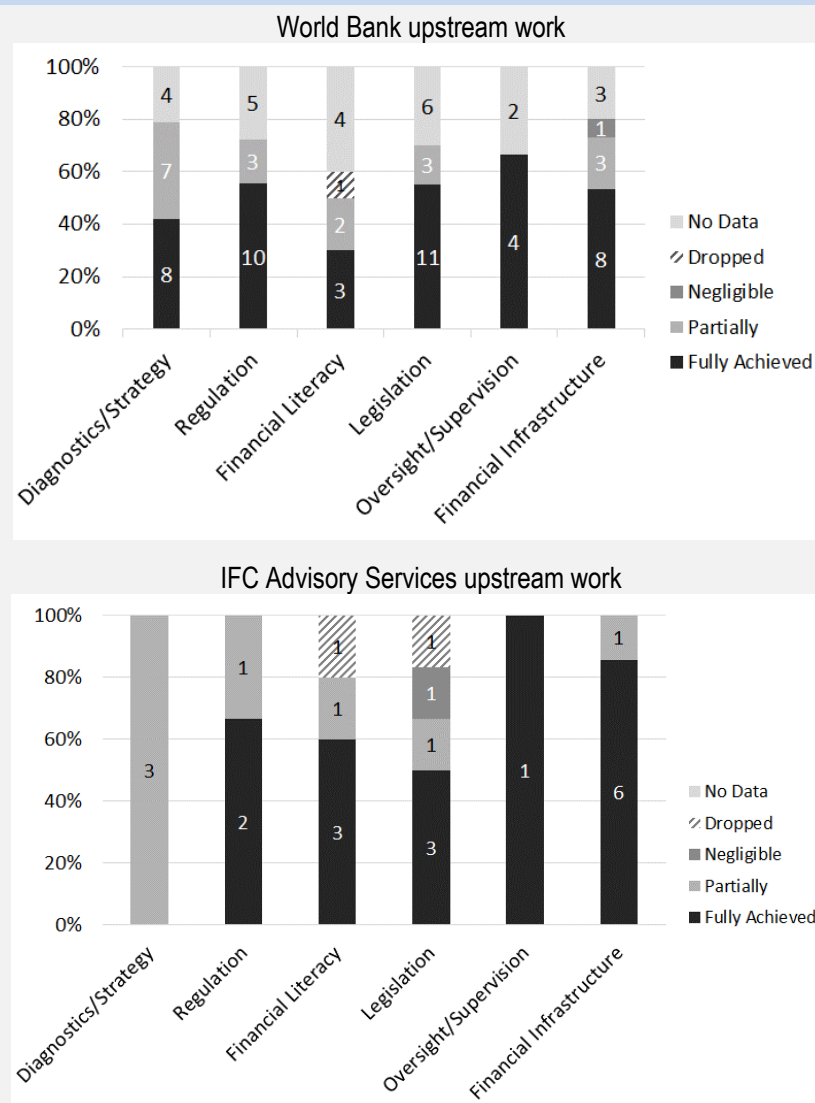
On balance, World Bank Group upstream interventions appear to be broadly effective (figure 3.4). In most areas of upstream involvement, the objectives have been fully achieved in more than half of the cases. For both the World Bank and IFC, interventions focused on oversight, regulations and financial infrastructure obtained the best ratings. Financial literacy interventions for the World Bank and financial inclusion strategy interventions for IFC Advisory Services are the two areas of involvement where effectiveness has most substantially faltered. It should be noted that close to one-third of the World Bank upstream interventions lack sufficient data to judge their effectiveness.

The desk and country cases studies reveal a more nuanced assessment of the effectiveness of World Bank Group upstream interventions. There are areas of involvement where interventions proved to be quite effective in certain country cases but far from it in others. They also show the importance of properly sequencing upstream and downstream interventions and of taking a more holistic approach to the identification and tackling of constraints.

It has proved challenging to successfully put in place a prudential and oversight framework that allows for the mobilization of savings by financial institutions that cater to the low end of the income pyramid. Having such a framework in place is consequential for realizing the benefits of financial inclusion associated with savings products. Research has documented this to be the case. But the standards (for example, managerial, governance, prudential) that financial intermediaries are required to meet to be allowed to mobilize savings are understandably demanding, including for the larger member-type intermediaries (for example, credit unions and cooperatives). Interventions typically had to contend with a large number of intermediaries with poor managerial capacities, very weak governance and accounting practices and very troubled financial soundness indicators. At the same, the supervisory agencies needed major strengthening or new agencies needed to be created.



Figure 3.4. Effectiveness of World Bank Group Policy Reform Interventions



Source: IEG portfolio analysis.

The effectiveness record is mixed. Among the successful cases are interventions in Mexico, which started in the early 2000s with the drafting of sector law and the support for its implementation that included the restructuring of the sector and financial intermediaries – operations, governance, products and services, and outreach – and the strengthening of the supervisor. At the outset of the process there were more than 600 SACCOs and other types of MFIs that came under the aegis of the law and the financial sector prudential regulator, with very few coming close to meeting the new law’s requirements. Ultimately, many institutions were successfully reformed, and currently more than 140 SACCOs and close to 50 popular financial societies, a type of MFI, have been authorized by the prudential regulator

to operate. The supervisor has implemented a risk-based approach to oversight with the support of an Apex institution.

Overall, the sector displays adequate financial soundness indicators and a healthy expansion in the number of clients and product, but some challenges remain. The World Bank Group has also had a long engagement with India in the reform of rural credit cooperative banks and the strengthening of microfinance sector oversight, including support for the development of the credit information system. Although the efforts achieved substantial reforms, the longer-term impact is not clear yet. In the case of Kenya, following the support to draft and enact sector legislation efforts at formalizing intermediaries have shown some success with 83 SACCOs and six deposit-taking MFIs licensed.

However, there are still weaknesses in oversight and capacity of responsible agencies. In the case of Tanzania, World Bank intervention to support the development of community-based savings and credit intermediaries like SACCOs has shown very limited results reflecting the challenges posed by the very large number of entities (some 5,800 SACCOs), and the limited resources and capacity of the supervisor.

A similar mixed record of effectiveness has been registered in interventions that support the adoption of a regulatory framework that provides for the transformation of prudentially unregulated MFIs into regulated deposit-taking MFIs. This type of transformation allows an MFI to widen the range of financial products it can offer—which typically is some form of credit—to include deposit taking (transactional and savings) while diversifying its sources of funding beyond, for example, grants and equity. In the case of Azerbaijan, the World Bank had supported the enactment of legislation in 2010 that provides for credit unions and MFIs' transformation into joint-stock company allowed to mobilize deposits. However, so far very little progress has been achieved as the regulator's concern over weak governance practice and capital adequacy of these entities has yet to be assuaged thus limiting the growth of rural financing. IFC was effective in supporting the transformation of some NGOs into prudentially regulated intermediaries, for example, in Pakistan.

There is also a mixed record in the somewhat related area of transforming state-owned entities into financial services providers catering to low-income clients. An important success was achieved in the World Bank-supported privatization of a loss-making, multipurpose state-owned bank in Tanzania, creating the National Microfinance Bank as a self-sustaining institution focused on microfinance. This institution has emerged as a commercially viable and very important microfinance

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service provider with a network of branches across the country. The transformation of the post office in Azerbaijan as a financial service provider from just payment and transfer services into also a deposit-taking institution proves more challenging than anticipated and dialogue is still ongoing to secure an international partner to assist Azerpost in becoming a more advanced financial service provider.

In the case studies, interventions supporting the establishment and regulation of infrastructure like credit bureaus have been more effective. Ghana provides a good example of the benefits of proper sequencing and collaboration across World Bank Group entities in helping put in place elements of an enabling environment. The World Bank provided support for the drafting of the Credit Reporting Act of 2007, with a private credit bureau licensed in 2008 – credit reports started in 2010. IFC provided technical assistance and education to key stakeholders in the use of credit information and in drafting a code of conduct. Most of the intermediaries that are required to provide information to the bureau are doing so, and the depth of credit information index in the World Bank’s Doing Business rankings jumped from 0 in 2009 to 5 in 2013. Similarly in India, IFC has been instrumental in the development and adoption of a code of conduct by the microfinance industry association that also “governs” credit information. Building on its advisory work, IFC also helped stakeholders to convene a meeting that produced a commonly accepted (and now universally applied) credit information format for nonbank financial companies, comprising most of the MFI industry.

A range of factors seem to underpin the more successful and the less successful upstream interventions:

- *Broad financial sector reforms* early on appear to have set the stage for subsequent engagements with a sharper focus on financial inclusion objectives (for example, improving access to finance to SMEs, underserved sectors of population – poor, women, rural), for example, in Mexico, Indonesia, and India.
- Where a fairly *explicit national financial inclusion strategy* has been articulated by the government (with or without the World Bank Group’s support), that has served as a reference point for more holistic approaches to setting up an enabling environment for financial inclusion. For example, in Indonesia, where a World Bank AAA report was influential in shaping the strategy, a broader range of interventions has been or is being pursued by the World Bank Group than is typically the case. Such a broad approach, which aims to overcome a host of constraints, includes interventions dealing with regulatory reform in agriculture finance, credit reporting and secured transactions registries, and “branchless” banking. In contrast, there are cases

where clear constraints to financial inclusion have not received sufficient attention by the World Bank Group, for example in setting up an enabling environment for rural finance and “branchless” banking in Tanzania.

- Lasting *government commitment* in conjunction with a flexible instrument for policy, technical assistance, and financial engagement played an important role in the restructuring of the popular savings sector in Mexico which has taken more than a decade to come about. The flexibility was important, among other things, to adjust the expiration period and amount of loans as the transformation of a large number of member-based financial intermediaries tends to be a protracted process. Absent such political commitment, progress in implementing a financial inclusion agenda can be stalled for years (as was exemplified in Tanzania until recently).

The approach hitherto taken by the World Bank Group regarding the identification and tackling of constraints to financial inclusion is neither systematic nor comprehensive. There is little evidence of World Bank Group activities geared toward the systematic and timely identification of regulatory, legal, or oversight constraints that could be impinging on the development of financial inclusion.

To be sure, there are country cases considered in this evaluation where the World Bank Group played a significant role in identifying major legal and oversight gaps (for example, credit cooperatives in Mexico) and in supporting the authorities in effectively addressing those gaps. It is less clear however that such an identification was part of a holistic assessment of the adequacy of the various elements (for example, intermediaries, credit information bureaus, registries, consumer protection, and payment systems) that support financial inclusion. The diagnostics of payment systems, remittances, and financial infrastructure were an exception in this regard.

In select countries, these were systematically covered through assessments at the country level, including in FSAPs. In addition, a range of global survey tools have been used including the Global Payment System Survey, a biannual survey among central banks to collect information on the status of payment and settlement systems; and the Remittance Prices Worldwide, a website providing data on the cost of sending and receiving remittances. *It is possible that in some country cases, the lack of traction in policy dialogue at the strategic level (for example, India) may have contributed to the absence of a coherent national strategy for financial inclusion.*

At the same time, this is also consistent with the fact that the World Bank Group had no dedicated tool in its financial inclusion tool kit designed to provide such an assessment. For example, though a range of financial inclusion issues are covered

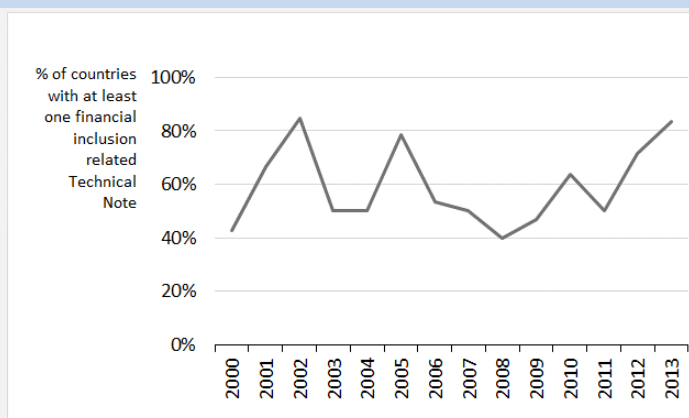
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under the FSAPs, it is seldom the case that a systematic and holistic approach is taken to assess the adequacy of the legal, regulatory, and oversight framework in support of financial inclusion. FSAPs systematically assess regulatory frameworks and supervisory practices in banking, insurance, capital markets, and other areas (such as anti-money laundering and combating the financing of terrorism, payment and settlement systems), but they do so from a stability perspective. Furthermore, unless financial intermediation targeting the lower end of the pyramid is conducted by banking institutions, an assessment of the adequacy of the oversight of such activities undertaken by other types of financial intermediaries – for example, MFIs, savings and loan cooperatives – is unlikely to be undertaken unless they may be thought as potentially posing a threat to financial stability.

From 2000 to 2013 about 70 percent of the countries that have performed an FSAP have also undertaken at least one assessment through technical notes covering aspects related to financial access, SME finance, financial infrastructure, or other financial inclusion-related issues. Financial inclusion related technical notes were particularly prominent 2002 and 2005, followed by a weakened demand for them during crisis years of 2008–09. In 2013, financial inclusion-related technical notes were back to the 2002 level, according World Bank Group's own analysis (figure 3.5). The focus of these technical notes was mainly on general access to finance and SME finance (39 percent), financial infrastructure (29 percent), and housing finance (19 percent). Microfinance and credit unions were less frequently the subject of the analysis, that is, in 10 percent and 3 percent of cases, respectively. Thus, the overall picture is of spotty and inconsistent coverage, especially in terms of services to poor households and microenterprises.

**Figure 3.5. Financial Inclusion Related Technical Notes in FSAPs**



Source: World Bank database.

When looking at how often financial inclusion–related terms were used in FSAPs, this World Bank Group analysis found an increase in the occurrence of such terms. In this context, it needs to be recognized that the World Bank is also in the process of ramping up its analytical support in the areas of consumer protection and financial literacy. In addition to the Global Survey on Consumer Protection and Financial Literacy, the World Bank has programmed 27 advisory services and analytical support projects globally to diagnose consumer protection and financial literacy aspects at client countries, with completion dates FY18. This is a quite sizable program, given that the World Bank Group traditionally implemented about 25 AAA projects per year during FY07–13. However to date, IEG found that there are FSAPs where reviews of consumer protection practices and credit information systems have been undertaken, but their findings are not integrated into a comprehensive financial inclusion diagnostic.

The momentum of increased attention to financial inclusion topics could be seized to continue to develop—and eventually implement—a more holistic and systematic diagnostic tool. Such a diagnostic could be used in country work at a time when a World Bank Group major intervention with significant financial inclusion content may be set to start or it could be conducted at certain time intervals (for instance, five years) to take stock of evolving challenges and the emergence of new products and businesses. The lack of a systematic diagnostic is a particular concern in areas where prudential regulations would not be applied. With the growing importance of mobile technology, for example, stability and consumer protection issues related to MNO-led mobile financial services systems will have to be incorporated in country diagnostics. As many of the yet-unbanked live in rural areas, SACCOs, which are of particular importance for the rural poor, will have to be covered by such assessment frameworks as well.

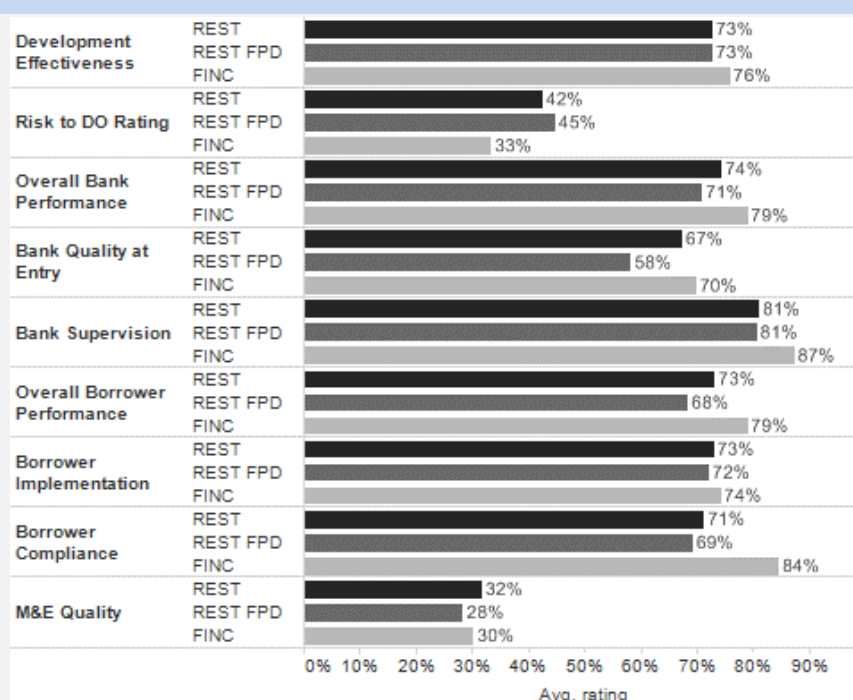
Work quality of World Bank lending in support of policy reforms was generally strong. Almost 88 percent of projects were rated satisfactory for quality at entry and strong supervision. Only M&E lagged, with only 56 percent of projects rated at least moderately satisfactory. Looking at the potential drivers of development outcomes, financial inclusion projects are as effective as or more effective developmentally than other Finance and Private Sector Development projects and the rest of the World Bank portfolio. Overall World Bank performance on these projects is strong, quality of entry is better than average, and supervision and borrower performance and compliance are excellent. Even the weakest characteristic for upstream financial inclusion projects, M&E, is no worse than the one of the rest of the FPD portfolio (figure 3.6).

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The World Bank's self-evaluation of its AAA work finds it be fairly successful in stimulating policy reform. AAA work is not subject to a rigorous evaluation regime, including an independent validation. World Bank self-evaluations activity completion summaries, exported from an internal database, hence provide the sole guide of quality and results. These self-ratings indicate success in about 70–80 percent of cases, with the exception of a few areas that stood out: supporting the preparation of new loan was highly successful in about 90 percent of cases; by contrast, shifting donor policies was only successful in half of the 16 cases.

**Figure 3.6. Work Quality Factor of World Bank Lending for Policy Reform**



Source: IEG portfolio analysis.

The evaluation has documented several instances of valuable IFC Advisory Services interventions fostering the establishment of important elements of an enabling environment. Some of these instances include when IFC investments into credit bureau entities revealed the need to upgrade the regulatory framework for financial contracting infrastructure. Although in some cases IFC was viewed as an “honest” interlocutor by country authorities, there were instances where that was not the case. Nevertheless, there is important value in the identification of regulatory shortcomings and hence in bringing such findings to the attention of World Bank colleagues that may be working on financial inclusion issues in the country.

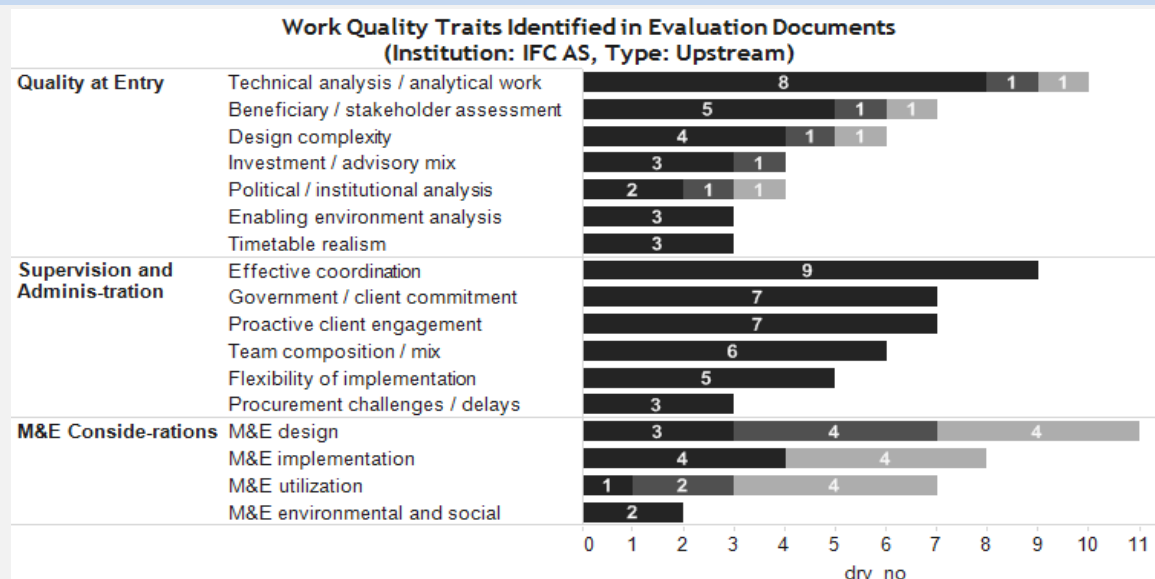
With the reorganization of work under the global practices, much of the staff providing “government-facing” advisory services has moved into the Finance and Markets Global Practice. Thus, it will be all the more important that any information exchange between IFC investment and those providing government-facing advisory services be done in a structured way so that it does not fall through the cracks even while observing safeguards against conflict of interest.

Similar to the World Bank, IFC’s work quality was also high for upstream advice. At quality at entry stage, adequate technical analysis or analytical work and sound beneficiary or stakeholder assessment were identified as the most critical factors across different IFC Advisory Services upstream interventions (figure 3.7). For example, India’s Omidyar project for a microcredit registry benefited a great deal from a sound technical analysis. Similarly, the success of the warehouse receipts project in Indonesia (financial infrastructure) can be greatly attributed to the sound technical analysis at the time of “entry.” The analysis reflected in the sound design complexity and took into account the status of warehouse facilities in the country, existing market infrastructure, the agribusiness sector among others – all of this analysis being imperative for the needs assessment and the subsequent delivery of benefits to the project beneficiaries.

It is worth noting here that most of the technical analyses for these projects were closely associated with beneficiary needs assessment, and that’s why assessment was identified as the second-most recurring driver in the evaluated upstream advisory services projects. Bank Group-wide collaboration plays a key role in the success. The Climate Innovation Center project in Ethiopia is an example of that close collaboration, where the World Bank provided funding to the National Bank of Ethiopia for the upgrade of its system, and IFC provided the advisory services. Again, an adequate technical analysis during the time of entry ensured the quality at entry and the eventual success of the project.



Figure 3.7. Work Quality Factor of IFC Advisory Services Support for Policy Reform



Source: IEG portfolio analysis.

During supervision and administration, effective coordination and securing government commitment and proactive client engagement were seen as the drivers of success. Most the projects mentioned, including in Cambodia, Ghana, India, and Indonesia, benefited from effective coordination between the various stakeholders involved in the interventions. This included but was not limited to clearly defining roles and responsibilities of both internal and external stakeholders, proactive follow-up and combined responsibility toward the smooth implementation of the projects. A relevant example of this was the iScore Egypt project, for which IFC Advisory Services helped the first private credit bureau in Egypt to smoothly roll out its services. A major contributing factor of success for this project was the effective project management, and coordination with all stakeholders involved, including bilateral organizations like USAID.

However, the lack of an adequate M&E design, implementation, and utilization made it difficult to attribute success of IFC interventions. This was the case in at least five projects, where it was determined that M&E considerations were inadequate, and were mixed or average in four advisory projects. In most of the cases, weak M&E only distorted the understanding of IFC's contribution toward impact achievement in relation to upstream financial inclusion objectives. However, there were cases like the ATF-Cambodia CMA Advocacy, where the weak M&E considerations ended up becoming a contributing factor to the failure in achieving the regulation and legislation objectives of the intervention.

## Conclusion

The World Bank Group has been able to leverage its impact at the country level through global partnerships. Partnerships clearly extend the reach, resources, and influence mobilized to promote access to financial services by the poor and microenterprises. Organizations like GPFI, CGAP, AFI, and the Clinton Global Initiative have a strong standing with relevant stakeholders, and can provide opportunities for knowledge sharing, policy influence and piloting and disseminating innovative approaches. Sector leaders in the World Bank and IFC make clear that partnerships play a large role in the World Bank Group's goal of universal financial access and longer-term inclusion goals as well. At the 2015 Spring Meetings, President Kim stated that, to promote financial access, "The World Bank Group's role is to convene and energize a coalition of partners – and also to step up our work."

The World Bank Group has been able to have a strong impact on global standard-setting bodies through its partnerships with CGAP and the GPFI (through the Regulations and Standard-Setting Bodies subgroup). This work engages with six global standard-setting bodies: the Financial Action Task Force; the Basel Committee on Banking Supervision; the Committee on Payments and Market Infrastructures; International Association of Insurance Supervisors; International Association of Deposit Insurers; and (since 2013) International Organization of Securities Commissions.

At the same time, these partnerships bear costs and risks: they require resources and senior staff of the World Bank Group, can inhibit or dilute its own "branding," and may at times pursue goals or methods not squarely aligned the World Bank Group's own strategy. Partnerships involve compromise and coordination. In the absence of results frameworks or rigorous quality control, there can be reputational risks. Recognizing the necessity of such partnerships to achieve its objectives, the World Bank Group should nonetheless encourage its partner organizations to adopt high standards, especially with regard to their accountability and learning systems of the partner organizations. CGAP has only recently developed a clear results framework, and IEG did not come across results frameworks, independent reviews, or evaluations of other partner bodies, beyond a progress report.

With regard to the World Bank Group's country-level engagement on policy reform, IEG concludes that the World Bank Group plays a significant role, but that its approach to identify and tackle constraints to financial inclusion is neither systematic nor comprehensive. The World Bank Group played an important role in identifying major legal and oversight gaps and most project were also executed with

### CHAPTER 3

#### POLICY REFORMS THAT SUPPORT FINANCIAL INCLUSION

good work quality. AAA work delivery is an important and often successful contribution to the policy reform process, based on World Bank's own self-rating scheme.

However, it is questionable whether the identification of constraints and priorities was part of a holistic assessment of the adequacy of the various elements of the financial inclusion framework. Some areas, such as retail payment systems, remittances and financial infrastructure were covered by structured surveys or recurrent diagnostics. In other areas, stronger analytical support is planned, such as in the area of consumer protection and financial literacy. At the same time, there is no dedicated tool in the World Bank Group financial inclusion tool kit designed to provide this type of assessment in a comprehensive manner. Currently, the World Bank Group is in the process of developing potentially important instruments such as the FISF and a new template for a financial inclusion module of Financial Sector Advisory Programs. The lack of a systematic diagnostic is of particular concern in areas where prudential regulations would not be applied.

Given the emergence of new technology as a potential solution such diagnostics would have to address also stability and consumer protection issues of MNO-led mobile banking systems—currently not systematically part of a country assessment. For the rural poor, SACCOs often matter; yet the World Bank Group's country diagnostic pay uneven attention to these important financial inclusion tools. Therefore, it would seem appropriate that the current increased attention to financial inclusion is seized to develop and implement a holistic and systematic diagnostic tool for financial inclusion.

IFC Advisory Services interventions were valuable in fostering the establishment of important elements of an enabling environment, such as financial infrastructure and financial literacy. Such projects benefited from high-quality analytical work and stakeholder assessments and were often executed in sound collaboration across the World Bank Group. However, lacking an adequate M&E system made attribution of success to IFC interventions difficult. In view of the recent restructuring, it is assumed that these interventions are now to be executed by the Global Practices and not by IFC Advisory Services. IFC Senior Management envisages IFA Advisory Services mandates being linked to investment opportunities, which is difficult to argue for upstream interventions. Going forward, it thus appears warranted that such mandates not be dropped but rather that adequate funding mechanisms be found. To the extent that some Advisory Services functions have migrated to World Bank Group global practices, lines of communication should be built (with appropriate safeguards) to assure that information generated from investment operations usefully inform upstream work.

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<sup>1</sup> CGAP's outcomes or impacts have to date not been rigorously evaluated due to lack of any results management framework or activity or project level evaluations and IEG validations thereof. In fact, the 2011 IEG assessment pointed at the weak M&E system and that the development of a results management system would be on its way.

<sup>2</sup> Banks are the only authorized deposit-taking intermediary. Eighty percent of their branches are located in urban areas.

<sup>3</sup> This case offers an interesting example of the importance of taking a holistic view of constraints and the importance of addressing them in a self-reinforcing fashion. The regulation of banking agents and mobile banking without the simplified account opening procedures in conjunction with the no-frills accounts would likely have a much more limited impact in reaching out to the unbanked.

## 4. Did Financial Inclusion Interventions Deliver to the Poor?

### Highlights

- ❖ Overall, World Bank lending activity heavily focuses on the most excluded countries. Though the majority of technical assistance focused on credit, a significant—and slightly increasing—share focused on payments, savings, and insurance.
- ❖ The World Bank has not reconciled its approach to subsidization nor adopted a uniform philosophy across networks (now global practices) and activities.
- ❖ The investments of the International Finance Corporation (IFC) in financial inclusion are small, but they occur in markets where they matter. They struggle with achieving adequate business performance but exhibit remarkable private sector development effects and good economic sustainability. The root causes for their low profitability are higher start-up costs and slower loan growth. IFC's work quality was good.
- ❖ Microloans are a relatively small services line of IFC-supported banks, accounting for 5–10 percent of their mixed loan portfolio, with the rest supporting client taking out larger loans, including small and medium-size enterprises. This is not necessarily a bad thing if it strengthens financial markets. At least small and medium-size enterprises are likely to benefit from such loans—and eventually microenterprises may benefit from the strengthening and deepening of the smaller end of the commercial finance market.
- ❖ IFC advisory projects helped build microfinance institution capacity, assisting in transformation into licensed banks and in the development of new products. They stand out for their high-impact achievement—at least in relative terms.
- ❖ The small number of countries with financial inclusion strategies in place during the portfolio period suggests a lot of potential for gaps, lack of complementarity and sequencing, and ad hoc-ism. A continuing challenge in evaluating downstream interventions across the entire World Bank Group is the lack of information on impact at the beneficiary level.

This chapter examines if and to what extent the World Bank Group support to the provision of financial services has improved access to financial services to low-income households and microenterprises. The analysis focuses on financial inclusion interventions that provided advice to microfinance institutions (MFIs) or funding for the provision of services, either through line of credits (to apex institutions or directly to MFIs) or through direct investments in MFIs. Collectively, these interventions are called “downstream support” to differentiate them from upstream policy support, treated in chapter 3.

Organizationally, the chapter covers interventions of the World Bank, International Finance Corporation (IFC) Advisory Services that target MFIs,<sup>1</sup> IFC investments, and

guarantees by the Multilateral Investment Guarantee Agency (MIGA) in support of MFI financing. None of MIGA's guarantee projects have yet been evaluated; hence, the analysis can only look at portfolio data and cannot present an assessment of MIGA's effectiveness. Chapter 4 concludes with an overview of World Bank Group activities outside the credit space. Because of the rapidly growing importance of technology in financial inclusion, the section on payments strongly focuses on mobile money and mobile financial services (MFSs).

To assess the success and learn from these interventions, the analysis within each section is presented stepwise. First, for each institution the type of interventions are presented and then their development outcomes assessed. Once all institutions have been discussed (World Bank, IFC investment and advisory, and MIGA), their ultimate effects on the provision of financial services are discussed based on the available data.

The extent to which the World Bank Group has supported countries with financial inclusion interventions during the last six years did not necessarily reflect in changes in financial inclusion, when analyzing the correlation of Bank Group interventions with Findex data 2014.<sup>2</sup> For the entire World Bank Group portfolio, Bank Group projects broadly did better in countries with more financial depth and better credit information; however, there is no statistical link between the development outcome of financial inclusion projects (a much smaller subsample) and these explanatory variables. Looking at the Findex data from 2014, financial inclusion went up for the bottom 40 percent in countries where the World Bank Group had more projects; however, there is no statistically significant relationship between financial inclusion going up and more financial inclusion projects.

Other things being equal, inclusion rose more in countries with shallower financial sectors and lower per capita gross domestic product, but less in FCS countries. There are payoffs in focusing on credit information and on deepening the financial sector, as it seems to enhance the World Bank Group's overall development effectiveness. There are payoffs in focusing on poorer countries as they showed an increased rise in financial inclusion rates (probably also because they had more to catch up). FCS countries remain more challenging. The next section provides a more detailed assessment of interventions for each Bank Group institution.

## **World Bank Support**

The World Bank's engagement in financing projects and conducting analytic and advisory work to strengthen financial inclusion is in theory grounded in national-

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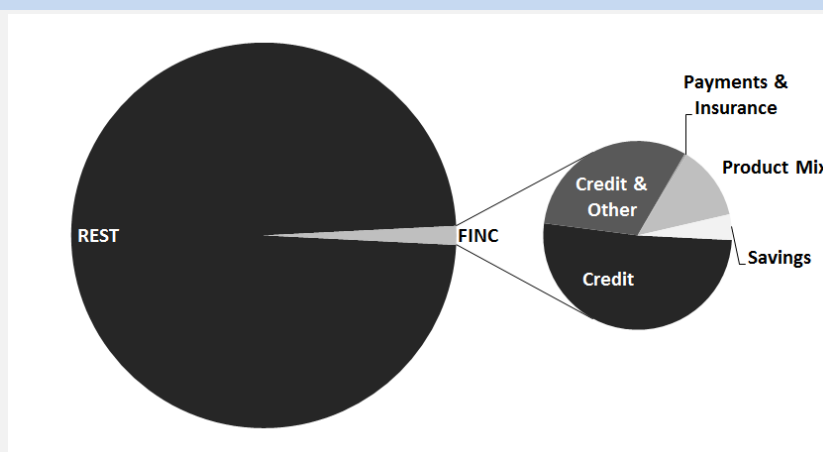
### DID FINANCIAL INCLUSION INTERVENTIONS DELIVER TO THE POOR?

level financial inclusion strategies based on a careful stocktaking of country conditions and in full cognizance of the interlinkages of financial inclusion with financial stability, financial integrity, market conduct, and the financial capability of consumers.<sup>3</sup> In practice, as noted in the discussion of upstream engagement, in a number of countries the Independent Evaluation Group (IEG) sees a less systematic set of activities in place downstream, often not tightly linked to each other by an overarching strategic framework. Nonetheless, in the financial inclusion portfolio aimed at poor households and microenterprises, there is a strong focus on the countries with the highest rate of exclusion, and often (and increasingly) operational portfolios support a diversity of services.

#### OVERVIEW AND RELEVANCE OF DOWNSTREAM SUPPORT

Given the diversity of the World Bank's portfolio, IEG found only a small percent of the overall portfolio focused on financial inclusion: 2 percent in volume and 6 percent in terms of numbers of projects. Most World Bank lending is focused "upstream" at the policy and institutional framework level, apart from technical assistance. Overall, almost two-thirds of the number of projects intervening "downstream" to provide direct financial services deliver credit (figure 4.1), but a significant share are focused on savings after 2010 (figure 4.2).

**Figure 4.1. World Bank Financial Inclusion Interventions as a Share of Total Lending Portfolio and by Type of Financial Services**



Sources: World Bank databases; IEG portfolio analysis.  
Note: FINC = Financial inclusion portfolio.

In spite of a marked increase in lending activity between the early portfolio period and the 2010s, only 22 downstream projects are seen to be financed in the 2013 period, with significantly more lending focused upstream. Technical assistance is more common than lending, and showed a similar increase in the 2010s, but is again mostly focused "upstream." This may reflect a comparative advantage of the World

Bank in focusing on policy and institutional aspects of financial markets, and then letting market forces, IFC, or other donors focus more downstream. It also reflects the focus on more nascent markets, where getting a policy and institutional framework in place is an appropriate priority as a precondition to later financing downstream (see below). IEG's analysis in case studies of the sequencing of upstream and downstream work suggested it was not always systematic, but that often, either sectorally or in a given type of financial service, upstream work preceded downstream interventions.

Although the majority of downstream technical assistance focused on credit, a significant share (although a small number of activities) focused on payments, savings and insurance. However, with growing evidence on the limited value of microcredit to most beneficiaries, as well as growing evidence of the benefits of savings and payments services (chapter 1), it might be expected that proportions of the portfolio would have shifted more dramatically. Yet, whether measured by number of projects or their commitment value, over three-quarters involve the provision of credit or credit combined with other services.

However, credit is not the whole story—in fact, only 24 percent of projects delivering credit had credit as their major component. In 54 percent of projects, credit played a more minor role. This contrasts sharply with projects where a mix of financial services was delivered or where payments, savings and insurance were the focus.

Overall, the World Bank's downstream lending activity heavily focuses on the most excluded countries. As demonstrated in chapter 2, fully 71 percent of financial inclusion lending projects and 72 percent of commitments are in countries in the lowest quartile of financial inclusion, based on the Findex measure of the bottom 40 percent of the population having an account at a formal financial institution (see figure 2.5a). In this respect, the portfolio is highly relevant to the World Bank's objective of shared prosperity for the bottom 40 percent. In fact, 99 percent of the World Bank's lending portfolio is focused on the bottom two quartiles of countries in terms of financial inclusion (that is, the countries with the highest rates of formal exclusion).

Downstream analytic and advisory activities (AAA) work is similarly focused, although less concentrated in the bottom quartile of inclusion, with 63 percent in the lowest quartile. The portfolio distribution is also well ahead of the microfinance market (indicated in figure 2.5a by the horizontal MIX bar), suggesting presence in providing services where microfinancial markets are less mature. This focus on countries with low levels of inclusion is also manifested in a regional pattern, with

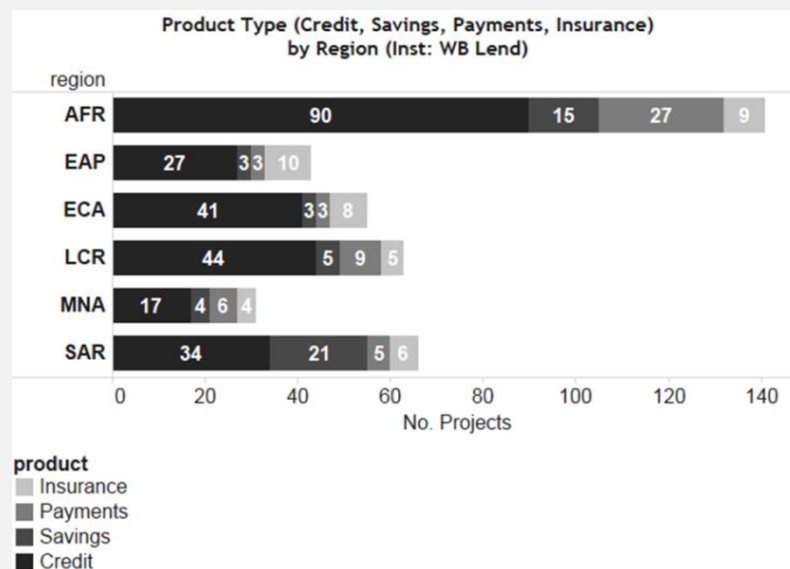


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### DID FINANCIAL INCLUSION INTERVENTIONS DELIVER TO THE POOR?

Sub-Saharan Africa leading all other Regions in terms of number of projects (figure 4.2).

**Figure 4.2. A Large Part of World Bank Portfolio is in Africa: A Majority Is Credit**



Sources: Business Warehouse; IEG portfolio analysis.

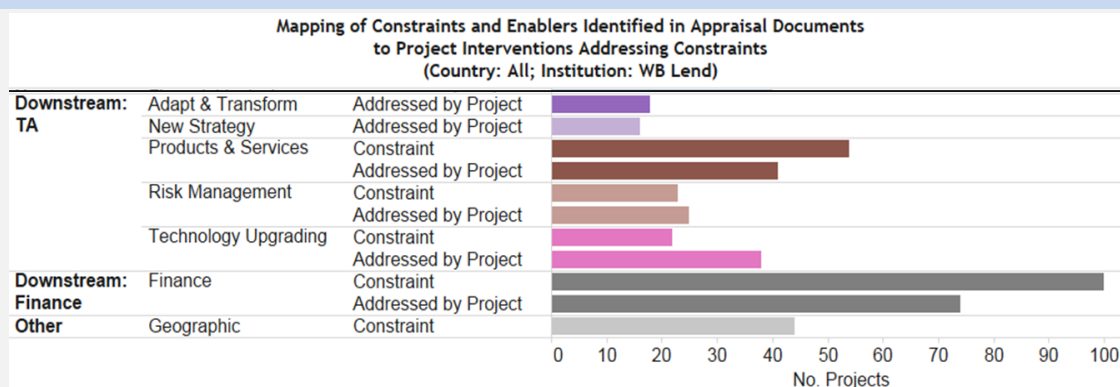
Note: AFR = Africa; EAP = East Asia and Pacific; ECA = Europe and Central Asia; LCR = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia.

Although data on whether interventions matched specific country needs are generally limited, the small number of countries with financial inclusion strategies in place during the portfolio period suggests potential for gaps, lack of complementarity and sequencing, and ad hoc approaches. For example, IEG's Tanzania country case study found very little activity in the rural financial market, in spite of the fact that most of Tanzania's poor live in rural areas and are served primarily by somewhat precarious savings and credit cooperatives. Some of this is driven by the priorities and capacity of the counterpart government—for example, in Ghana, the World Bank focused strongly on removing access to finance constraints in the agriculture and agribusiness sectors as well as for micro, small, and medium-size enterprises (MSMEs; although with mixed success).

World Bank projects often cite prior analytical or technical work, however at times the focus can be selective. In India, a seminal 2004 study galvanized both World Bank and counterpart activity in providing financial services to the poor. However, since then, there has been no comprehensive analytic work, save for a thin addendum to a Financial Sector Assessment Program (FSAP). There is certainly a fairly good fit between problems the World Bank identifies as important in project

documents and the focus of projects in financial inclusion (figure 4.3), although finance is somewhat more commonly identified as a problem than it is addressed.

**Figure 4.3. The Fit between Constraints Identified in World Bank Project Appraisals and Those Addressed in Projects**



Source: IEG portfolio analysis.

Note: TA = technical assistance.

## RESULTS AND SUSTAINABILITY

### *Development Outcomes*

Very few uniquely downstream projects were evaluated during the period: 14 downstream technical assistance projects and 6 downstream finance projects. World Bank loans, IFC investments, and MIGA guarantee projects are subject to a regular results monitoring and evaluation (M&E). These include a self-evaluation, followed by an independent validation by IEG. Based on this, development outcomes are assessed of these interventions on a routine basis at the time of operational maturity, project completion, or, for World Bank loans, at project closure, that is, once the loan is fully disbursed. Using predetermined criteria, development outcome is scored.

Based on these project-level evaluations, projects using a mix of upstream and downstream or downstream technical assistance and finance in the same project were more common and had more successful development outcomes. Overall, development outcomes of financial inclusion projects corresponding to the portfolio overall (figure 4.4). However, given the small numbers of evaluated projects in downstream technical assistance and finance, it is hard to firmly establish a trend.

#### **Box 4.1. Upstream and Downstream: World Bank and Bansefi in Mexico**

In Mexico, after a series of failures of credit cooperatives adversely affected consumers (especially in rural and marginal areas), the World Bank worked with the government to

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support sectoral reforms through both upstream and downstream support, including a series of projects supporting a newly created state-owned bank, Bansefi, created to assist and consolidate the sector.

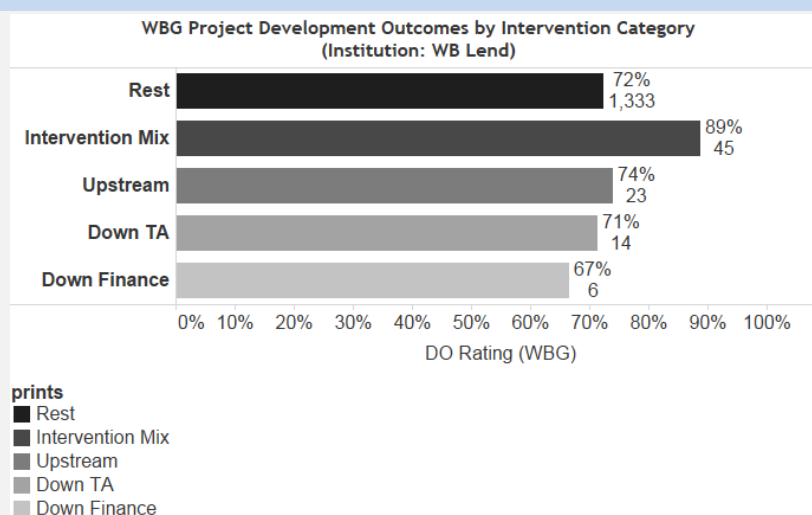
The projects supported both upstream work to restructure and consolidate the credit cooperative sector and to establish a regulatory framework and oversight architecture, and downstream work to provide technical assistance to a large number of individual financial intermediaries in the sector. The result was expanded access to financial services and a broader range of products offered.

The World Bank Group supported cooperatives in becoming accredited and helped Bansefi to reorganize the sector to deepen access to financial services. According to the Comisión Nacional Bancaria y de Valores, about 135 savings and loan cooperatives have become accredited and are now formally reporting to the supervisor.

Source: IEG.

A continuing challenge in evaluating downstream interventions is the lack of information on impact at the beneficiary level. Commonly, only outputs or outcomes are measured, as outlined more in detail in the last section of the chapter.

**Figure 4.4. Development Outcome Ratings of World Bank Financial Inclusion Interventions**



Source: IEG portfolio analysis.

### ***Should the World Bank Subsidize Financial Inclusion?***

Some World Bank Group financial inclusion interventions subsidize service delivery in a variety of ways. The 2007 Financial Sector Strategy states, “[T]he developmental mission of the World Bank Group necessarily leads it to focus on market and institutional infrastructure—including contract rights, contract enforcement institutions, and key market infrastructures (payments systems, credit bureaus,

accounting and disclosure standards, corporate governance, etc. )” (World Bank 2007, viii).

Nonetheless, the World Bank Group has recognized that, in some Regions and countries more than others, state engagement in the financial sector is higher and that to be engaged in financial sector development requires engagement with state providers of financial services. Thus, over time it has provided technical assistance and funding (such as lines of credit) channeled through state-run financial institutions. At times this may result in contradictions, for example, in countries where the World Bank is channeling financing through state institutions while IFC is attempting to build up commercial institutions serving an overlapping client base. The example of Turkey was noted in the recent IEG small and medium-size enterprise (SME) evaluation, but the India case study carried out for the present evaluation establishes additional examples (see, for example, box 4.2).

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**Box 4.2. Questions of Sustainability in Financial Inclusion Services through Rural Self-Help Groups in India**

The Project Performance Assessment Report for the World Bank’s Andhra Pradesh Rural Poverty Reduction Project raises questions about the sustainability of the political, economic, and related social structure of subsidies put in place under the World Bank-supported program. A major problem was that the extremely popular – but expensive – program reaching into every village invited political interference including interest rate subsidies and full waivers and promises of loan waivers. The latter, offered by both major political parties in a recent political campaign, “changed . . . the [self-help group] relationship with the World Banks, group credit ratings, and it resulted in high non-payment fees.”

In addition, the heavy fiscal burden of the government-affiliated Society for the Elimination of Rural Poverty running the self-help groups combined with the expense of interest rate subsidies called the sustainability of the self-help group program into question when, with the “bifurcation” of Andhra Pradesh into two states, the fiscal challenges of both new states became evident. The Project Performance Assessment Report sharply questions the sustainability of the subsidies: “Heavily subsidized interest rates, rebates, and waivers raise questions about the long-term viability and sustainability of the bank linkages portion of this program. They also run the risk of allowing for the politicization of an otherwise formidable platform for women’s and families’ social and economic development.”

*Source:* World Bank (2015).

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Similarly, the World Bank Group has tended to discourage subsidization of the interest rates in most circumstances. A 2002 Donor Brief by the Consultative Group to Assist the Poor (CGAP) captures the conventional wisdom of the time:

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### DID FINANCIAL INCLUSION INTERVENTIONS DELIVER TO THE POOR?

“Subsidized interest rates generally benefit only a small number of borrowers for a short period. Interest rate subsidies are an inappropriate use of donor or government funds because they distort markets and can encourage rent seeking. Programs that target specific populations with subsidized interest rates have generally suffered low repayment rates, institutional dependency, and limited growth” (CGAP 2002, 2).

However, initial subsidies are accepted. The same CGAP brief mentioned above accepts initial subsidies to help MFIs “reach the scale and efficiency needed to cover its costs from interest income.” For the World Bank, subsidies have been an accepted instrument for expanding financial access to the poor in World Bank policy under certain conditions. For example, Operational Policy 8.30, which governed financial intermediary lending from 1998 to 2014, stated the following:

“In some cases (for example, poverty reduction programs), subsidies may be an appropriate use of public funds. The [World] Bank supports programs involving subsidies only if they: (a) are transparent, targeted, and capped; (b) are funded explicitly through the government budget or other sources subject to effective control and regular review; (c) are fiscally sustainable; (d) do not give an unfair advantage to some [fiscal intermediaries] compared with other qualified and directly competing institutions; and (e) are economically justified, or can be shown to be the least-cost way of achieving poverty reduction objectives. Subsidies that do not meet these tests are phased out, or are substantially reduced, during the [financial intermediary loan]” (World Bank 1998).

In this qualified acceptance of subsidies, the World Bank Group deviates significantly from the International Monetary Fund (IMF). The World Bank apparently accepts various kinds of subsidies as long as they abide by these standards. This deviates significantly from the IMF, which cautions sharply against price subsidies:

“Explicit and implicit price subsidies burden the government budget and can aggravate the country’s fiscal position. . . . Price subsidies reduce allocative efficiency by distorting relative prices. . . . The methods used to finance subsidies — higher taxation or higher deficit financing — further worsen resource misallocations. . . . The capture of benefits of subsidies by middle- and upper-income households raises issues of equity and fairness. . . . Subsidies for certain activities — agriculture, energy consumption, and timber exploitation — can contribute to environmental degradation” (Gupta and others 2000).

A key challenge in subsidizing financial services to the poor can be that the growth of subsidized services may be limited by the fiscal capacity and political willingness of the state (or donors) to support them. In the case of Andhra Pradesh, the cost to the state government of the large bureaucracy supporting the self-help group system and of direct subsidies to reduce interest rates to zero on loans to self-help groups and small farmers contributed to high deficits, while the politics about subsidized credit led to promises of loan forgiveness that undermined credit culture (that is, repayment discipline).<sup>4</sup>

Subsidies can be more or less efficient, depending on how they are designed. In economic textbooks, the most efficient subsidy is defined as a lump sum subsidy, which makes the recipients better off because they can choose to spend it in ways that maximize their happiness. Subsidies of a particular good or service are seen as inefficient because they distort prices and can only be realized by a recipient by consuming more of the subsidized service or good. Thus, a poor person can only benefit from a subsidy on credit by borrowing. On the one hand, this may lead them to consume more credit than they would otherwise want, potentially to the neglect of other goods and services like food, housing, and education. On the other hand, if the person has no use for credit, they may not benefit at all from the subsidy.

So in purely theoretical terms, the poor would benefit more from a cash transfer than from an equivalently valued subsidy on interest rates. CGAP notes that if a donor's objective is to transfer resources to poor beneficiaries, microcredit might not be the most effective tool. Other types of interventions such as support for social services and even grants might be more appropriate for extremely poor or destitute populations.

Governments may choose to subsidize credit to overcome market failures, which lead either consumers to demand or providers to supply suboptimum amounts of credit (or other financial services). For example, because of asymmetric information, borrowers may lend less to the poor than they might if there were perfect information. If governments find it too difficult or costly to achieve better information, they may choose a subsidy to induce markets to more closely replicate an optimal level of credit provision. Or governments may decide that the poor ought to consume more financial services than they do or are able to, given the existing market. Some institutions, such as credit bureaus, may have public good aspects that lead to their under-provision if left to market forces.

In such cases, a question arises on how to structure the subsidy. One approach would be a one-time subsidy to the consumer or supplier to reduce the initial cost of establishing an institution, account or a transaction. Some argue that this is likely to

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be less distorting of price signals than an ongoing subsidy of the price of financial services. In addition, the ongoing subsidy may bring certain political economy risks, such as potential lobbying for its maintenance by beneficiary groups beyond the point where it has delivered its intended benefits or diversion and capture of the stream of subsidy by certain influential groups not intended as beneficiaries.

What is clear from the World Bank Group's portfolio is that, in practice, there is no consistent philosophy on subsidy guiding it. This is why very different approaches may be found across institutions and networks. In countries where IFC is financing private commercial institutions, the World Bank may finance public institutions as the vehicles for delivering financial services to the poor. In India, rural women's self-help groups are financed on a different basis than are beneficiaries of MFIs, with active subsidization and suppression of interest rates and state subsidization of the organizational costs of the self-help group system, as well as project-financed community funds providing further subsidy. For the World Bank Group, in the same country, to be financing both commercially based and commercially financed institutions and state-supported and heavily subsidized institutions targeting many of the same clients illustrates the lack of a coherent institution-wide approach.

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#### **Box 4.3. Mongolia: Commercial Services Model Works Best**

The Mongolian Sustainable Livelihoods Project (P067770) experimented with three approaches to help rural households manage risk: (i) subsidized credit under the Pastoral Risk Management component; (ii) credit offered on commercial terms under the Microfinance Development Fund (MDF); and (iii) rotating funds operated by local authorities. The Fund approach subsidized the introduction of new financial products, but offered them at commercial rates. IEG's Implementation Completion and Results Report Review found that "of these three approaches, only the MDF approach proved viable and sustainable. The performance of the subsidized credit and the [revolving loan funds] was weak, the former having low repayment rates and weak administration and the latter dropped from the project due to weak performance. The MDF did demonstrate the feasibility of increasing microfinance outreach through the commercial financial sector."

*Source:* IEG 2008.

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Another question confronting the World Bank is whether it should be supportive of government initiatives that involve subsidies to achieve financial inclusion. One way to achieve large numbers in financial access is to roll out massive government-led schemes, for example, through the establishment government-to-person payment accounts or through "no-frills" bank accounts in the public or private banking system. CGAP studies of Brazil, Columbia, Mexico, and South Africa found that

government-to-person payment schemes required recurrent operational subsidies from the government to make the accounts profitable for private banks to offer and maintain.

India's massive rollout of the Pradhan Mantri Jan-Dhan Yojana scheme offers additional cautions—the World Bank found that 72 percent of accounts opened under the scheme have zero balances (implying dormancy; Demirguc-Kunt and others 2015). This suggests that unless services are properly tailored to the poor, effective inclusion may be limited. There is also mounting evidence of the cost—the Indian Banker's Association stated in January 2015 that the initial round of no-frills accounts cost the issuing banks over \$300 million.<sup>5</sup> Other reports indicate that most of these accounts were issued by state-owned banks, while private banks have been slow to issue such accounts, further signaling questions about commercial viability.<sup>6</sup> The Banker's Association states that once public subsidies flow through the accounts, they may begin to pay for themselves.

Subsidization is likely to remain an issue going forward despite technological progress that eventually may enable reaching the very low end of the retail market in a sustainable manner. All this creates important questions for the World Bank that need to be answered at a strategic level. Does a program that most beneficiaries lack the incentive to use and that private banks lack the incentive to offer provide the basis for long-term and high-quality financial inclusion? If the World Bank's strategy is to build sustainable markets for financial services, is this a step in the right direction? And if subsidies are justified to reach the poor, can they be designed in ways so that price signals for efficient allocation and use of services are not lost?

### ***Drivers of Success and Failure, Work Quality, and Sustainability***

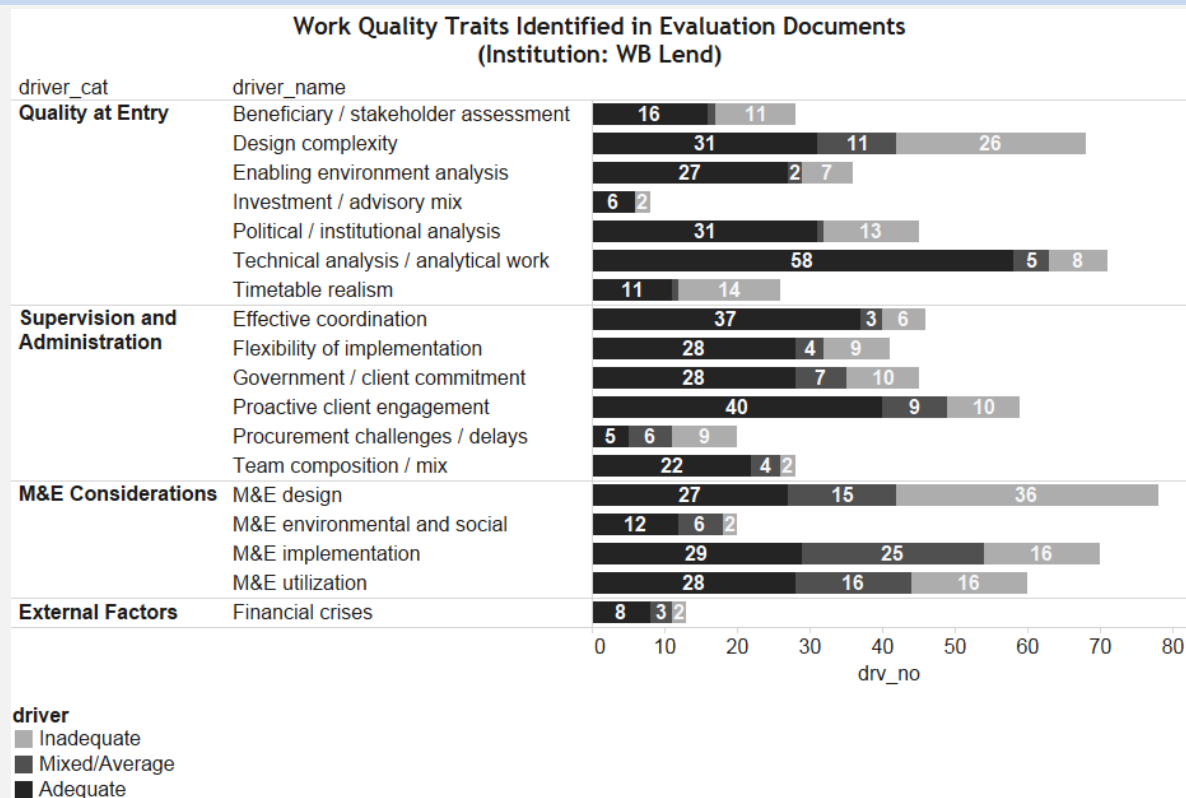
IEG's review of the evaluated portfolio finds many areas with relatively few problems, several of which have gradually been addressed. Design complexity (discussed below) is one of the two most frequently cited weaknesses of World Bank lending projects in financial inclusion, at least during earlier periods, that is, for projects approved fiscal year (FY)99–08. At the entry level, inadequate timetable realism and beneficiary assessment are also fairly common, even though an improvement trend can also be noted toward the end of the evaluation period. In terms of supervision, problems with government and/or client engagement are most commonly cited as problematic. With regard to M&E, the design of M&Es has more often been a weakness than a strength of financial inclusion projects but tends to be better for projects approved recently, that is, FY09–13. Implementation and utilization of M&E are also frequently weak (figure 4.5).



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**Figure 4.5. Work Quality Traits Identified in IEG Evaluations**



Source: IEG portfolio analysis.

One challenge in World Bank lending projects has been excessive complexity, often manifested in too many components and subcomponents, but also by projects that are inappropriately suited to client government capacity. Consistent with previous IEG evaluations on other topics, the financial inclusion portfolio again demonstrates that more complex designs yield poorer outcomes. Comparing the ratings for all project exited FY07–13, complexity at entry clearly shows that those rated inadequate (38 percent of those rated) for complexity had a 50 percent chance of achieving a negative development outcome rating, versus only 3 percent of those rated adequate (46 percent of those rated).

Some projects, in trying to achieve a “holistic” approach, add components that can move forward unevenly and require a number of different relationships with different counterpart agencies and different World Bank staff. Others may apply an “international best practice” design that is too sophisticated for client capacity experience suggests that simpler designs in financial inclusion lending, on average, yield superior outcomes.

The global practice has internalized this lesson, however, during the last few years, and design complexity improved. Projects approved FY09–13 show design

complexity is less frequently an issue. For only 2 of 10 approved and evaluated projects (20 percent) was design complexity an issue during FY09–13, that is, were rated “inadequate,” whereas it previously was an issue for 14 of 31 projects (45 percent) approved and evaluated FY04–08.

For M&E, the trend is less pronounced. Even though the design of M&E systems improved, usage of indicators remain a challenge. For 53 percent of the projects approved and evaluated during FY04–08 (19 of 36), M&E design was inadequate, but it was found inadequate for only 20 percent (3 of 15) for projects approved and evaluated FY09–13. Similarly, IEG’s ratings for project M&E went up from 28 percent rated “successful” for project evaluated FY04–08 – 40 percent for projects evaluated FY09–13.

This improvement is in line with World Bank’s overall improvement trends in M&E, but reflects substantially less improvement than for FPD projects for which successful M&E ratings moved up from 34 percent for projects evaluated FY04–08 to 50 percent during FY09–13. But what matters most in M&E is its usage. IEG’s analysis of the usage of indicators showed that usage did not change over time. In fact, for three of the five indicator categories, it declined. Most indicators (about 50 percent) relate to “financial intermediation” as expressed in, for example, dollar amount lent to MFI clients. Substantially fewer (13 percent) try to assess actual beneficiary effects. In light of these findings, ongoing efforts to improve the M&E systems are important and – once implemented – would enable the World Bank to track progress of its financial inclusion interventions (see later in this chapter for a detailed analysis).

## **IFC Support to MFIs**

### **OVERVIEW AND RELEVANCE OF IFC INVESTMENTS**

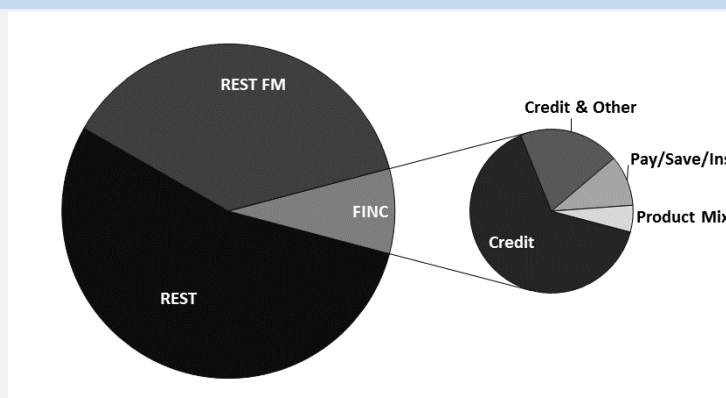
IFC’s investments in financial inclusion are small on average, but they occur in markets where they matter the most. Overall, the larger proportion of World Bank Group downstream interventions are carried out by IFC. Of 2,430 investments, 245 – or 10 percent – support financial inclusion as defined in this evaluation (figure 4.6). These account for 4 percent of IFC’s invested volume, indicating a smaller than average investment volume compared to other sectors. As demonstrated in chapter 2, many of IFC’s investment take place in countries with very low inclusion rates and where the average size is very small, indicating that these markets cater to the poor. This reach into low-inclusion countries indicates IFC’s high strategic relevance. IFC’s investments in MFIs are hence small, but highly relevant.

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Most investments support either fully licensed banks that are active in the microcredit space or nonbank microfinancial institutions (NBMFIs). Across most Regions, IFC investee MFIs are most commonly banks, follow by NBMFIs. Only in Sub-Saharan Africa do IFC-supported NBMFIs outnumber IFC-supported banks. IFC's investee companies can be greenfields or existing MFIs. IFC invests in greenfield MFIs to create the initial microfinance infrastructure in Regions where such infrastructure is missing and/or where existing banks do not lend themselves easily to downscaling. Greenfields also aim to transfer know-how and build local management capacity. Most greenfields are located in Sub-Saharan Africa, followed by East Asia and the Pacific. Latin America and the Caribbean and the Middle East and North Africa, by contrast, see the most IFC investments in existing MFIs. IFC supports these with the intention to see them grow and develop into flagship institutions for the local markets.

**Figure 4.6. IFC Investments in Financial Inclusion**



Sources: World Bank databases; IEG portfolio analysis.  
Note: FINC = Financial inclusion portfolio; FM = Financial market portfolio.

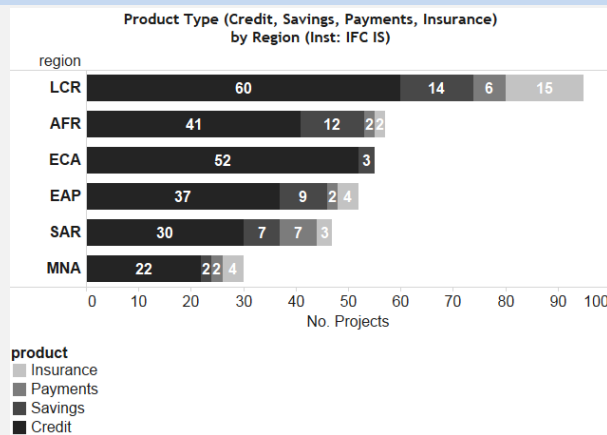
IFC's support through investments focuses on the provision of credit. A full 87 percent of IFC investments have as their primary purpose to provide funding to MFIs so they can lend in the form of microcredits to their clients. Seven percent involve payment or insurance schemes and a very small share of projects focused on savings (figure 4.9). This pattern is understandable in that noncredit projects would not be require much financing and would thus absorb very little of IFC's funding capacity. Provision of noncredit financial services is, however, important for the poor. IFC can – and does – engage in turning non-deposit-taking MFIs into deposit-taking institutions. To what extent IFC has an impact on increasing deposit taking will be analyzed later.

IFC's investment activity contracted in response to the 2008 global economic crises. Generally, IFC invested in MFIs through about 35 investment projects annually

during the evaluation period. The number of projects halved between 2008 and 2010 in response to the 2008 global economic crisis, then recovered subsequently to about precrisis levels in 2011. With regard to credit focus, the patterns remained unchanged over the years.

Investments were concentrated in the Latin America and the Caribbean Region, which was also the Region where the most projects occurred that looked *beyond* credit. With almost 100 projects during the evaluation period FY07–13, this Region attracted the most investments, followed by a cluster of Regions that received about 50 projects each during FY07–13. This cluster encompassed Africa, Europe and Central Asia, East Asia and Pacific, and South Asia. The strong focus on Africa is a result of IFC’s effort to establish greenfield MFIs in this Region in an attempt to create an MFI industry based on best practice standards. The Middle East and North Africa Region received the fewest projects. Interesting to note, across the Regions Latin America and the Caribbean has the highest relative share of projects that include a focus on noncredit projects, that is, savings and insurance schemes (figure 4.7).

**Figure 4.7. IFC Investments across Regions**



Sources: Business Warehouse; IEG portfolio analysis.

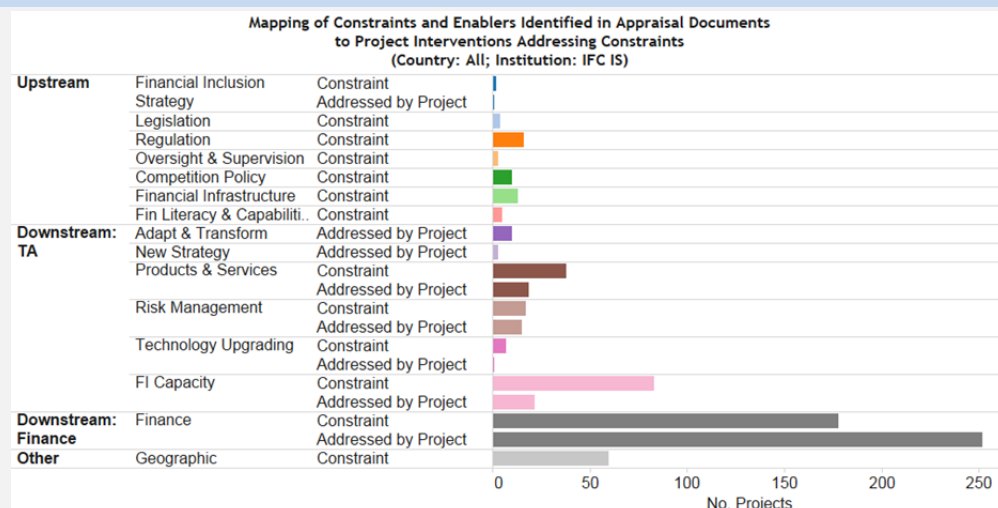
Note: AFR = Africa; EAP = East Asia and Pacific; ECA = Europe and Central Asia; LCR = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia.

IFC’s investments also addressed constraints beyond funding of MFIs, including building capacity in MFIs, transforming them into full banks, downscaling, assisting in product design, and improving risk management. The majority of IFC investments aimed to provide funding for MFIs; that is, they addressed a financing constraint. However, one-third of projects also identified capacity constraints of MFIs and about 10 percent of projects contain measures to create capacity within MFIs. IFC investments also assist MFIs designing products and services (10 percent of projects) and improving risk management (8 percent of projects; figure 4.8).

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**Figure 4.8. Constraint Addressed by IFC's Investments**



Sources: Business Warehouse; IEG portfolio analysis.

Note: TA = technical assistance.

In addition to its traditional support to MFIs through debt and equity investments, IFC also facilitates the growth of microcredit through other – innovative – mechanisms, such as credit-linked notes, local currency lending or foreign exchange facilities. These are not part of the evaluation portfolio per se (and represent only a marginal share of IFC's microfinance engagement) but are illustrated in box 4.4.

#### Box 4.4. Innovative Approaches in Support of Financial Inclusion

Credit-linked note. Traditionally, IFC has focused on supporting commercially oriented MFIs so they can provide credit to the poor. This has been pursued, as we have seen above, through debt and equity support. Given the tremendous credit gap, IFC has realized that a much greater involvement of the private sector is needed to realize the potential of microfinance. It has therefore taken steps to leverage its own resources to support MFIs by working with the private sector. Initially, this was done through helping specialized private equity funds focused on the microfinance sector. In a next step, IFC started to develop partnerships with large international banks. To encourage and facilitate their microfinance business. These partners engage typically in microfinance business in the context of their corporate and social responsibility program, but at times become interested in mainstreaming this business into their core business. This raised headroom constraints at the individual client level, requiring them to look for mechanisms to off-load their risks. IFC supports such a client through a "risk participation transaction" using a credit-linked note. This structure transfers a portion of the credit risk of the MFI client held in the book of the client to IFC. Through a Special Purpose Vehicle, the IFC client transfers 80 percent of the risk to that vehicle through Credit Default Swaps, keeping 20 percent on its own.

Local currency lending. Managing foreign exchange risk is a persistent challenge for MFIs, donors, and investors. Cross-border debt and equity invested in microfinance brings important benefits for MFIs, as it provides longer-term debt maturity and often is not available in the local market. However, it comes with foreign exchange risk. MFIs need loans in their own currency to match their revenues as their microfinance clients borrow in local currency. International finance institutions such as IFC mobilize long-term local currency financing through various derivative and structured and securitized products. For example, a partial guarantee from IFC allowed BRAC (formerly Bangladesh Rural Advancement Committee) to borrow \$18 million more in local currency from Citibank in 2008.

Foreign Exchange facilities. Another example of managing foreign exchange risks for MFIs is foreign exchange facilities, which offer MFIs and microfinance investors a method to hedge foreign exchange risk, even for currencies for which hedges are not commercially available. In the longer term, MFIs could reduce their foreign exchange risk exposure by relying more heavily on local currency deposits, but—as this evaluation has found—is often costly and time consuming.

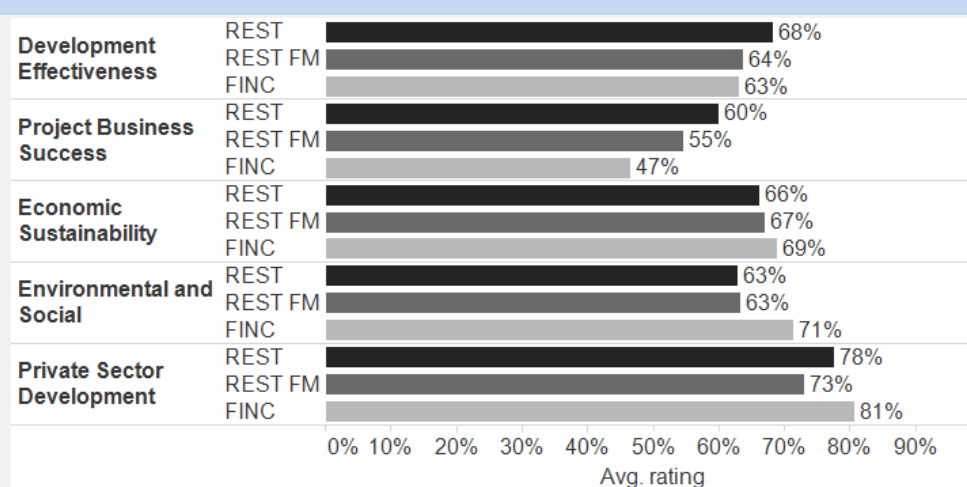
Sources: IEG staff, CGAP (2010).

## RESULTS AND FACTORS OF SUCCESS AND FAILURE

### *Development Outcomes*

When looking at development outcomes, financial inclusion investments perform slightly below average. Of 90 evaluated projects, 57 (63 percent) were rated satisfactory or better—that is, were successful. This compares to a success rate of 67 percent across the entire IFC investment portfolio (figure 4.9).<sup>7</sup>

**Figure 4.9. Development Outcome Ratings**



Sources: IEG-validated public sector reforms; IEG portfolio analysis.  
Note: FINC = financial inclusion portfolio; FM = financial market portfolio.

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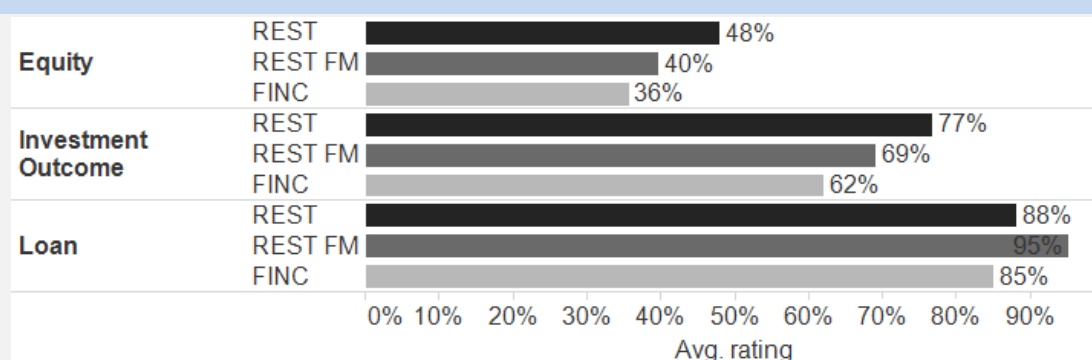
### DID FINANCIAL INCLUSION INTERVENTIONS DELIVER TO THE POOR?

The investments by IFC in MFIs struggle with achieving adequate business performance but exhibit remarkable private sector development effects and good economic sustainability. Looking at the various elements that make up the overall development outcome rating, that is, project business success, economic sustainability, environmental and social compliance, and private sector development effect, a revealing pattern emerges. IFC investments in MFIs rate lowest on project business success, with fewer than half of all evaluated projects (47 percent) rated satisfactory or better, compared with 62 for IFC's average portfolio. This indicates that investments tend not to turn profitable in the time frame given, that is, before they are labeled "operationally mature," which is typically two years after incorporation.

Project business performance is lowest in Europe and Central Asia, with only 27 percent (of a total of 12 projects) rated successful, followed by Sub-Saharan Africa with 35 percent (of 19 projects) rated successful. The best project business performance was found in South Asia, where 3 IFC-supported MFIs were rated successful, or 75 percent of the Region's portfolio of in total 4 projects. This has to be contrasted with the high private sector development rating of 81 percent of evaluated projects and the relatively high Environment and Social rating of 71 percent (figure 4.10).

As a consequence of their low business performance, IFC's investments also exhibit lower investment outcomes, particularly equity investments. Only 63 percent of MFI investments yield a successful investment outcome for IFC, compared with 71 percent of the financial sector subportfolio and 78 percent for IFC's portfolio as a whole. This relatively low investment outcome for MFIs investments is mainly driven by the investment outcomes of equity investments which are particularly vulnerable, pointing to the risk involved and reflecting the challenges for these investment to turn profitable (figure 4.10).

**Figure 4.10. Relative Low Investment Outcomes of IFC's Investments in MFIs**



Sources: IEG-validated public sector reforms; IEG portfolio analysis



*Note:* FINC = Financial inclusion projects of IFC downstream, that is, investments in MFIs; FM = financial market portfolio.

The root causes for the low profitability of IFC's MFI investments were higher start-up costs for greenfields or higher operating costs for existing MFIs and slower loan growth. Investees typically exhibited higher costs during start-up than expected because of (i) delays in approval by the regulators and significant regulatory risks; (ii) greenfield management fees that can be burdensome for early stage operations; (iii) slow deposit gathering; and (iv) high employee turnover, which decreased efficiency. On the revenue side, loan volume grew more slowly than anticipated. IFC often expected a higher number of loans based on the projected level of productivity per loan officer. The gap between projections and reality was particularly strong in Sub-Saharan Africa but also in other Regions, where the assumptions of productivity were taken from other greenfield operations (mostly from Latin America and the Caribbean), but such assumptions proved hard to achieve in the local context.

In some cases, insufficient assessment of the regulatory difficulties and “red tape” has caused investment to get delayed. In some cases it took almost two years, with resulting cost overruns. Major delays in approving the operations occurred in the Democratic Republic of Congo, Ghana, and Liberia. IFC found that the pre-operational phase took longer and cost more than anticipated. It was a complex undertaking that, among other things, included interacting with regulatory authorities, renovating branches, training staff, preparing policies and procedures, and configuring the information technology platform. Delays in regulatory approval were a common issue in half of the cases.

### ***Catering to the Poor***

The extent to which loans are taken out by the poor can be measured by their average loan size. Only household income data could establish a precise record of the actual income level of a client base of an MFI. These are typically not available in an efficient manner on a large scale for several thousand MFI clients. The literature as well as practitioners have hence resorted to the average loan size as a proxy for reaching the poor, that is, to assess to what extent a loan portfolio caters to the poor. To control for the income level of the country – a \$1,000 loan may be small in Turkey but it is large in Bangladesh – the average loan size over gross national income (GNI) per capita is typically taken as an indicator.

Average loan size values can be computed using Microfinance Information Exchange (MIX) data. MIX reports provide detailed information on the financial, operational, and social performance of the microfinance industry (1,650 MFIs), including key data points such as gross loan portfolio, average loan and deposit



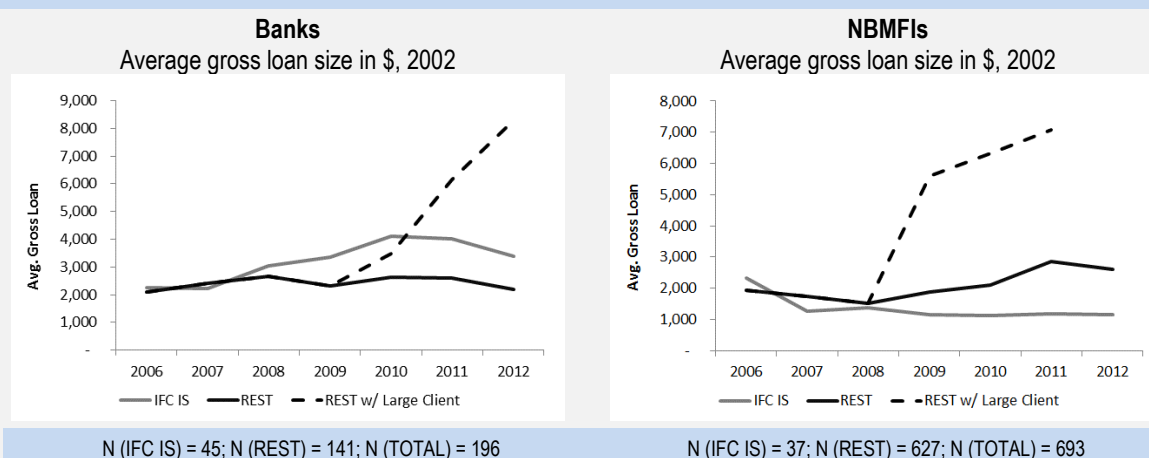
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balances per borrower, yield on gross portfolio, and so forth. For this evaluation, within the 1,650 MFIs reporting to MIX, 103 were identified that received IFC support. These account for 73 percent of IFC clients in the entire evaluation portfolio of 142 IFC-supported MFIs. This total number of 142 has been corrected (the total number of IFC investee companies is higher) as not all IFC investee companies can reasonably be expected to report to MIX.<sup>8,9</sup> For IFC-supported MFIs, the derived values were complemented by those computed based on reported loan sizes in IFC's Development Outcome Tracking System.

IFC-supported banks<sup>10</sup> issue loans that are, on average, slightly larger than the ones issued by their peer banks; those of NBMFIs tend to be smaller. Looking at the absolute volume of the loans (in U.S. dollars), IFC-supported banks (that reported these data consistently) issued loans with an average loan volume of \$2,000 in 2006, steadily growing to \$3,000 in 2012. IFC's loan volumes were initially comparable to other peer banks, but as of 2007, IFC-supported banks increased their loan volumes to \$3,000 while their peers remained at about \$2,000. For NBMFIs, the situation is different, inasmuch as IFC-supported NBMFIs issued loans smaller than their peers. Note that the entry of one Chinese Bank and two Chinese NBMFIs into the MIX market leads to a drastic increase in average loan size as of 2010, as their microloans are significantly larger than the MIX markets' average. Hence, in figure 4.11, the MIX market data is presented comprising all contributing MFIs, that is, including these bank (dashed line as of 2009), and excluding them (full line throughout).

**Figure 4.11. Absolute Average Loan Size: IFC-Supported MFIs versus Market**



Source: MIX data.

Note: IS = Investment Services; REST = MIX market without IFC-supported MFIs.

Considering the GNI per capita in the respective countries, the difference between IFC-supported banks and their peers widens. Putting the average loan size in relation to the GNI of the respective country allows one to factor in the populations'

income level; this yields the “relative average loan size” in terms of U.S. dollars/GNI. According to this measure, banks support through an IFC investment show an about equal relative loan size initially 2006–07 (\$2/GNI per capita), but increasing to about twice as large a relative loan size (\$4/GNI per capita) during 2009–12. For NBMFIs, the situation is somewhat different as overall average loan sizes decreased during 2000–12 for both IFC-supported NBMFIs and their peers, with IFC-supported NBMFIs issuing loans about 20 percent smaller than their peers (figure 4.12a). The relative average loan size differs across Regions. It is relatively highest in Sub-Saharan Africa, hovering about \$3.50–\$7.00/GNI per capita, and lowest in South Asia, with only \$0.40–\$0.50/GNI per capita indicating that in the latter Region’s MFIs are the most successful in reaching the poor.

The difference between absolute average loan size and relative loan size can be explained by the differences in geographic focus areas of IFC and the rest of the MIX market. As seen above, when looking at the relative average loan size in terms of loan size over GNI per capita, the gap between IFC-supported banks and the average loan size of the MIX market widens. Looking closely at where these MFIs are located reveals that IFC tends to support MFIs located in countries that have lower-income levels, that is, those that have a lower GNI value. Of the 21 IFC-supported banks, for example, seven are in low-income countries, whereas only five of the rest of the MIX-reporting MFIs are located there; equally seven IFC-supported banks are in upper-middle-income countries, and nine of the MIX MFIs are located in these countries.

This indicates that IFC tends to operate more in lower-income countries and less in high income countries, which in turn drives the relatively average loan size (dollar/GNI per capita) up for IFC-supported MFIs. But is also corroborates the conclusion of chapter 1 that IFC’s support is pioneering in as much as it reaches out to those countries that have the lowest financial inclusion rates and low average loan sizes.

The analysis of the relative loan size (U.S. dollars/GNI per capita) reveals also that microloans represent about 5–10 percent of the loan portfolios of those banks that IFC supports with investments where microenterprises or poor households are the or one of the declared beneficiaries. For this assessment, the average relative loan size of the MIX market was computed and found to amount to 1.6 times GNI per capita. The results of plotting the entire portfolios of the banks that received funding from IFC in the context of its financial inclusion agenda are shown in figure 4.12b.

Most IFC-supported banks (90 percent) have mixed portfolios, that is, they are not only issuing microloans (of about 1.6 times GNI per capita), but also SME loans.

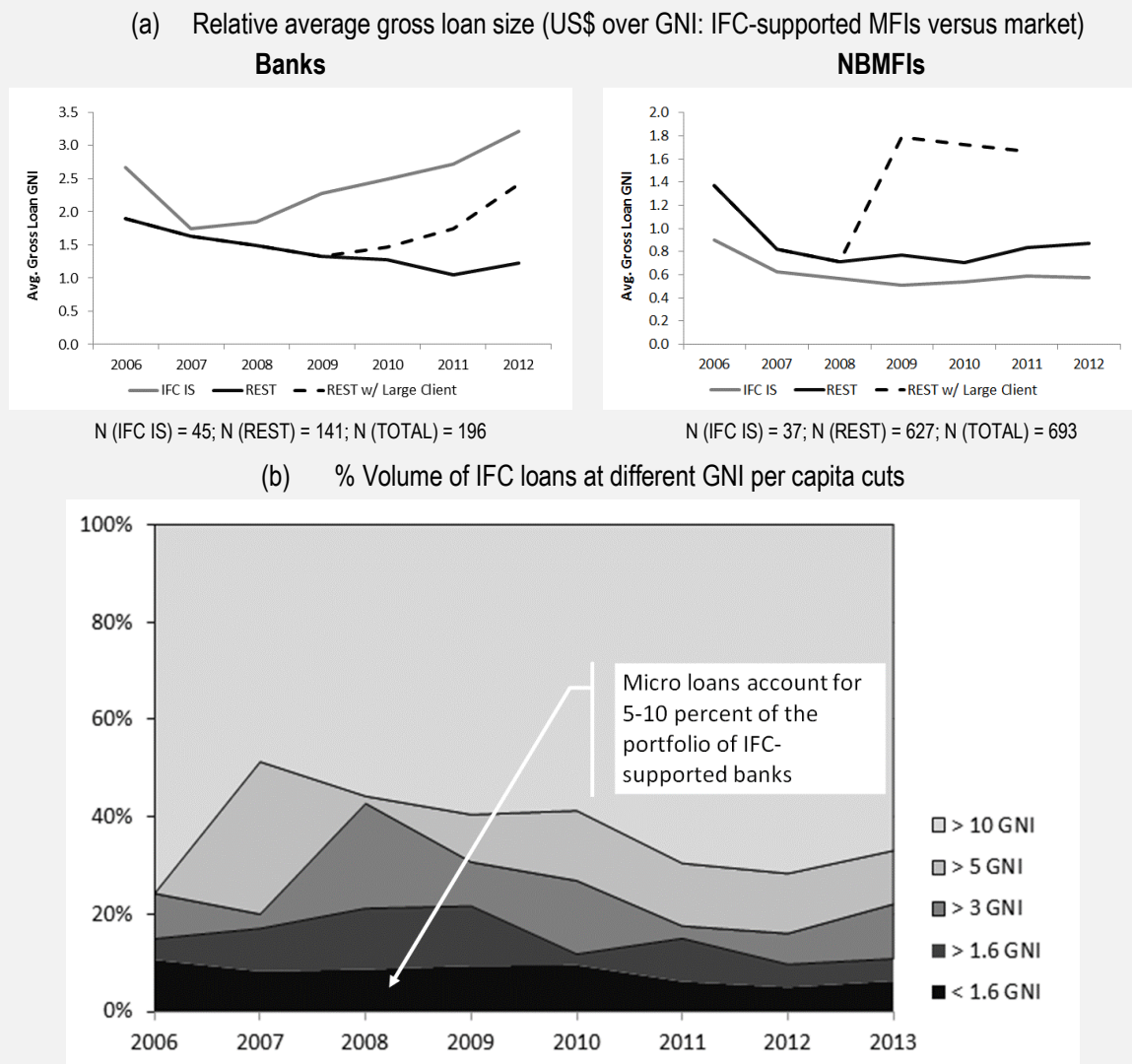
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Hence, although about 5–10 percent of their portfolios are microcredits, the rest of these portfolios are larger (up to 10 times or more). These go to clients taking out significantly larger loans, including SMEs.

IFC therefore plays a role in the microsegment, but only a fraction of its support caters to the small retail segment of microcredits. This is not necessarily a bad thing as, at least, SMEs are likely to benefit from such loans – and eventually microenterprises may benefit from the strengthening and deepening of the smaller end of the commercial finance market. Issuing SME loans is likely also to be more lucrative for MFIs and could thus be seen as supporting the microcredit business lines. The fact that microloans represent only a fraction of the loan portfolios of supported banks can partly be attributed to the fact that IFC-supported banks found it difficult to branch out and support the rural poor, except for selected cases like in Mexico through its support of Compartamos and Progresemos.

Figure 4.12. Relative Average Loan Size of IFC-Supported MFIs



Sources: MIX data; IFC Development Outcome Tracking System.

Note: IS = Investment Services; REST = MIX market without IFC-supported MFIs.

MFIs often shy away from rural activity, which is unfortunate, as this is where most of the poor live. To expand into the rural areas, traditional distribution channels based on brick-and-mortar branches would have to be replaced by less costly models, such as correspondent banking or tablet-based agent banking. Many institutions are deterred because demand is difficult to assess and household incomes are variable, as a large share of potential clients rely on weather-dependent agribusiness, as seen in Tanzania and Latin America and the Caribbean. This requires, among other things, innovative product design, such as loans with flexible payback profiles, ideally modeled after the income situation of the client household, as pioneered in Tanzania by the IFC-supported Access Bank, or mobile banking,

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which several IFC client MFIs have ventured into. At times, the payback-culture of the rural poor has been affected by debt forgiveness programs or promises, as in the case of India. These findings are corroborated by IFC's own observations, as in its recent Smart Lessons, "Small Beginnings from Great Opportunities" (IFC 2015).

The focus on an urban clientele was found to be particularly true for greenfield operations, as confirmed by the recent IEG cluster evaluation of IFC's Microfinance Program in Africa (AMP), which concluded that "[t]he main beneficiaries of the program are middle-income individuals (mostly women) in cities. The program is progressively expanding in selected countries its reach to lower-income individuals and rural areas but it is taking longer than initially expected" (IEG 2015). Further findings of IEG's AMP evaluation are summarized in box 4.5.

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#### **Box 4.5. IFC Africa Microfinance Program: Creating Greenfield MFIs**

The AMP started in April 2007 with a programmatic approach of 5 microfinance transactions in five countries in Sub-Saharan Africa and grew to 20 operations as of 2013. It was designed to expand access to finance services for poor populations and low-income microentrepreneurs and to establish commercially viable microfinance entities to provide access to credit and financial services for previously excluded populations. IFC was a major contributor to these commercially oriented MFIs. Overall, the AMP generated positively to market development but it required more time and resources than expected.

Overall, the program had mixed results. Some leaders emerged from the program that exhibited balanced growth between loans and deposits and demonstrated an ability to gain profitability and market share. Less successful operations, however, are still struggling to grow. On the positive side, none of the projects are currently in special operations, have defaulted or had their debt rescheduled. Despite the positive private sector development impact, none of the supported operations reached the profitability expected by IFC. Impact has been of relatively small scale, and the main challenge for IFC and the program remains to scale up existing operations. The recently concluded IEG review of the AMP concluded the following:

- Greenfields can be a powerful tool in countries where IFC has first-mover advantage.
  - IFC was a major contributor in pursuing commercially oriented microfinance on Africa's map and establishing microfinance infrastructure in several countries.
  - AMP generated positive market developments but required more time and resources than expected. None of the projects achieved the profitability expected in the Board Report.
  - The main beneficiaries of the program are middle-income individuals (mostly women) in cities. The program is progressively expanding its reach to lower-income individuals and rural areas in selected countries, but it is taking longer than initially expected.
  - New greenfielding in Africa stopped in 2012, and since then IFC, has been focusing more on expansions, transformations, and digital finance.
-

The main challenge for the AMP is to take stock of what has been achieved and possibly scale up existing operations.

Source: IEG 2015.

Monitoring and transparently reporting to what extent IFC's loans reach the poor and microenterprises is important going forward. Currently, IFC defines a microenterprise as having less than \$100,000 in assets and annual sales and a microloan as having a volume of less than \$10,000. This may be adequate for Turkey, but is much too high a threshold for "micro" in, for example, Tanzania. The MIX market can serve as an indicator for what is an adequate volume of a microloan: MIX-reporting MFIs typically issue microloans of about 1.6 times the GNI per capita in a respective country. This appears a reasonable proxy for a relative loan size and would translate into microloans averaging \$10,970 in Turkey but about \$860 in Tanzania.

IEG's own analysis shows that about 60 percent of the microloans of an IFC-supported bank would be considered micro using such a definition. Going forward, IFC may want to consider first defining what constitutes a microenterprise in the various economies in which IFC operates. Based on such a definition, IFC could then set thresholds for loan sizes to be considered micro. This would allow IFC to report on the share of the microloans reaching the poor using loan sizes, cognizant of the country-specific income situations and granularity of the economies.

The current practice of labeling investment as "in support of microenterprises" could cause confusion and may raise undue expectations about IFC's reach and the number of microenterprises it is helping. According to IFC's own analysis, the median and average annual sales of IFC-supported microenterprises amounts to \$152,000 and \$530,000—both considerably above the set threshold for microenterprise loans of up to \$100,000. Similarly, the median and average total assets amount to \$131,000 and \$352,000, respectively, compared with a cutoff point of \$100,000. IFC-supported microenterprises appear to meet the criteria only with regard to the number of employees (IFC 2013).

Many of IFC-supported MFIs are located in low-income countries, most of which have high exclusion rates. This indicates that IFC operates at the frontier. Data show, however, that within these markets, IFC's support does not necessarily reach the poorest of the poor. The mixed portfolios of IFC-supported banks typically have a share of 5–10 percent of microloans; within the microloan segment, average loan sizes are slightly higher than the ones of peer banks but smaller than those of peer NBMFIs. IFC-supported MFIs are found hesitant to enter the rural space for a range

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of issues. Going forward, IFC would have to find innovative business models, products and technologies that would enable reaching the poor, including through innovations that would allow lowering transaction costs. This is likely only possible through trial and error or through a research agenda that pilots such innovative business models as IFC tries to scale up its MFI business.

Equally important for the poor is the extent to which IFC-supported MFIs were able to promote saving. Savings are financial services that seem to be potentially more beneficial for the poor than credit. As seen in chapter 1, studies assessing the impact of providing access to savings products are, on average, more positive compared with the impact studies on microcredit. Studies pointed at higher investment rates, and at their power to mitigate risk. Yet, the focus of the World Bank Group's inclusive finance support has been on credit and has only gradually embraced other services, despite their usefulness for the poor.

The historic focus on credit has simple reasons: (i) the ease of regulating credit, (ii) its built-in commitment mechanisms, and (iii) the lower cost of providing credit relative to local resource mobilization. However, increased savings would not only offer a value proposition for the poor, increased mobilization of savings in the local currency would also make MFIs more impervious to foreign exchange fluctuations, reduce their need for hedging, or reduce the foreign exchange risk passed on to customers. And finally, it may also make financial markets less vulnerable, as international funders tend to withdraw funding to frontier markets during crises. Hence, it is important to understand to what extent MFIs engage in deposit taking.

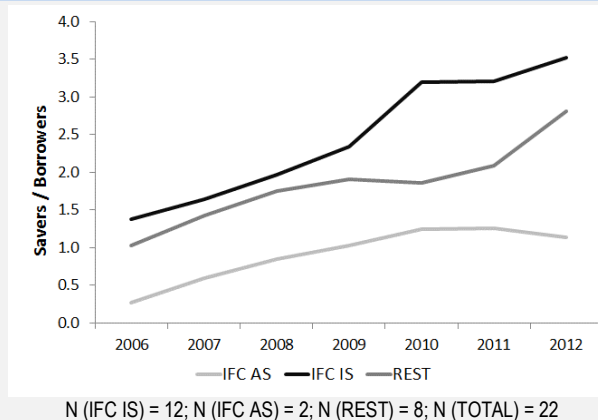
It is IFC's strategy to increase savings, even though at present IFC's portfolio is heavy on credit. Most investments support the provision of credit (87 percent of IFC investments) as this is what consumes funding; savings would not. However, it is IFC's strategic intention to increase savings mobilization as "a key to sustainability [of the MFIs market] and poverty alleviation." It aims to do so by increasing back-office capacity in the MFIs it finances by setting in place adequate incentive structures, by exercising its influence at the Board, or by assisting in innovative product design and/or developing market and strategy studies. At the upstream level, IFC Advisory Services works on regulatory improvements that enable deposit taking (see chapter 3).

Looking at the few MFIs that systematically report savers and borrowers, those MFIs that were supported by an IFC investment tend to have higher number of savers than their peers. During 2006–12, IFC-supported banks managed to increase local resources mobilization continuously, even more so than their peer banks (figure 4.13). This findings is, however, to be regarded as an indicative value only because

only small portion of MFIs report data on savers and borrowers. Encouraging deposit taking with its investee MFIs was more difficult in some Regions than in others, as found by IEG's evaluation of IFC's Africa Microfinance Program (IEG 2015).

With the exception of ProCredit Bank DR Congo, for most MFIs of the Africa Microfinance Program the ramping up of customer deposits has been slower than expected and has resulted in a dependence on donor funding to finance loan growth. In 6 of 10 evaluated MFIs, the institutions focused on growing the loan portfolio first and then on gathering deposits. Although the projects were able to reach more than 100,000 clients on average, the level of deposits per account was low (\$312 per account, which is similar to \$258 in the rest of Africa but significantly lower than \$1,500 in Latin America and the Caribbean) and resulted in high loan-to-deposit ratio. When supporting operations, IFC may wish to require sponsors to give similar importance to deposits as to loans to experience a more balanced growth.

**Figure 4.13. Promoting Savings: IFC-Supported MFIs versus MIX Market**



Source: MIX data.

Note: AS = Advisory Services; IS = Investment Services; REST = MIX market without IFC-supported MFIs.

### ***Drivers of Success and Failure, Work Quality, and Sustainability***

Generally, when looking at the country-level engagement pattern of IFC investment, IFC's approach appears opportunistic rather than part of a broader strategy, and sometimes it seems to come late. This trend emerged from most country cases reviewed. For example, in Indonesia, although IFC has several successful investments in MFIs that provide microfinance, it lacked an overall engagement plan. Or in Tanzania, it intended to be involved in early bank privatization efforts but eventually opted not to; several years later, it came back to invest in the two



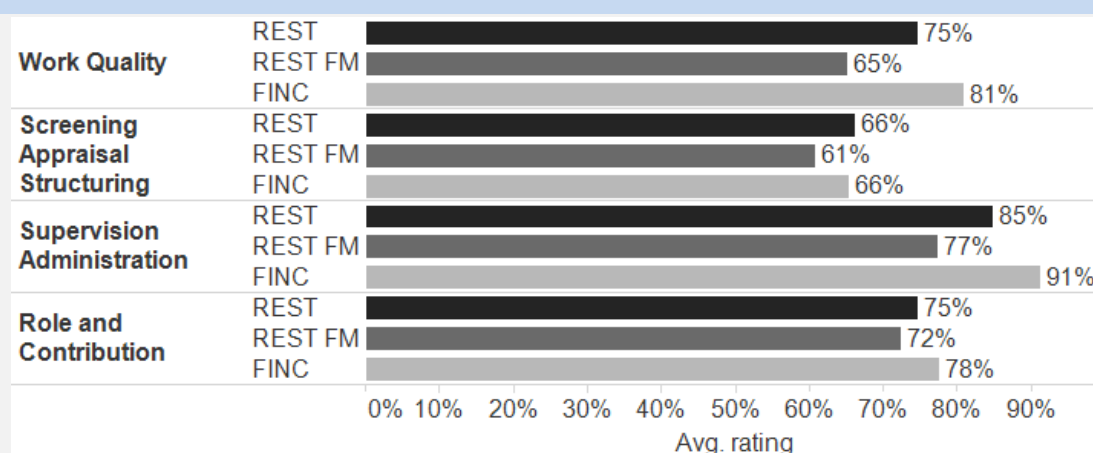
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established microfinance providers after they had received assistance from the World Bank and were invested in by another strategic partners from the private sector and Danish International Development Agency, respectively. Also in Azerbaijan, IFC loans for MFIs came later – typically after other international financial institutions and impact funds. For example, one of its investments in a leading MFIs came 13 years after it was established with U.S. Agency for International Development support and well after other international finance institutions invested, instead of assisting it initially.

The fact that IFC tends to invest rather late may lead to missed opportunities, as in greenfield operations; IFC did benefit from a first-mover advantage. In countries where IFC had first-mover advantage with greenfield operations (the Democratic Republic of Congo, Liberia, Madagascar, Nigeria, and Senegal), its investees were able to achieve higher market share than those where IFC was a late comer (Cameroon and Ghana). In the first set of countries, AMP projects became market leaders. In more mature markets, some were able to enter as niche players, contain costs, and obtain early profitability. Three examples of this approach were Access Nigeria, Accion Nigeria, and Ecobank-Accion Ghana.

**Figure 4.14. High Work Quality of IFC Investments in MFIs**



Sources: IEG-validated public sector reforms; IEG portfolio analysis.

Note: FINC = financial inclusion portfolio; FM = financial market portfolio.

A closer look at IFC's management of its investments in support of financial inclusion reveals high work quality (figure 4.14). Eighty-two percent of evaluation downstream projects were rated satisfactory or better on work quality. Although screening, appraisal, and structuring was carried out at comparable quality standards as IFC's portfolio as a whole (67 percent rated satisfactory), IFC excelled with regard to supervision and administration. Full 91 percent of microfinance

investments were rated satisfactory or higher. IFC's role and contribution was also rated as satisfactory or higher for 79 percent of projects (figure 4.15).

Work quality is important, as IFC has substantial control over development outcomes in diverse country conditions through it. Controlling for relevant country characteristics such as per capita gross domestic product, depth of credit information and credit, and base level of inclusion, for IFC projects (investment and advisory), significant predictors of outcome include design and complexity; prior analysis; and M&E. These factors under IFC control are significant predictors of outcome, whereas country characteristics are not. This indicates that IFC has substantial control over outcomes in diverse country conditions through its work quality.

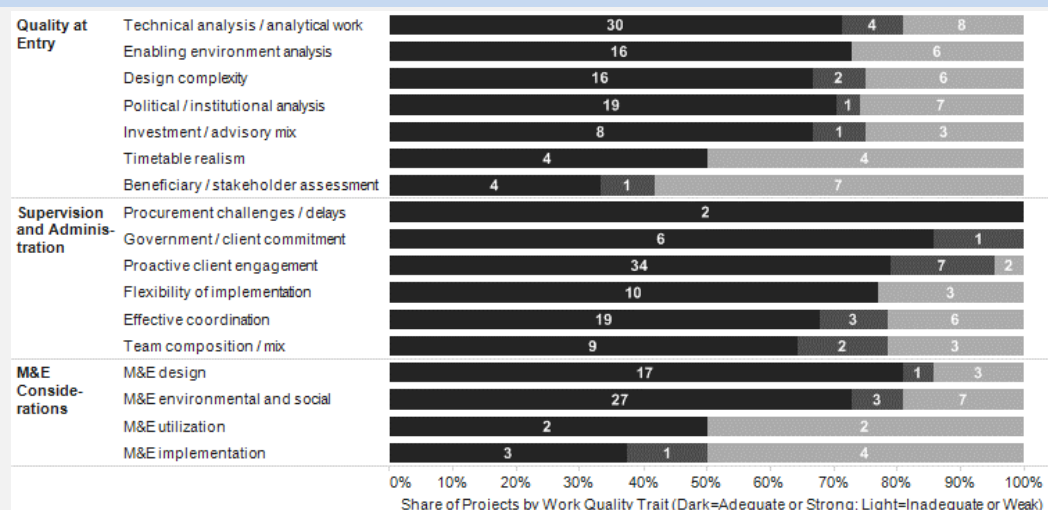
An analysis of the drivers of success and failure reveals a set of recurring opportunities and issues. Again, lack of realism with regard to timing of an IFC investment, inadequate analysis of the political and institutional context and of beneficiaries or stakeholders, and flaws in technical analysis were identified as weaknesses (figure 4.16). However, these shortcomings mainly apply to projects in Sub-Saharan Africa; IFC had overoptimistic projections in terms of number of loans, average balance per loan, and mix of loans between microloans and SME loans. As with all IFC investment, breakeven was expected to occur within 16 months of launch. Although some operations attained breakeven within two to three years, profitability was affected significantly. Break even for most operations was achieved between years 4 and 5, and recovery of earlier losses only occurred after that period. Thus, for most greenfield operations, projecting breakeven results after two to three years proved to be optimistic.

Relevant sponsor experience was key. Sponsor quality was one of the key factors of success across projects. In Pakistan, the committed and strong strategic sponsor (Telenor) was one of the key drivers for a successful investment in Tameer Bank, assisted through a well-timed technical assistance delivered by a parallel IFC advisory project. Management was able to quickly deal with the deteriorating asset quality and revision needed to the business model. This is similar to in Mexico, where sponsor quality, experience, and commitment were drivers of success for IFC's investment in Progresemos, for example.

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**Figure 4.15. Work Quality of IFC Investments**



Sources: IEG-validated public sector reforms; IEG portfolio analysis.

Starting a new MFI is not the same as supporting an existing, functioning one — pointing at specific requirements for sponsor quality in the case of greenfields. Many firms and organizations have experience in providing specific consultancy services to MFIs, but few have the necessary expertise and capacity to create, manage, and build them. The case study on Ghana thus concludes that the selection of sponsor with appropriate experience is essential, particular in greenfield operations and in the challenging environments that IFC often operates in. The recent IEG evaluation of IFC's AMP concluded equally that very few of the AMP's sponsors had relevant greenfield experience in Africa at the time of the program set up. Most sponsors were consulting firms specialized in acquisitions, or transformations but had no relevant experience in starting greenfields or managing day-to-day operations, especially in Africa. Access Holdings had some experience with start-up and managing operations in Access Bank Azerbaijan (in 2002) with the support of IFC, the European Bank for Reconstruction and Development, and KfW, and has grown significantly. Two of the three AMP operations with Access Holdings were evaluated as "high" performers. In the case of Advans Holding, it had consulting experience and acquisitions experience, particularly in Amret in Cambodia, but it did not have previous greenfield experience or managing operations in Africa, which was one of its main weaknesses. All three evaluated projects of Advans Holdings were rated as "low" performers. (IEG 2015, 20)

IFC may draw on this experience in selecting its partners for future projects.

IFC-supported projects encountered greater difficulty in attracting and retaining qualified personnel. This is valid across most Regions. Both operations in Mexico, Progreseemos and Compartamos, suffered from difficulties attracting and then

retaining high-caliber staff. Identifying appropriate loan officers posed a challenge in Peru, where candidates with roots in the local areas proved often to perform best. Understanding the business of MFI clients turned out to be important and in the case of a rural expansion would require knowledge of the agricultural sector, as in Tanzania.

In Africa, the issue of staffing is even more pronounced than in other Regions because of educational constraints, higher employee turnover, hard living conditions, and poaching of trained personnel. There were a number of IFC-supported projects where staff joined to receive good banking training and after some time went to other institutions as experienced middle managers. This is a positive spillover for the local markets; however, for the investee entities, it increased operating costs and reduced staff productivity. In these projects, the frequent changes of personnel have not been confined to second-level employees but have also happened with top-tier employees. Some operations have had more than four CEOs in five years. These changes affected the performance of the institution as the new employees and managers had to learn the specificities of the market.

IFC's efforts to establish MFIs in pioneering environments suggests that the institution is working at the limits of what is feasible with the business model of self-sustaining, commercially oriented MFIs. IFC works in countries with the lowest inclusion rates, and its volume of loans issued in these countries corresponds roughly to the share of the entire MIX market. As the MIX market data contains about 30 percent of NGO-type of MFIs, IFC's presence in these low inclusion countries is remarkable – potentially suggesting it is at the boundary of what is feasible, at least given IFC's investment horizon and associated expectation when investment should turn profitable.

These MFIs issue loans that are larger than the ones of their peers, which in general should allow them to produce sufficient yields. But in reality, loan volumes increase too slowly and resource mobilization is too costly so that many of these MFIs take longer to become profitable, often four or even five years for greenfield operations. This poses challenges for IFC scheduled exit, as these get delayed as well. IFC work quality was found high and is therefore not a factor for the low business success. This raises the question of whether IFC's – beyond which catering to the very low retail end of the market would only be feasible with subsidies.

#### **IFC ADVISORY SERVICES IN SUPPORT OF MFIS**

Fifteen percent of IFC advisory work supports financial inclusion through downstream related advisory projects. Of 1,612 advisory mandates that IFC implemented during the evaluation period FY07–13, 322 projects (20 percent)

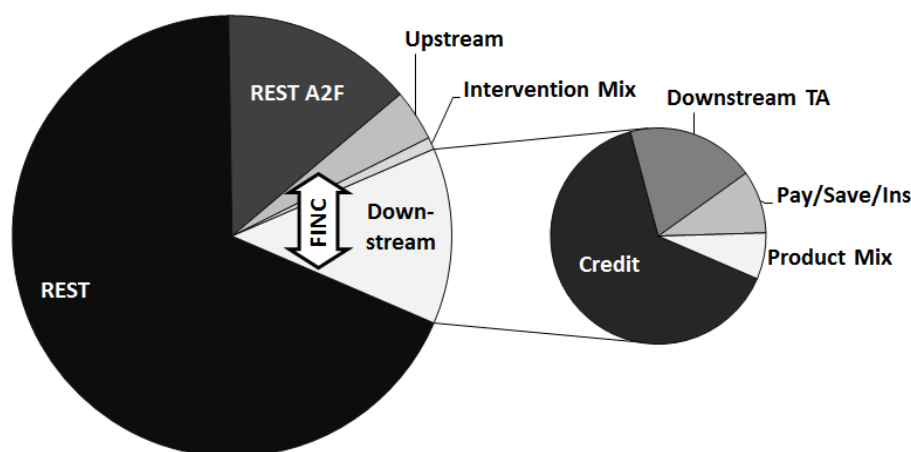
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focused on supporting financial inclusion. Financial inclusion projects fall typically within the access to finance business line which together with all other access to finance projects implemented 513 projects. This business line is the second-most important business line of IFC advisory, only surpassed by sustainable business advisory, with 555 projects.

**Most IFC advisory projects are in support of MFIs; that is, they are downstream advisory.** Of these 322 financial inclusion advisory projects, only some 60 address issues related to the policy and regulatory environment, hence are upstream projects; most advisory projects (262) are genuine downstream projects or 15 percent of all advisory projects (figure 4.16).

**Figure 4.16. IFC Advisory in Financial Inclusion**



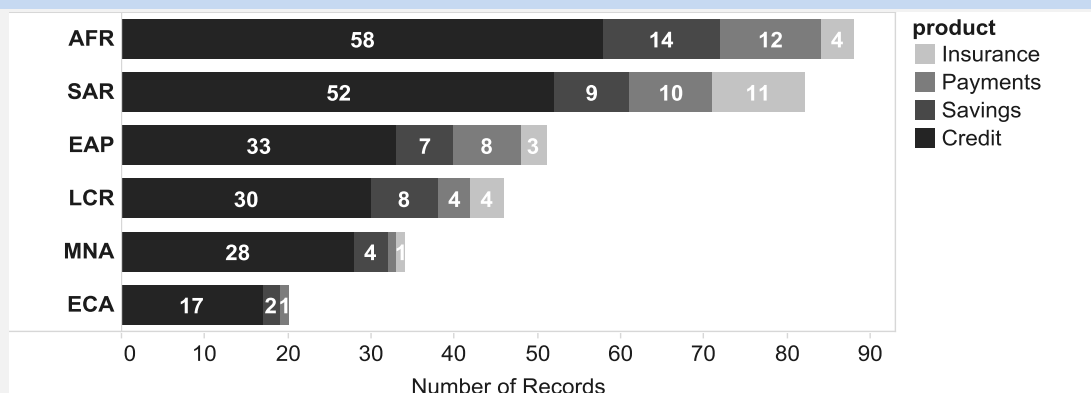
Sources: Business Warehouse; IEG portfolio analysis.

Note: FINC = Financial inclusion portfolio; A2F = Access to Finance business line; TA = Technical assistance.

The majority of these IFC advisory projects addressed credit-related financial inclusion issues, with a varying share of projects related to payment systems, savings, and insurance. One hundred twenty-eight projects (63 percent) of IFC advisory projects address credit issues and only about 10 percent payment, savings, or insurance-related issues. Looking at the portfolio over time, every year about 60–80 percent of all financial inclusion advisory work deals with projects involved in the provision of credit; between 5 and 20 percent are devoted to payments and 7–27 percent to savings; insurance is addressed the least, with about 2–8 percent of projects, depending on the year. Figure 4.16 shows these proportions. Over the time period FY07–13 the share of non-credit-related projects varied but did not show an increasing trend.

Africa and South Asia were the regional focus of IFC's advisory work. About 88 (27 percent) projects took place in Africa, followed by the South Asia Region with 82 projects (26 percent). Sixteen percent and 14 percent took place in East Asia and Pacific and Latin America and the Caribbean, respectively; and Europe and Central Asia attracted the fewest projects, with only 6 percent. This regional pattern aligns well with the finding of chapter 2 that indicated that IFC advisory (together with World Bank lending) strongly focuses on countries with the lowest financial inclusion rates. In fact, IFC advisory overemphasizes these low inclusion countries, underscoring their strategic relevance. Across most Regions, the share of credit-related projects hovers around 65 percent, with the exception of the Middle East and North Africa and Europe and Central Asia Regions, where they account for 85 percent (figure 4.17).

**Figure 4.17. IFC Advisory across Regions**



Sources: Business Warehouse; IEG portfolio analysis.

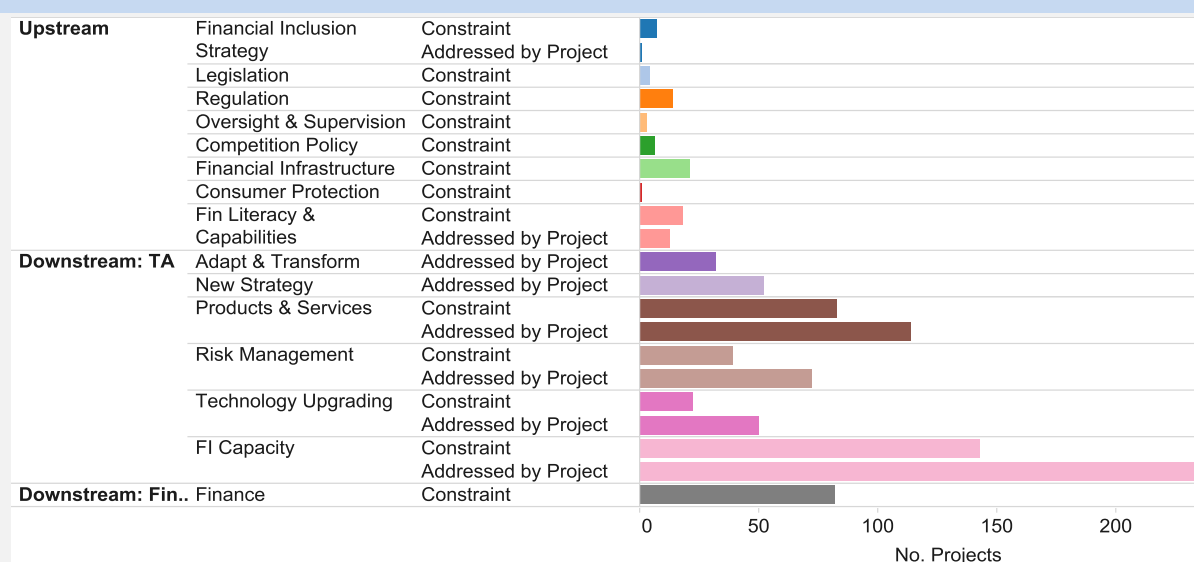
Note: AFR = Africa; EAP = East Asia and Pacific; ECA = Europe and Central Asia; LCR = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia.

IFC advisory projects build capacity with local MFIs, help client MFIs develop products and services, and improve risk management processes. Looking at the constraints that IFC advisory mandates address (figure 4.18) reveals that they mainly aim at building capacity with MFIs; that is, they train MFI staff in managing their institutions and associated processes. With about 150 projects, this is the single most important focus area. Developing product and services for MFIs is the second-most important area they focus on, followed by improving risk management, strategy development, technology upgrades, and adaptation and transformation, that is, assisting non-deposit-taking MFIs in “graduating” into deposit-taking institutions.

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**Figure 4.18. IFC Advisory in Financial Inclusion**



Sources: World Bank database; IEG portfolio analysis.

Note: FI = financial inclusion; Fin = finance.

## RESULTS AND FACTORS OF SUCCESS AND FAILURE

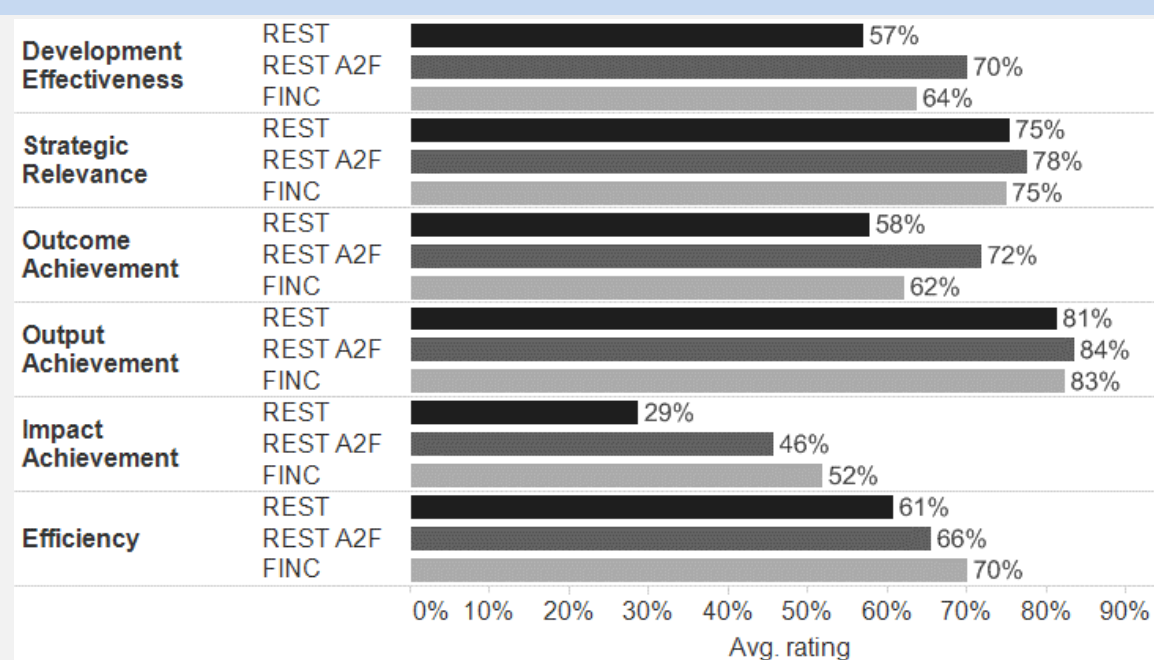
### Development Outcome Ratings

Measured by their development outcome rating, about two-thirds (64 percent) of IFC downstream advisory services are rated satisfactory or better, that is, are successful. This success rate corresponds roughly to the remaining access to financial advisory portfolio, where 70 percent are rated successful, but above the success rate of the portfolio as a whole, of which 57 percent are rated successful.

Looking at the components that jointly make up the development outcome rating, IFC advisory projects rate high on output achievement (83 percent rated successful) and on strategic relevance (75 percent rated successful). Performance drops when it comes to outcomes achievement, for which only 62 percent of projects are successful – 10 percent lower than the average access to finance advisory service.

IFC advisory projects stand out for their high-impact achievement – at least in relative terms – and for their high level of efficiency, compared with other advisory services. Overall, 52 percent of projects achieve their impact, below the 62 percent of projects that still achieved their (more immediate) outcomes. In relation to other IFC advisory projects, 52 percent is a relatively high success rate. About 46 percent of the remaining access to finance projects achieve their impacts – and only 29 percent of the advisory portfolio as whole (figure 4.19).

Figure 4.19. IFC Advisory in Financial Inclusion Outcome Ratings



Source: World Bank database; IEG portfolio analysis.

Note: FINC = financial inclusion; REST A2F = Remaining Access to Finance business line.

### Drivers of Success and Failure by Engagement Type

IFC advisory projects pursue a range of objectives, including capacity building, product development, and risk management advice. None of these engagements is the same; each is driven by different contexts, client interaction patterns, and level of technical depth. A disaggregated analysis is hence likely to generate more useful lessons to be learned. To this purpose, the below paragraphs summarize drivers of success and failure for the major three type of engagement of IFC advisory: building capacity (which is often used to pursue transformations of non-deposit-taking MFIs into banks), product development, and risk management (figure 4.20).

Most IFC advisory projects include activities that aim to improve the institutional capacity of MFIs and financial intermediaries. As one of the most used methods for improving institutional capacity, staff training activities achieved their results in approximately two-thirds of evaluated IFC Advisory Services projects.

Factors that facilitated the success of such capacity building activities include client commitment, relevance and tailoring of training activities, choice of project partner (training facilitator), and appropriate target setting. In Pakistan, for example, the selection of a high-quality project partner helped with the successful delivery of a training program that focused on improving staff capacity to operate and better understand the newly installed management information system. These same

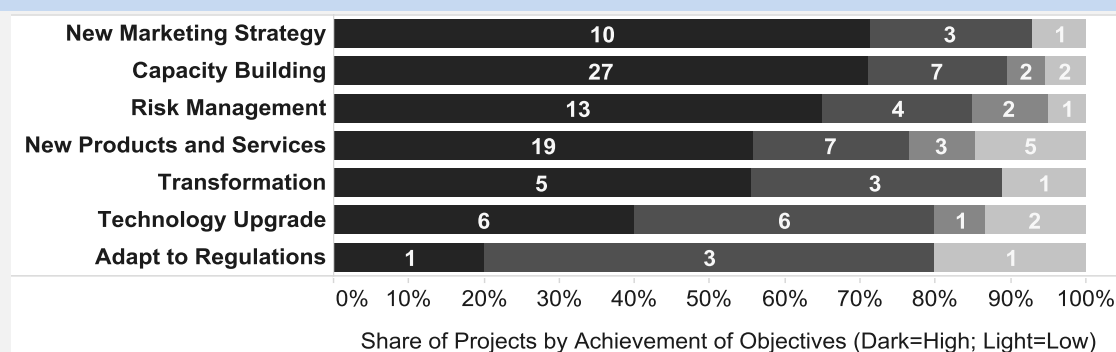


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factors were also observed in projects that failed to deliver their intended benefits, though in these instances they had a negative effect on performance. Weak client commitment and client reluctance to pay for in-kind contribution of staff time and facilities needed to complete trainings were factors that negatively affected performance. IFC's technical assistance grant to Progresemos in Mexico faltered, as it left the selection of the facilitator to the client who then partnered with a provider that advised on lending techniques that were not suitable for the local context.

**Figure 4.20. Achievement of Objectives in IFC Advisory Downstream Projects**



Source: IEG portfolio analysis.

Capacity building and staff training activities enable the successful delivery of other related activities in the IFC advisory portfolio. Having strong institutional capacity and well-trained staff is an enabler of the successful delivery of other project activities; in fact, capacity building and training activities are often interlinked with the delivery of other services. For example, in the above-mentioned case in Pakistan, training on the use of new information systems in Pakistan helped the institution ensure the successful adoption of this new technology infrastructure. The project tailored its consultant services and placed in-house team for 12 months, which allowed for fast resolution of information technology issues; evaluation documents referred to this as best practice. Other key areas of IFC advisory support include risk management, new product and service development and adoption, and transformation support.

Importantly, IFC advisory projects supported transformation of MFIs and NGOs into regulated microfinance banks. Ten percent of the evaluated IFC advisory portfolio ( $n = 90$ ) had transformation activities embedded in project design. Supporting transformation projects often included feasibility studies, pre-incorporation costs, risk management improvements, information technology upgrading, as well as other capacity building and training activities. In the Pakistan example, IFC advisory supported the institution with a feasibility study, an independent audit of the portfolio and licensing costs, and information technology

system support. The transformation was successful, and IFC made an equity investment in the new bank.

Transformation from an NGO to a microfinance bank was achieved in just over half of the relevant project portfolio; however, most projects faced internal and external factors that delayed results. Although Kyrgyz Republic's Bai Tushum was able to transform into a deposit-taking institution, at first, it was not able to increase deposits, preventing the institution from transforming "in practical terms"; the institution received its company license in 2009 and deposit license in 2011. A mix of internal, external, and project-specific factors was responsible for this delay, according to evaluation documents: optimistic time frame under the project design and low absorptive capacity of the World Bank and rigidities related to the regulators' approval process for the bank licensing application. As of June 30, 2014, Bai Tushum had provided loans to over 45,182 customers, an increase of 45.5 percent over the same indicator in June 30, 2013. Bai Tushum expanded business considerably upmarket and increased the average loan size to \$2,200 (IFC 2014).

Similarly, in Colombia's WWB Popayan, a nonsupervised NGO aiming to transform into a bank, the company delayed transformation and deposit taking, as the management was conservative and did not want to request a banking license until the institution was completely prepared to operate as a regulated entity. This conservative approach was in response to experiences of other local MFIs that had requested banking licenses before being prepared to operate as a bank.

IFC advisory projects helped MFIs and financial intermediaries develop new products and services. Those supported by IFC Advisory Services vary significantly depending on the type of institution being served and needs of the client and market: from rather targeted and tailored designs, to the use of technology and data-driven decision making, to cases where product design is aligned with corporate or parent company processes and specifications. The successful development and rollout of new products and services is closely related with staff skills and training, appropriate tools and systems, and client and manager buy-in.

In Pakistan, IFC advisory was successful in helping the Tameer Bank introduce mobile banking in nonrural areas, given the results of a feasibility study that identified over-expansion into rural areas as a potentially "huge burden on the World Bank's internal resources and capacity." On the other hand, two projects under the African Micro, Small and Medium-Size Enterprise program were not able to launch as many new products as planned given the parent company's policy that all products be tested and developed in Kenya before they can be customized and

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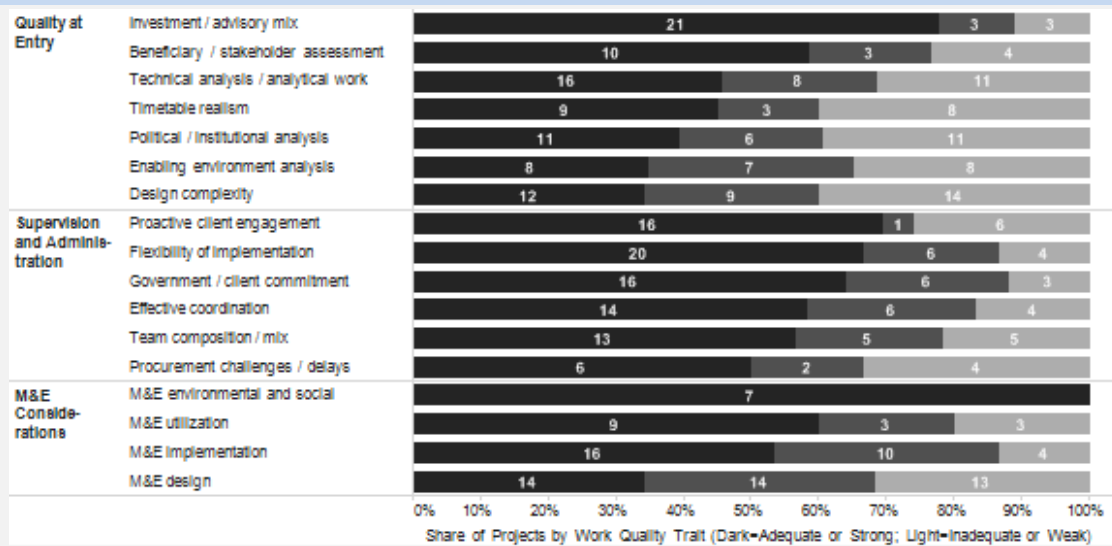
rolled out at the subsidiary level (see Tanzania Diamond Trust Bank and Burundi Diamond Trust Bank).

#### ***Work Quality Drivers at Various Stages of the Project Cycle***

Across all IFC downstream advisory projects, certain work quality drivers emerge. Figure 4.21 illustrates the drivers of success and failure across all IFC advisory projects along the entire project cycle, from quality at entry, supervision and administration to M&E. Starting with what drove quality at entry, more than half of the projects evaluation reports referred to the right mix of investment and advisory services. In Tanzania, for example, the Gender Entrepreneurial Management Project with Exim Bank attributed the program's success to its combined investment and advisory approach and its close working relationship with the Finance and Markets Global Practice team, stating that "without the one team approach, [the team] would not have been able to design and get the program off the ground" with adequate beneficiary and stakeholder assessment.

IFC's advisory and investment mix and successful coordination with the World Bank had overall very positive results. The main conclusion that can be drawn from World Bank Group coordination across units is that this interaction was key to success of the financial inclusion agenda across the objectives. In the case of Pakistan and specifically IFC interventions, success seems to be rooted in joint investment and advisory interventions. This is particularly true in the case of the three phased interventions for Tameer Bank, for which timeliness and appropriateness of the joint interventions were the main drivers of success. Another example of successful IFC advisory/investment coordination is the support for Bai Tushum bank in the Kyrgyz Republic. The second-most prominent driver of success at the quality at entry stage was beneficiary and stakeholder analysis, successfully done in 58 percent of projects (figure 4.21).

Figure 4.21. Work Quality Drivers in IFC Downstream Projects



Source: IEG portfolio analysis.

The single most important factor that resulted in failure at the stage of quality at entry was design complexity. This was seen as a challenge in almost two-thirds of IFC downstream advisory projects (figure 4.20). In India, for example, a recent project completion report suggests allowing time and resources to structure complex advisory projects that have several components and different several performance indicators and conditions on disbursement.

Looking next at supervision and administration, proactive client engagement was referred to most often as a success driver. In Mexico's Compartamos, for example, the commitment of the sponsor was key to the success. Conversely, project delays were the most frequently identified deficiency, due to a range of issues including turnover in IFC project team leadership such as in HF Cajas Mexico projects, funding constraints on the client side in the transformation projects of Bai Tushum, and external factors such as regulatory requirements seen in a range of greenfield operations in Africa.

Last, with regard to project M&E, failures to establish a clear baseline, indicators, and targets made measurement and attribution of project results difficult in two-thirds of evaluated IFC advisory projects. Furthermore, failure to identify and track the right set of indicators can prevent projects from identifying issues early on. In Tanzania, lack of indicators on staff productivity meant that IFC was unaware of the bank's staff turnover problems until the end of the project. The type and quality of indicators identified is also relevant and can be a challenge to proper measurement and attribution as shown in the case of the Burkina Faso and Malawi African Micro, Small and Medium-Size Enterprise projects. In Burkina Faso, no targets were set for

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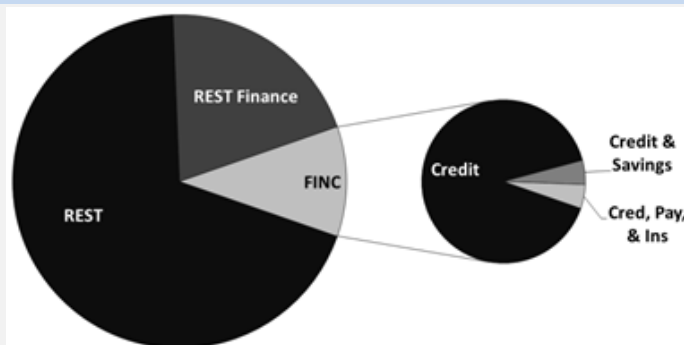
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the project's nonperforming loan (NPL) indicators, whereas in Malawi, the project completion report was difficult to validate because it contained unclear attribution claims and different versions of expected targets.

### MIGA Support to MFIs

Eleven percent of MIGA's portfolio supports financial inclusion through political risk insurance guarantees. Of the 197 guarantees implemented by MIGA between FY07 and FY13, 25 have components that support financial inclusion in client countries (figure 4.22). MIGA's financial inclusion support also accounted for 4 percent of its total gross exposure during this time period. Financial inclusion projects lie exclusively in the financial sector; though they account for 30 percent of projects, financial inclusion projects represent only 10 percent of volume in this sector. On average, financial inclusion projects are smaller than the rest of the financial sector portfolio with projects averaging \$25 million compared with just over \$100 million for other financial sector projects. All of MIGA's guarantees are in support of financing MFIs, that is, they are "downstream" support. None of the MIGA guarantee projects has thus far been evaluated, making an assessment of the effectiveness of MIGA's support difficult. The following section therefore focuses on providing an overview of MIGA's activity level in the financial inclusion space.

**Figure 4.22. MIGA Guarantees in Financial Inclusion as a Share of Its Total Portfolio**



Source: IEG portfolio analysis.

Note: FINC = financial inclusion portfolio.

Through its guarantees, MIGA has supported financial sector development in client countries by working with MFIs and financial intermediaries. MIGA's support to MFIs includes guarantees through its Small Investment Program that will support the creation and subsequent expansion of GeoCapital Microfinance LLC, a fast-growing MFI in Georgia. It also supported the creation of a licensed commercial bank, BRAC Afghanistan Bank, where BRAC NGO is the bank's sponsor and Afghanistan's primary microfinance provider.

In Pakistan, MIGA supported the coverage of an equity investment in Kashf Foundation, a local NGO established to reduce poverty and empower women through the provision of microfinance services. Kashf Microfinance Bank was created to focus on lending and taking deposits from microentrepreneurs and small businesses in Pakistan. MIGA provided three contracts of guarantee; the project was led by IFC, which provided an integrated investment and advisory services package to the project enterprise. MIGA's guarantee with Erste, a Serbian bank, aimed to supported productive businesses through the extension of affordable credit.

Prominent in the financial inclusion portfolio is MIGA's master contract issued with ProCredit Holding. Headquartered in Germany, ProCredit Holding is the parent company of 21 banks (ProCredit Group) and provides finance to some 750,000 very small, small, and medium-size enterprises across the world. The guarantee issued by MIGA aimed to relieve ProCredit Holding from German capital adequacy ratio requirements, thereby freeing funds to be injected in its subsidiary banks, allowing these banks to increase lending activities. (*Note:* Although ProCredit subprojects were covered under two master contracts [each with a unique project identification], these subprojects were recorded as a single project for each host country. In cases where the host country had more than one guarantee, the collection of guarantees for that host country counted as one project [Georgia, Serbia, Ukraine]).

MIGA's financial inclusion support was heavily focused on delivering credit-related services to the poor. Nineteen of the 21 projects focused exclusively on credit, while two projects provided a mix of credit and other services. Looking at the portfolio over time, most of MIGA's activity is concentrated in the latter half of the evaluated period. This concentration is due to a group of MIGA guarantees issued under a master contract with ProCredit Holding. Sixteen of the 25 financial inclusion projects belong to these two master contracts.

Because so much of MIGA's portfolio is dominated by an intervention with a single institution, MIGA's engagement moves with ProCredit's strategy. If ProCredit's strategy evolves over time, moving out of the micro- and very small-enterprise finance market, MIGA risks losing most of its financial inclusion portfolio.

### **A Look beyond Credit**

This section looks at Bank Group interventions that support the provision of financial services other than credit. Most of the discussion in this report thus far has addressed issues related to credit. This partly due to the historic genesis of financial inclusion, which has its roots in microcredit and only gradually embraced other

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financial services as well, such as payment, savings, or insurance. It is also partly because most of the World Bank Group's interventions are related to the provision of credit. Yet about 30 percent of Bank Group interventions – and 50 percent of World Bank's recent AAA work – goes beyond credit (see chapter 2, figure 2.4).

Getting a better understanding whether and under which circumstances access through payment systems leads to financial inclusion is one of the focus areas of a recently launched global work program of advisory services and analytical support. Based on a limited literature, noncredit financial services appear to have a higher potential to benefit the poor. Payment systems in particular seem to be a plausible entry for the poor to connect to the formal financial system. High dormancy rates of newly opened accounts in India and low usage of newly opened accounts in low-income and lower-middle-income countries more generally casts doubt on the assumption that access necessarily leads to inclusion (Kelly and Rhyne 2015).

Recognizing this challenge, the World Bank is in the process of launching a program of about 15 advisory services and analytical support initiatives in a range of countries. A global program of an additional 27 such projects focus on consumer protection and financial literacy aspects with completion dates in FY15–18. Jointly, these advisory services and analytical support activities will be important efforts in understanding financial inclusion aspects beyond credit. Because few of these activities have yet been implemented and none yet evaluated, the following discussion focuses on those interventions for which the outcomes were already subject to project-level evaluations.

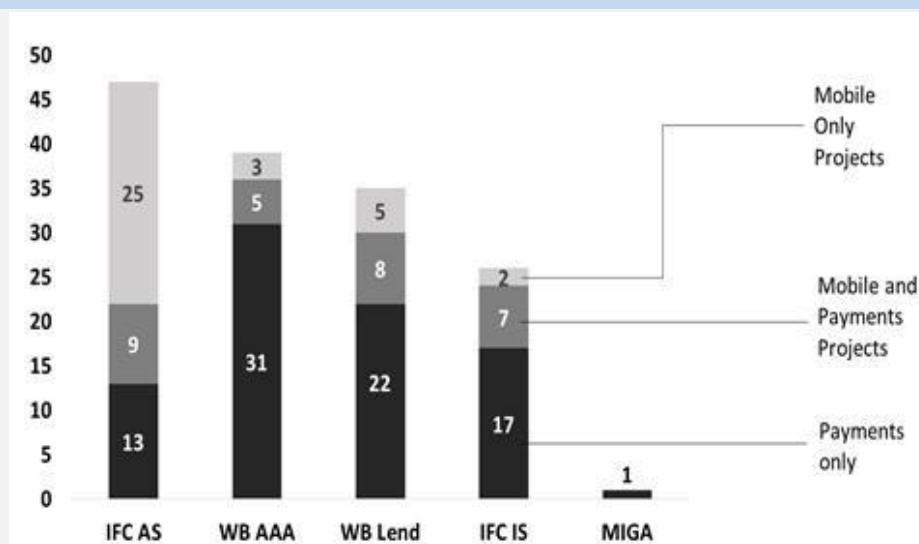
#### **TECHNOLOGY TO DELIVER ON FINANCIAL SERVICES: PAYMENTS**

Mobile channels<sup>11</sup> have the potential to provide access to financial services, in particular to payment systems in ways that are more cost-efficient, safe, and convenient than existing alternatives. In recent years, mobile channels are also being piloted for the provision of savings, credit, and insurance services. In many developing countries, mobile network operators (MNOs) already have unique assets and incentives to deliver these services in a sustainable and scalable way: trusted brands, widespread distribution, and secured access to communication channels.

Looking at the broader space of payments, MFSs, and technology, advisory services are the most common tool of assistance. Across all 148 Bank Group interventions in this space, IFC's advisory services is the most important single source of support to mobile money and MFSs, whereas World Bank's AAA largely supports payment systems. The latter is also well aligned with the focus of World Bank lending, which is also on payment systems; these comprise national government-to-person payments, national person-to-person payments, online payments, international

remittances, and a general payment-related projects. Interestingly, IFC Investment Services also focus is on payment system and not on MFS (figure 4.23).

**Figure 4.23. World Bank Group Support to Payments and Mobile Money**



Source: The Global Index Database 2014.

Note: AS = Advisory Services; IS = Investment Services; Lend = lending; WB = World Bank.

Within the payment space, World Bank Group interventions mostly target international remittances (44 projects). This is followed by 15 on national government-to-person projects, 20 national person-to-person projects (26 online payment projects, and 50 projects supporting general payment-related matters). These numbers are cumulative across these interventions and many projects had overlapping components of these different payment types. Because of the potential that the current financial inclusion debate allocates to mobile money and MFSs, large parts of the following section discuss aspects of mobile money and challenges to its applications.

Looking specifically at mobile money, uptake of such services has been very uneven across the globe, largely concentrated in eastern Africa (figure 4.24). Between 2011 and 2014 the number of unbanked shrank by 20 percent, from 2.5 billion to 2 billion. Despite this progress, still more about half lack access to an account. Of the 54 percent of adults in developing countries who have an account, almost all have an account at a financial institution: only 1 percent has both a financial institution account and a mobile money account, and 1 percent have a mobile money account only.



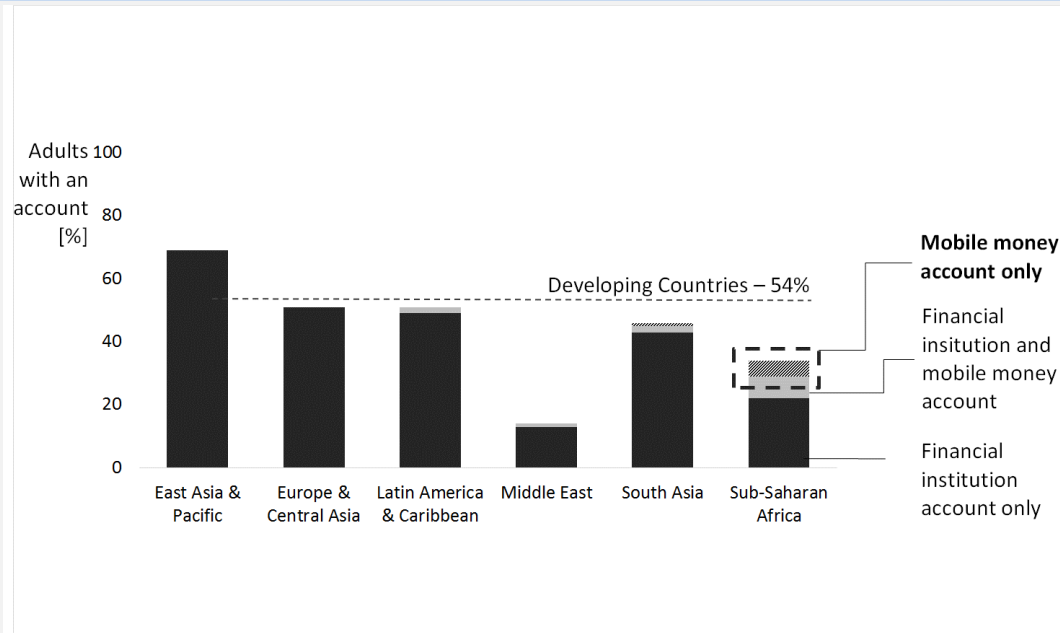
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The exception is Sub-Saharan Africa, where mobile money accounts drove the growth during 2014, making this Region the only one where mobile money is currently a major factor in providing the poor with financial services. Even within the Region, mobile account penetration is concentrated in eastern Africa where mobile account penetration increase by 9 percent, whereas accounts with a financial institution remained unchanged at 26 percent. In some of these countries, the growth in account ownership during 2014 was largely due to an increased mobile account penetration (like in Kenya or Uganda) – or almost entirely, as in Tanzania. However, a few countries outside Sub-Saharan Africa may be a fertile ground for mobile banking, like Indonesia where the recent policy reform, assisted by the World Bank Group, may have laid the foundation for future growth.

Mobile account penetration need not necessarily reach the poor – yet. Two contrasting cases are the neighboring countries of Kenya and Tanzania. In Kenya, adults in the poorest 40 percent are significantly more likely than adults in the richest 60 percent to have a mobile money account (27 percent versus 14 percent). In Tanzania, the growth in mobile account ownership account for almost the entire increase in overall account ownership, yet poverty is a barrier to access to mobile accounts: although account penetration increased overall by 23 percent (from 17 to 40 percent), increase in account penetration for the poorest 40 percent amounted only to 16 percent (from 7 to 24 percent), and account penetration grew by 26 percent for the richer 60 percent (from 24 to 50 percent). Kenya's higher level of mobile account penetration may partly be due to that fact that it was among the first countries (after South Africa) to embrace this concept (Findex data 2015).

**Figure 4.24. Account Penetration and Mobile Money Uptake Globally, 2014**



Source: The Global Findex Database 2014.

Originally conceived to reduce the switching of mobile phone clients to competing MNOs and increase average revenue per user, MNOs have led the deployment of mobile money, not banks. By 2014, there were 255 mobile money services available in 89 developing countries, corresponding to 61 percent of the developing world. During 2014 alone, mobile money was rolled out in six new markets: Dominican Republic, Myanmar, Panama, Romania, Sudan, and Timor-Leste (GSMA 2014). This trend was enabled by the parallel growth of mobile money agent networks that offer cash-in or cash-out services as low-cost alternatives to bank branches and even ATMs. The number of mobile money agent outlets grew by 46 percent during 2014, reaching a total of 2.3 million for 89 markets in developing countries – dwarfing ATMs and major remittance service providers in developing countries. Along with growth, competition also increased, with 52 markets having two or more providers.

Despite impressive expansion, mobile money is still largely used for payments services only. In any market, payment transactions in the form of air time top-up or person-to-person transfers are the dominant services offered by providers and used by customers. Air time top-up represented 62 percent of the total number of mobile money transactions performed in 2014; person-to-person transfers were 25 percent. In terms of transaction amount, person-to-person transfers, however, led, with 73 percent of the global mix. Savings, credit, and insurance constitute a very small portion in terms of transaction volume and amount. In recent research sponsored by the Financial Sector Deepening Trust of Kenya, it was found that approximately 34

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percent of the users of mobile money services maintained a small balance in their financial account, but only a small proportion (approximately one-sixth of users) indicated that they were in fact “saving.” The majority of mobile money customers were cashing out their transfers almost immediately.

Current challenges include interoperability and inadequate regulatory frameworks, affecting as many as 2 billion adults. With the growing number of service providers in a single market, the issue of interoperability among the different mobile money providers as well as collaboration among different mobile money providers, including banks, MFIs, insurance companies, and other financial service providers, become important. Regulators encourage interoperability among MNOs or direct MNOs to work with banks to offer mobile money services; however, because of monopolies and exclusivity arrangements of some mobile agent networks, such interoperability may be stalled, as has been the case, for example, in Kenya.

In addition, regulatory deficiencies pose a limit to growth. Only about half (42) of the developing countries with mobile money services (89)<sup>12</sup> have adequate regulatory frameworks, leaving the vast majority (1.9 billion) of adults in countries with nonenabling regulatory environments (GSMA 2014).<sup>13</sup> Of the 52 developing countries where mobile money is not yet available, 12 have a regulatory approach that slows down the launch of services, adding another 204 million adults to the list of those suffering from lack of enabling environment. Key regulatory challenges are summarized in box 4.6.

#### Box 4.6. Regulatory Challenges

There are two main types of mobile money deployments: the MNO-led model and the bank-led model. For the MNO-led model, the MNO acts as a de facto bank. This model places most of the regulatory responsibility on the MNO, and mobile money agents play a central role. The most successful MNO-led model is M-PESA. MNOs have been successful throughout the world to increase subscriber base, but they have limited financial service discipline and are weak on compliance issues such as anti-money laundering and know-your-customer requirements. MNOs generally lack experience in financial services and payments risk as well as the regulatory and legal governance of payment systems.

Bank-led mobile means that a bank offers financial services to their account holders through a network of agents and also through online account services. Unlike MNOs, banks are best positioned to employ risk management programs that ensure regulatory compliance for money laundering and other risks; however, banks are naturally risk-averse and will only launch a new service once it has been proven to be secure. Banks in developing countries have been slow to offer MFSs because of the perceived lack of return on capital investment.

The mobile money industry also developed a hybrid model in which MNO Telenor purchased a 51 percent stake in Tameer Microfinance Bank in Pakistan. Without interoperability between MNOs and banks, both MNO-led or bank-led models are closed-loop services. The lack of interoperability acted as a major block for mobile money services to reach scale. The regulator plays a key role in facilitating this interoperability between two main players, namely MNOs and banks. For the successful deployment of mobile money, collaboration is also necessary with other stakeholders in the mobile ecosystem, including airtime agents, telecom retailers, and regulators (Jenkins 2008).

Mobile money regulations have been evolving, and there has been a sudden change of course that affected mobile money business directly. In Nigeria, the Central Bank decided to only allow bank-led and non-MNO-led third-party service providers to operate mobile money services in late 2012 after seeing the virtual monopoly created by M-PESA in Kenya. The Central Bank of Nigeria viewed that a dominant MNO-led mobile money provider could quickly create a monopoly and might pose a systemic risk for the country. MTN Banking was the leading MNO as well as the largest mobile money service provider in Nigeria before this new regulation. The MNO had to suspend its mobile money service since the Central Bank's guidelines prohibit MNOs from playing a lead role in any mobile money service.

Source: Jenkins 2008.

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### ***World Bank Group Engagement in the International Policy-Setting Arena***

The World Bank has exercised intellectual leadership in the area of global remittances by influencing the international policy agenda. Given the importance of remittances for the poor (see chapter 1), the World Bank assumed leadership of a Global Working Group on Remittances, which was authorized in 2007 and created in 2009. The work of this group is credited with stimulating global and country-level reforms that have significantly reduced the weighted average cost of remittances, resulting in tens of billions of dollars of savings to migrant workers and their families. Remittance costs are tracked through the Remittances Price Worldwide databased, hosted by the World Bank.

The World Bank Group has also played a role as thought leader in setting the global agenda on *digital* payments for financial inclusion, along with a small group of international policy makers (box 4.7). For the G20 initiative of mobile financial inclusion, World Bank Group has been providing intellectual support through its analytic work. The World Bank's Development Research Group produced the report *The Opportunities of Digitizing Payment* (World Bank 2014) to explain how digitization of payments, transfers, and remittances contributes to the G20 goals of broad-based economic growth, financial inclusion, and women's economic empowerment with evidences from the actual deployed of mobile money and MFS.

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More specifically, the World Bank has also been spearheading efforts in the areas of retail payment infrastructure by establishing Payment Aspects of Financial Inclusion Task Force with the Committee on Payments and Market Infrastructures in November 2013.<sup>14</sup> Payment Aspects of Financial Inclusion will support the Financial Inclusion Action Plan approved by the G20 at the Seoul Summit in November 2010. Building on the work already carried out by Committee on Payments and Market Infrastructures and the World Bank, this task force is expected to fill the gap in international financial institution guidance and recommendations. It aims to publish a report in the second half of 2015.

Similarly, IFC has also helped to advance the financial inclusion agenda in Africa through its partnership with the MasterCard Foundation. The Partnership for Financial Inclusion in Sub-Saharan Africa involves \$37.4 million in funding. The two main objectives of this partnership are to expand microfinance and advance MFSs in Sub-Saharan Africa.<sup>15</sup> A third objective of this initiative is knowledge sharing and learning activities. The partnership aims to scale up microfinance and accelerate the development of MFSs in Sub-Saharan Africa to reach a total of 5.3 million previously unbanked customers by 2017.

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#### Box 4.7. Important Players in the Mobile Money Space

**The Groupe Speciale Mobile Association** represents an interest of MNOs and related companies and has been the one of the main players in promoting mobile money in developing countries with its effort through Mobile Money for the Unbanked. Groupe Speciale Mobile Association was formed in 1995 as an association of mobile operators and related companies, and its mission is to support the standardization, deployment and promotion of the GSM mobile telephone system. The Mobile Money for the Unbanked program is supported by the Bill and Melinda Gates Foundation, the MasterCard Foundation, and Omidyar Network.

**The Gates Foundation** has been actively engaging with the agenda of MFS and financial inclusion. Under its Financial Services for the Poor initiative, it has committed nearly \$500 million since 2006 to explore ways to increase access to financial services. The Gates Foundation's Financial Services for the Poor program aims to play a catalytic role in broadening the reach of robust, open, and low-cost digital payment systems, particularly in poor and rural areas – and expanding the range of services available on these platforms. The Gates Foundation has also been an investor in this space. For investment activities, investors such as Omidyar Network have been supporting a large number of start-up mobile money providers and FinTech investments. A large number of venture capital and private equity funds have also been active investors in early or growth stage companies in this space.

*Source:* IEG staff.

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***Country- and Project-Level Engagement of the World Bank Group***

At the country level, with a few exceptions, the World Bank Group has not been a major player in setting the agenda for regulatory reforms to facilitate a wider use of mobile money for broad-based financial inclusion. In the majority of developing countries, IEG found that the World Bank Group has neither led upstream engagements that would have helped to develop enabling regulatory frameworks nor made major technical or financial contributions to mobile money and MFS deployments, except in a few successful cases.<sup>16</sup> For example, World Bank Group has not worked with M-PESA in Kenya, nor did it play a major role in the growth of mobile money in Tanzania, two East African countries pioneering mobile money for about a decade.

There are also countries where the World Bank Group's work has helped advance the agenda. For example, in Indonesia the World Bank's knowledge products, such as the 2010 report on Improving Access to Financial Services in Indonesia, addressed the importance of financial inclusion including mobile banking and mobile money. This report and a continuous flow of cutting-edge and quality knowledge of financial inclusion issues by the World Bank were critical and complementary to the government program of financial inclusion, as confirmed by IEG's mission.

The World Bank implemented 88 projects related to mobile money and payment systems, primarily assisting countries with regulatory barriers. Of these, 88 projects implemented during the period from FY07 to FY14, two-thirds (67 percent) focused on countries with regulatory barriers as per Groupe Speciale Mobile Association classification, and 33 percent on the countries that already had enabling regulatory environments. This is a sign of strategic relevance of Bank Group projects, given the need for regulatory reform.

For IFC, the focus is more on countries with already-existing enabling environments, where IFC supported 12 projects, compared with 10 projects in countries with regulatory barriers. This is understandable, as the financial service providers that IFC invests in would require a minimum of regulatory stability. Interestingly, regulatory barriers do not seem to necessarily affect the scale of IFC-supported operations or the commercial viability of mobile money services. For example, IFC supported the deployment of mobile money in countries with regulatory barriers as per Groupe Speciale Mobile Association classification, that is, bKash in Bangladesh and Easypaisa in Pakistan. Both companies have been able to scale up their operations to reach a large number of previously underbanked and unbanked populations.

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Factors such as the size of the potential market, the lack of competition, the gap between mobile phone penetration, and the access to a formal banking service have more influence over the performance of mobile money deployments for the initial stage of payment services than the regulatory environment. For example, bKash in Bangladesh succeeded in addressing this gap between the low level of the formal access to financial service and mobile phone subscription, and it has increased its customer base to more than 11 million in just within two years of its operation.

To achieve the broad-based concept of financial inclusion to offer savings, credit, and insurance in addition to payment services and over-the-counter transactions is an important issue that needs to be addressed by regulators and industry players. Over-the-counter transaction means that at least one end of the mobile money domestic transfer is conducted through agents with unregistered mobile money customers without the individual mobile wallet of the user (either the sender or the receiver or both). These transactions have helped rapid expansion of mobile money services in countries such as Cambodia, Bangladesh, and Pakistan. In Pakistan, this type of service represents more than 90 percent of mobile money transactions.<sup>17</sup> This widespread phenomenon in developing countries may well be one of the major obstacles to realizing the concept of financial inclusion, as it would trap the industry to offer only payment transaction services such as domestic people-to-people transfers and bill payments with these unregistered customers, without access to savings, credit, insurance, and other services by the poor.

IFC has generally been opportunistic in both providing advisory services and has invested in rather a limited number of mobile money or payment services providers with mixed financial and development results. IFC invested in just a handful of investments totaling \$54.3 million in nine equity investments for mobile money and FinTech companies by the end of 2013, while IFC's advisory service committed over \$36.9 million in 34 projects as of January 2014.

For some of its investments, IFC took risks by investing early when its client companies were at the initial stage of its operation (for example, companies like bKash in Bangladesh and FINO in India) before establishing solid revenues and profitability. It appears IFC had a good additionality for supporting these companies at the start-up phase. For bKash, IFC was an early investor in 2013 before an investment by the Bill and Melinda Gates Foundation in 2014; however, the Gates Foundation provided \$10 million in grants to bKash, which was one of the critical factors in bKash's success. The grant supported implementation and technical assistance of new mobile money services. This technical assistance was implemented by the consultancy firm Enclude. It provided a comprehensive assistance by fielding consultants in Bangladesh and supported bKash's market research, financial

modeling, business and capital planning, agent network setup and rapid rollout, and the implementation of a risk management program.

### **Results**

Across all payment and mobile money-related projects, the majority were successful; however, few projects were evaluated. Most projects evaluated were World Bank lending projects in the payment space of which the large majority (15 of 16 evaluated) were successful. For example, the World Bank's Development Policy Loan in Mexico<sup>18</sup> aimed to enhance access to finance by improving the enabling environment and financial system stability, including removing the barriers to mobile payments system. The mobile banking system was developed after this project by combining the new regulations supported by this intervention with the already-existing banking regulations. Four of six evaluated IFC advisory projects were positive, and two were rated negative by way of development outcome. For IFC investment projects, two were positive and one negative.

Too few projects on mobile money have been evaluated to derive statistically representative conclusions; hence the below discussion focuses on illustrating drivers of success and failure. For example, with IFC's combined investment and advisory services support, FINO, an Indian financial inclusion solutions and services company, succeeded in increasing an access to financial services in rural communities. Through its 32,000 business correspondents, rural client enrollments have increased substantially. More than 10 million new customers were added in 2011, with another 12 million new customers in FY12. Another joint investment and advisory project to support a new mobile banking operation in the Europe and Central Asia Region did not successfully reach the targeted number of active customers for its new service.

For the companies offering payment services and mobile money, supported by IFC's investment or advisory services, results so far have been mixed in terms of commercial viability, sustainability, and development impacts. Some of IFC's client companies have shown commercial viability of mobile money or payment business by generating profits with a substantial increase of its customer base, while others have faced difficulty operationally or financially as they struggle to reach scale. The mixed results of IFC investments are not surprising, considering the status of the mobile money industry. The successes of M-PESA, bKash, and a few additional mobile money deployments are still the exception, and not the norm. In fact, as noted in the latest 2014 Market Monitoring Unit report, the vast majority of mobile money deployments launched to date suffer from underinvestment and struggle to



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become profitable, while some succeeded in reaching scale and generating sufficient revenues from mobile money operations.<sup>19</sup>

bKash is one of the successful IFC investments so far for mobile money as it has increased its customer base substantially. bKash started its commercial operation in the second half of 2011, grew its customer base to 2 million accounts by the end of 2012, and increased to 11 million registered accounts by the end of 2013. bKash now has over 5 million MFS accounts, through which low-income Bangladeshis are conducting more than 400,000 transactions per day through more than 50,000 financial service agents. Although Bangladesh's central bank has approved more than 20 licenses to offer MFSs, bKash has a market share of 50 percent of the transaction volume.

In Pakistan, IFC and CGAP successfully helped deploy new mobile money services for Tameer Microfinance Bank. It has expanded access to financial services to geographical Regions that were hard to reach through conventional banking channels. Mobile money deployment has enabled the bank to serve more than 94,000 clients and more than 190,000 microsavers (9 percent and 7 percent of market share, respectively) and has over 70,000 mobile money accounts.

IEG found that two phases of advisory services to Tameer Microfinance Bank effectively assisted the greenfield MFI to upgrade its technology, roll out a mobile banking product, and train staff to use the new information management systems and branch managers in other areas, including human resources and marketing management. IEG's review of the first project found that it was a very successful project in terms of development results as IFC and CGAP helped the bank introduce a new mobile money service. CGAP had an important role as it introduced Tameer Microfinance Bank when it was a relatively small MFI to Telenor, one of the major MNOs. Telenor took a 51 percent stake in the bank to benefit from mobile money deployment. CGAP also provided grant funding for rolling out the product. The main success drivers of this project includes IFC joint advisory and investment operation, coordination with CGAP, client company commitment and involvement, and good quality of consultant work.

IFC supported WIZZIT, the third-party mobile money processor in South Africa, with both advisory and investment operations. In 2004, WIZZIT started to provide standard banking services via mobile phones to the unbanked and underbanked populations, with the notion that the poor need full banking services. In 2008, CGAP also offered a grant of technical assistance to test different approaches to customer acquisition to achieve a steeper growth. Its operation has been facing a number of

issues from finding a suitable banking partner to identifying financial products that are attractive to the poor.

In comparing the success of M-PESA, a Harvard Business School case study (Rangan and Lee 2010) points out the problem of the WIZZIT business model as follows: “Founders of WIZZIT were very creative in bringing the costs down dramatically and improving access to banking services, so the poor could afford to bank. The problem is that this is not the way that the poor think of money. They hardly have any savings. Their main need is money transfer.” Regulatory uncertainty and changes on know-your-customer (KYC) requirements, such as anti-money laundering and combating the financing of terrorism, also had negative impacts on the business of WIZZIT and MTN Banking, another mobile banking service in South Africa

Since mobile money deployments are new services and often start as greenfield start-up companies, it would make sense to support companies with both IFC Advisory Services and Investment Services operations. Grant funding from the U.K. Department for International Development to M-PESA and the Bill and Melinda Gates Foundation’s funding to bKash were instrumental to the success of these new mobile money deployments. IEG’s review of IFC’s portfolio finds that IFC also had a joint advisory and investment operation that supported the same client companies at the country level, including in Bangladesh, Pakistan, South Africa, and Vietnam with mixed results so far.

Although it is a mid-term review, an independent evaluation<sup>20</sup> of IFC’s partnership with the MasterCard Foundation confirmed a good work quality of the IFC team there and its collaborative approach to developing MFSs in Côte d’Ivoire. In the initial stage of the project, IFC worked with the industry players and the regulator to help develop market knowledge and explore business models by sharing knowledge and expertise at industry workshop in close collaboration with CGAP. With the presence of a local project coordinator and MFS specialist, the IFC team undertook market research with cocoa farmers and leveraged its existing relationships with a cocoa exporter to come up with a business model to pilot an MFS solution for cocoa farmers. The IFC team has also been working with the bank’s social safety net team to explore the potential of digitize the government-to-person payments.

## **SAVINGS**

About 20 percent (169 projects) of World Bank Group financial inclusion portfolio have a component addressing issues related to saving; however, only seven are stand-alone saving-focused interventions. These projects are evenly distributed across World Bank lending and IFC advisory and investment. Savings interventions

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are concentrated mostly in Africa and South Asia Regions, with 30 percent and 27 percent, respectively.

IFC got engaged in advancing the savings-related agenda of financial inclusion through its investment very recently. More than 80 percent of IFC investments in savings were approved between 2007 and 2013 and are concentrated mostly in the Africa and Latin America and the Caribbean Regions, closely followed by East Asia and Pacific and South Asia Regions.

IFC promotes savings in the majority of projects (more than 50 percent) through financing transformations of MFIs into deposit-taking institutions and setting up greenfields or new MFIs, which are then encourages to raise local deposit. Quite often, these interventions were indirectly supported by other Bank Group projects that provided upstream support to governments or central banks to develop regulations that enable the aforementioned transformations. Faulu Kenya is an example of the transformation of the MFI into a deposit-taking institution, which is also supported by technical assistance from IFC Advisory Services. The remaining investments mostly financed IFC investees that have successful operations, and IFC financing provides additional support to them for expanding their services to more beneficiaries by way of central bank regulations. FINO India is an example of a financial institution benefiting from the central bank's regulation to allow MFIs to offer broader range of financial services (including savings), after which IFC Investment Services financed FINO's operations to achieve this objective.

As shown above, IFC's investments in MFIs was associated with raising relatively more savings than their peers. Despite this finding, which pertains to the general effect of IFC's investments in MFIs, it should be noted that 8 of the total 14 evaluated investments that had an explicit savings component got a positive development outcome ratings; 30 percent got a negative rating.

IFC Advisory Services advance the savings agenda largely by developing new products and technology upgrade. Contrary to IFC investments, its advisory services' used to focus on savings throughout the entire evaluation period FY07-13. Again, a significant share of projects (19 of 51) are focused in the Africa Region. Most advisory support is geared toward individual MFIs (80 percent) and provides support in developing new savings-related products (38 projects), followed by projects focusing on technology upgrades, staff trainings or capacity building, and risk management. Eleven projects supported transformations of MFIs into deposit-taking institutions, which were in turn supported through technical assistance aimed at product development, risk management, and capacity building. The upstream interventions and mixed intervention projects focused mostly on financial

literacy and financial infrastructure (of which, savings was also a part). Support to broader policy reform issues related to savings are rarely addressed by IFC Advisory Services. Less than 10 percent also provide upstream support.

Of the 26 evaluated IFC advisory projects, 13 received a positive success rating and 15 percent (4) a negative rating. An interesting project worth mentioning is a stand-alone savings project in Cambodia, where IFC assisted the Angkor Mikroheranhvatho Co, Limited, MFI in developing its savings product to at least 50,000 clients by offering the product to all the clients residing within a 5-km radius of an Angkor Mikroheranhvatho branch. The project was designed to be demand-led and tailored to the specific needs of the beneficiary banks/MFIs in Cambodia in an area of core IFC expertise. It contributed to the strategic objectives of the government of Cambodia to further develop and strengthen Cambodia's financial sector and was rated as positive by way of development outcome.

The World Bank provided assistance mainly through technical assistance and policy reform work that addressed savings-related issues. Most savings-related World Bank lending projects are in the form of technical assistance (28), aimed at building capacity of MFIs and central banks. The World Bank also supported 19 upstream interventions and 3 financing projects. Most of these projects are in the South Asia Region (21), followed by Africa (15).

World Bank lending related to savings has been largely successful, owing to the World Bank's good technical analysis. Of the 26 evaluated projects, 21 had a positive development outcome rating. The most common driver of success found among these projects (for 18) turned out to be an adequate technical analysis to ensure quality at entry; client or government commitment followed as the second best driver in 14 projects. It is worth mentioning here that of these 26 projects, 20 had at least a component of an upstream intervention, which also explains the government commitment playing a crucial role in the success of these projects. World Bank AAA projects supported the savings component as a part of a mix of advice for financial sectors and by targeting greater financial inclusion objectives.

#### **INSURANCE: PILOTING WHAT THE POOR NEED MOST**

Most people in developed countries take insurance for granted, yet microinsurance products are only now being piloted for the poor. Overall, about 10 percent (117 projects and AAA) of World Bank Group interventions in the financial inclusion space deal with microinsurance. Across all Bank Group instruments, there is a somewhat increased emphasis on insurance in recent years. Relatively more interventions address regulatory issues (12 percent); funding of microinsurance companies is rarer (6 percent). Of these 117 Bank Group financial inclusion projects

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with an insurance component, IFC investment has the largest share with 28 percent, and World Bank lending has a smaller share (23 percent). Regionally, these projects have often targeted Latin America and the Caribbean and South Asia.

IFC investments in the insurance space have been rather recent. Approximately 70 percent of investments were approved in the period 2010–13. About half of the portfolio was classified as focusing exclusively on insurance, both life and nonlife (15 projects). For example, IFC's investment in Protecta, Peru's first and largest specialized microinsurance company, focused on life insurance as well as annuities and accident insurance products. The remaining portfolio often mixed the provision of insurance with other products, in particular credit. Thirteen such projects were delivered through microfinance (both bank and nonbank) institutions. IFC's quasi-equity investment in the Institute for Financial Management and Research Rural, India, is one such example, as the company provides a comprehensive range of financial products; IFC's investment in Institute for Financial Management and Research aimed to promote this business model with potential to move beyond microcredit through both conventional credit delivery on the asset side and strong strategic partnerships to promote savings/investments/insurance on the liability side. "

Of the five evaluated projects, only one received a positive development outcome rating pointing at the challenges of such projects. Only two of the projects received a positive private sector development rating. Although Protecta eventually obtained a development outcome rating of moderately unsatisfactory given concerns about future profitability, sponsor commitment, and increased competition, the project received a positive private sector development rating as the company covered previously underserved segments and most of its branches were outside of Lima. In addition, by providing equity to the formation of this microinsurance company, IFC played a catalytic role in expanding the array of financial services available to a previously underserved segment of the population.

Also IFC advisory services' focus on insurance increased in recent years. More than 60 percent of IFC advisory projects supporting the insurance sector were approved after 2010. Forty percent of projects are in the South Asia Region; nine of these are in India. Two-thirds of advisory projects with an insurance component also included other services. Most projects were done through downstream technical assistance (70 percent).

For the World Bank, there was no particular increase in insurance-related lending over time; the Africa Region received the largest share of insurance projects; East Asia and Pacific saw the biggest share of projects that focused exclusively on

insurance. The periods FY07–09 and FY10–13 saw seven and nine projects approved, respectively. Half of these (eight projects) involved upstream interventions that included insurance as one of their multiple objectives. For example, in Peru, a series of Development Policy Loan prior actions aimed to strengthen the capacity of supervised financial institutions by enacting norms that ensured adequate management of overindebtedness, corporate governance arrangements, and underwriting standards so as to allow for an expansion in the services that financial institutions may provide and enable the development of new instruments targeted at the poor such as microinsurance.

In Tanzania, the Farm Income Diversification Programme Phase II provided more explicit support for the development of a supervisory methodology and policy framework for the insurance sector – including the drafting of regulatory guidelines and supporting accounting principles and standards – so that the industry would meet the appropriate legislative requirements. According to the project's Implementation Completion and Results Report Review, the country's FSAP emphasized the needs in insurance regulation and supervision, which were subsequently addressed by the Insurance Supervisory Department, hired with Farm Income Diversification Programme Phase II funds.

An interesting innovation is agriculture and weather or index-based insurance, intended to buffer income shocks due to droughts, floods, or natural disasters – but such interventions have been rare. Eight such World Bank lending projects were approved during the evaluation period FY07–13, of which three were in Africa. For example, in Ethiopia, the Financial Sector Capacity Building Project supported index-based weather insurance by providing technical assistance to insurance companies and potential clients, through feasibility studies to determine the scalability of index-based weather insurance and explore potential linkages to input financing, and by determining the capacity and infrastructure investments needed for the National Meteorological Service Authority to provide data for the expansion of index-based products.

IFC advisory projects also supported agriculture or weather or index-based insurance, half of the eight projects located in the Africa Region. For example, a project in Rwanda would focus on developing local capacity and a favorable environment for delivering flexible, affordable, and responsive weather insurance to low-income farmers to achieve long-term food security in the country. In Mozambique, a project developed and deployed two index-based weather insurance products against flood and drought events.

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Support to weather or index-based insurance schemes has been most prominent in AAA work. Twelve of the 27 insurance-related AAA activities dealt with such agriculture and weather or index-based insurance. These projects were evenly spread across all Regions. In some cases they were broad programs; in China, the Innovations for Agricultural Insurance AAA was developed in response to a request from the Ministry of Finance to conduct a comprehensive assessment of the agricultural insurance industry in China and provide recommendations for its development. In other cases, they can have sector-specific components, as in Jamaica, where the main output produced was a feasibility study for weather index insurance to protect the members of the Coffee Industry Board, and the facilitation of a prefeasibility study for developing and implementing a Caribbean Catastrophe Risk Insurance Facility parametric insurance solution for agricultural losses in Jamaica. Another example is the World Bank engagement with the Agriculture Insurance Company of India Limited (Box 4.8).

#### **Box 4.8. World Bank Technical Assistance for Agricultural Insurance in India**

Crop insurance for small farmers can provide income smoothing in case of drought, flood, or natural disaster. India had the world's largest crop insurance program, covering 25 million farmers. Yet issues in design, leading to long delays in claims settlements, as well as problems with pricing and product design, limited its growth, leaving 95 million farmer households not covered, despite significant government subsidy.

In 2006, the World Bank launched nonlending technical assistance to the Agriculture Insurance Company of India Limited, a state-owned agricultural insurance company, aimed to (i) reform National Agricultural Insurance Scheme so that it operates on a commercial, actuarially computed basis, albeit with government subsidizing premiums up front (as opposed to paying claims in arrears) and (ii) to extend crop insurance to the majority of India's farmers, especially to smallholders operating in rain dependent states.

Phase 1 of the project dealt with the development of a sound actuarial rating methodology (a "pricing model") for agricultural insurance. Phase 1 cost \$215,000 and was funded by the World Bank and the Swiss Trust Fund for Rural Finance Reform in India. Phase 2, funded by the Financial Sector Reform and Strengthening Initiative, provided a design for weather insurance contract design and ratemaking. With this World Bank technical assistance, the government piloted a modified National Agricultural Insurance Scheme, a market-based scheme with involvement from the private sector.

The new program had the potential to reduce claim settlement time, distortions induced by government subsidy, and basis risk while substantially expanding the number of households covered. The pricing model that the World Bank's technical assistance had proposed has become the industry standard, utilized not only by the state-run insurance company, but by new private players in the market who had rapidly growing market share. In addition, proposals for refining products and technology for assessing losses,

utilizing more refined crop-cutting samples and satellite-based meteorological data, were being developed, piloted, and tested by the government.

Source: IEG staff.

Lessons on weather or index-based insurance mainly point to the complexity of these schemes and the low uptake. Lessons learned include that not only (historic) weather data are required for weather index insurance that protects farmers but also vulnerability functions for the different crops. If these data are not appropriately available, much time-consuming work is required before a feasibility assessment of index insurance can be undertaken. In Jamaica, this is made more difficult by the prevailing short-term multicropping on very small farms, given the different vulnerabilities of different crops.

Alternative approaches are therefore required, such as the compilation of historic crop damage data in the best possible resolution; but this requires considerable effort in the absence of standards and a centralized data repository. In such circumstances, microlevel index insurance sold directly to farmers is not promising, and macro- and mesolevel implementations of index insurance are recommended. When key milestones depend on partners (like Caribbean Risk Managers) with resources committed to many other ventures, the progress of the project is subject to their availability and is more difficult to predict. Potential sources of funding for macrolevel weather index insurance premiums should be addressed at an early stage. Additional lessons on index-based weather insurance are summarized in box 4.9.

#### **Box 4.9. Weather Index Insurance**

Index-based weather insurance protects farmers against risks such as drought and flood by linking payouts to the weather requirement of the insured crop, and may encourage investment in more weather-sensitive but higher value crops. For example, instead of a payout in case of low yield, a weather index insurance policy would pay if there was too little (or too much) rain as measured at a local weather station or by satellite. Using an index as the basis for the insurance reduces information requirements and bureaucracy, can increase transparency (facilitating underwriting), and can reduce costs allowing greater affordability to farmers. The World Bank has assisted a number of countries in piloting weather index insurance.

Although this insurance has the potential to help small farmers mitigate the risk associated with extreme weather, early pilots of weather-based index insurance sponsored by the World Bank resulted in low take-up, due in part to high costs, low trust, and the difficulties of communicating the benefits of this product. Key design features that may assist small farmers in adopting weather insurance include measures to improve product understanding, increase trust in the product provider, and reduce farmers'



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liquidity constraints to paying premiums. However, the World Bank has yet to find a robust service delivery model.

Sources: IFC 2011; World Bank 2015 (<http://www.worldbank.org/en/news/feature/2015/04/15/making-index-insurance-work-for-the-poor>.)

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### What Do We Know about Beneficiary Effects?

Only about 2 percent of World Bank Group projects attempt to actually measure beneficiary effects; most track volume of finance provided, that is, an output. As pointed out in the preceding section, the design of M&E systems of World Bank projects has improved recently (FY07–13). Yet, the usage of indicators remains a challenge, according to IEG’s analysis of the latest cohort of evaluated projects. Of the 255 evaluated financial inclusion projects, approximately 75 percent contained financial inclusion indicators. Of these, most measure the extent of finance provided or level of financial intermediation (about 45 percent), that is, the number and volume of loans; a limited share of these (ten percent) also report on number and volume of deposits and other account holders.

About 20 percent of projects track outputs related to the provision of workshops, trainings, reports, and studies. For example, in the case of World Bank lending support through Ghana’s Rural Financial Services project, a training component measured training sessions held and people trained but not the outcome or impact of the training. Overall, the project was measured by number of rural microfinance clients (which substantially increased), number of accounts, and assets of rural financial institutions but not on the impact of the finance on rural clients’ income, well-being, or microenterprise performance. An equal share (20 percent) track the performance of institution or MFIs. About 7 percent track changed in the enabling environment or other goals related to policy reform work. Only 2 percent report on beneficiary effects such as improvements in welfare or increases in income. In assessing beneficiary effects, the availability of baseline data is often a challenge (box 4.10).

Those few projects that focus on tracking beneficiary effects indicators focused mostly on tracking the number of jobs created by MSMEs and the productivity and profitability of MSMEs, as well as income and welfare improvements to beneficiaries overall. Within the beneficiary category, most are with World Bank lending projects; only one is an IFC investment. IFC does gather data on job creation systematically in the Development Outcome Tracking System at the client level; however, these data refer to jobs created by the actual MFI (that is, IFC’s direct client), not by microenterprises supported through credit. One of the few examples from IFC’s

portfolio that successfully captured jobs creation is the IFC project in which IFC provided a loan to the Romanian-American Enterprise Fund to on-lend to Romanian microenterprises. According to evaluation documents, the project was to provide credit to small borrowers so that they could create jobs for themselves and others. As was expected, the project did create jobs for the borrowers. At appraisal, the project had intended to create over 5,000 jobs (about 2,000 for women), and the number of active borrowers data appears to indicate that this was achieved. At appraisal, the project had also expected to sustain another 15,750 jobs (6,800 for women), but no data on the multiplier effect is available from project files. In general, labor market conditions were improved by growth in the economy that resulted in high demand for construction workers, and large-scale emigration to Italy and Spain. By 2006–07, labor market conditions had tightened and unemployment was 4–5 percent, down from 7–8 percent in 2003–04.

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**Box 4.10. Setting Baselines for Beneficiary Assessments**

Note that in both cases there were issues with setting a baseline; this can be an issue in trying to assess beneficiary effects. In the examples here, surveys had to be commissioned to understand beneficiary effects.

In Bangladesh, the World Bank Learning and Innovation Loan, Financial Services for the Poorest, aimed to reduce the number of the poorest through use of microcredit and other financial services to enhance incomes and livelihood. Indicators used to track achievement of this objective included income of at least 50 percent of those that are earning less than 50 cents a day raised to more than 50 cents a day and incomes of at least 50 percent of those earning less than a dollar/day raised to more than a dollar/day. At project closing, these indicators stood at 93.5 and 83.4 percent, respectively. However, differences in baseline household income figures in the 2005 and the 2007 impact evaluations suggest a lack of established baseline earning figures. Lessons from the Implementation Completion and Results Report (ICR) Review include the fact that a baseline survey is essential for assessing targeting success. In this type of projects, there is a possibility of selection bias because of the strong incentive of the implementing agency (in this case, the POs) to include beneficiaries who are more likely to succeed. So, the beneficiary selection process needs to be strictly monitored.

In Mongolia, the World Bank lending Sustainable Livelihoods project was designed to help establish a Microfinance Development Fund, strengthen revolving funds, and develop an index-based livestock insurance scheme. According to the ICR, although indicators were not designed at baseline, a 2006 survey on changes in the livelihoods of sub-borrowers of the Fund measured the monetary income changes among sub-borrowers. These measurements were clustered under the indicator: microfinance services available and used by poor households to build assets and to smooth consumption on a financially- and institutionally-sustainable basis. According to the ICR Review, the ICR lacks information on reduced poverty incidence but notes that 271 out of 313 formal herder groups took out loans for income-generating and risk-mitigating activities and also that 90 percent of borrowers reported an income increase.

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Sources: Implementation Completion Report Reviews.

One World Bank project that collected considerable information on beneficiaries was the Andhra Pradesh Rural Poverty Reduction Program, where, according to IEG's recent Project Performance Assessment Report, good M&E, including a baseline survey and impact evaluation, were conducted and confirmed household level benefits of the project's financing. The impact evaluation further confirmed strong benefits for the poorest beneficiaries. Impact evaluations may not answer all questions about a project, including their systemic efficiency and sustainability, but they do illuminate direct beneficiary effects.

IFC does publish occasional success stories or lessons learned reports; systematic assessments of beneficiary effects are rare to date. IFC typically presents experience in a format of a narrative or in the form of lessons learned, for example, the recently presented report on *Small Beginning for Great Opportunities*. This report presents a wide range of lessons to be learned from IFC's experience in microfinance. However, few of these publications or data sources provide systematic evidence on actual beneficiary effects. An exemption here is the recently published in-depth study on the success of agriculture loans in rural areas in Tanzania (Tower, Noggle, and Stuart 2014).

The assessment of beneficiaries in the context of this evaluation is therefore limited to structured interviews and focus groups conducted in the course of the missions that the evaluation team undertook when preparing this report. An example of such an assessment is presented in box 4.11. Collectively, these assessments confirm the results of the broader literature, that is, that the expectations of microcredit pulling millions out of poverty have not been fulfilled. Credit helped the poor manage their day-to-day struggles and provides choices and options. Microenterprises visited during missions barely grew, yet MFI clients found the funds obtained through credit useful in paying school fees or paying for emergencies.

#### Box 4.11. Beneficiary Assessment: Example from Mexico

The beneficiary consultations with five groups of clients of MFIs and local saving and credit associations, so-called *Sociedades Cooperativas de Ahorro y Préstamo*, found an overall positive, although not transformative, impact of the interventions. Although gaining access to formal sources of financial services was not transformational in so far as lifting them from poverty, it did help them improve their quality of life. Some of the groups the mission met with in situ inhabited quite hard-to-reach locations with poor road access. MFI and social capital markets representatives had to visit client groups in their locations

because transport cost was otherwise a significant barrier to these clients, particularly when measured relative to average transaction ticket.

Lending was typically structured as group lending, though individual contracts are signed with each member of the group. Uses of the funds varied ranging from working capital to fund microbusiness inventory (for example, resale of cloths in small village) to animal feed to raise goats and chicken for sale in local markets. The microbusiness and family finances comingle, and it was not unusual for borrowers to allocate part of the proceeds from the loans to meet family expenses (for example, school fees for their children).

Typically, the borrowers are women who undertake microbusiness operations to complement the income of their husbands, who have unsteady work and income. Some of the borrowers showed a sophisticated financial capability acumen “solving” demanding cash flow management problem over the duration of the borrow-repayment cycle.

Borrowers identified a range of benefits including the generation of small profits that were being used to fund improvements to their precarious houses and a better ability to cope with unexpected expenses and demands (for example, a sudden illness of child) made possible by the group lending. The weekly group payment was still “collected” by MFI agents, with individual borrower shortfall covered from the prefunded pooled rainy-day fund that the group sets up to cover emergencies, and borrowers had the capacity to afford better schooling opportunities for their children.

Some of the groups reported intense competition from other sources of funding but attached valued to ongoing lending relationships with the MFI agent representative. Most of the group have several borrowing cycles with the MFI. MFI funding was provide at the equivalent of 80 percent annual rate, much higher than that of the associations (though borrowing from this source has hidden opportunity costs associated with the requirement predeposit for the duration of the loan as a qualifying condition for borrowing). The agents provide a modicum of financial education to these clients.

*Source: IEG country case study Mexico.*

Realizing the need to track progress toward the Universal Financial Access goal, the World Bank Group has started efforts to develop an M&E framework. Through such an M&E system, the Finance and Markets Global Practice intends to understand whether reforms succeed and whether they stimulate investment, behavior change, and economic growth and improve overall quality of life. A standardized M&E framework for the Financial Inclusion Support Framework global program and Financial Inclusion Support Framework country programs has been drafted. It focuses on direct outputs, outcomes, and impacts of financial inclusion interventions; welfare indicators are not foreseen in current drafts. The global practice also started working on developing a framework to measure the results of World Bank on advisory services and analytics.

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As the World Bank Group is ramping up its support to client countries in their pursuit of the 2020 Universal Financial Access Goal, M&E has become more important than ever. The broader academic literature, as well as this evaluation, confirm that the expectations that microcredit would pull millions out of poverty has not been fulfilled; yet credit, and with it other financial services, have helped the poor manage their day-to-day lives and provide choices and risk mitigation mechanisms. In view of these rather modest effects to date and the nature of the policy options that the World Bank Group is likely to consider going forward, a sequenced approach would provide a sound alternative.

Such a sequenced approach would focus on clearly delineated and evaluable interventions; it would build on deriving lessons from past and ongoing interventions and feeding these lessons into the design of future projects. With only 2 percent of Bank Group operations reporting on beneficiaries' outcomes, such a feedback loop clearly does not exist.

Having a well-established M&E system in place has become even more crucial, as the World Bank Group experiments with ways that could help achieve the envisaged Universal Financial Access goal, such as massive rollouts of no-frill accounts or digitalizing government-to-people payments. Such a "push" approach for financial inclusion is likely not only costly but will also require subsidies. World Bank Group will need to keep an eye on outcomes to ensure that financial services are rolled out to the people who can productively make use of them—and that these services make their lives better. This is even more relevant in view of the high dormancy rates of recently opened no-frill accounts in India, for example, where 72 percent of accounts show zero balance (Demirguc-Kunt and others 2015).

## **Conclusion**

The World Bank Group supports MFIs in the delivery of their services through funding, either through lines of credit, direct investments, or advisory services, that is, downstream technical assistance. Of the World Bank's entire lending portfolio, only 2 percent in volume and 6 percent in terms of numbers of projects focus on financial inclusion. For IFC, the share of investments in MFIs represents a larger share of its portfolio: 10 percent in numbers and 4 percent in volume (dollar value).

Overall, World Bank downstream lending activities focus heavily on the most excluded countries. Its work focuses on credit, even though a significant share of its downstream technical assistance focused on payments, savings, and insurance—a

promising trend given that noncredit service are reported to have equal, if not higher, benefits for the poor than credit only.

With regard to the sustainability of World Bank financial inclusion interventions, some level of subsidization is likely to remain going forward. Even though technological progress may eventually allow MFIs to reach the lower end of the retail market, in the near term, efforts to reach rural areas and to achieve mass rollouts of no-frills accounts are likely to involve some subsidy. Self-help groups have routinely involved subsidy, while the costs of no-frill accounts are often absorbed by state-owned banks. Reaching the “last billion” of unbanked that will persist beyond 2020 is likely to pose as yet unknown challenges to systems and associated costs; those who remain unbanked at that time are likely spread out over many countries and will predominantly be located in the rural space. To date, the World Bank has not harmonized its approach to subsidization nor adopted a uniform philosophy across networks (now global practices) and activities.

A challenge in World Bank lending projects has been excessive complexity, often manifested in too many components and subcomponents. During the last few years, the global practice has internalized this lesson, however, and design complexity improved. For M&E, the trend is less pronounced. Even though the design of M&E systems improved, usage of indicators remain a challenge.

Within the World Bank Group, IFC has the largest volume of downstream investments in financial inclusion. On average, these investments are small, but they occur in markets where they matter, that is, they reach countries that have high exclusion rates. IFC typically supports fully licensed banks but also supports nonbank MFIs. The investments by IFC in MFIs struggle with achieving adequate business performance but exhibit remarkable private sector development effects and good economic sustainability. The root causes for the low profitability of IFC’s MFI investments were higher start-up costs and slower loan growth. Microloans are a relatively small services line of IFC-supported banks, accounting for only 5–10 percent of their mixed loan portfolio, with the rest supporting clients taking out larger loans, including SMEs. This is not necessarily a bad thing as at least SMEs are likely to benefit from such loans – and eventually microenterprises may benefit from the strengthening and deepening of the smaller end of the commercial finance market.

IFC work quality was found to be high – and is hence not to blame for the low business success. This raises the question of whether IFC’s approach of relying on self-sustaining MFIs as their main business model has found its limits – beyond which catering for the very low retail end of the market would only be feasible with

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subsidies. For example, IFC-supported MFIs are found hesitant to enter the rural space for a range of issues. Therefore, going forward, IFC would have to find innovative business models, products, and technologies that would enable reaching the poor, including through innovations that would allow lowering transaction costs. This is likely only possible through a trial-and-error approach or a research agenda that pilots such innovative business models as IFC tries to scale up its MFI business. Important for such an approach would be that IFC reports on the share of the microloans reaching the poor by using loans sizes, cognizant of the country-specific income situations and granularity of the economies.

IFC-supported MFIs managed to increase resource mobilization by growing the number of savers among their clients – more so than their peers. This is a potentially promising development given that savings has been found to have more positive effects for the poor than credit.

IFC advisory projects build capacity with local MFIs, help client MFIs develop products and services, and improve risk management processes. Measured by their development outcome rating, about two-thirds (64 percent) of these projects are successful, corresponding to about the remaining access to financial advisory portfolio. IFC advisory projects rate high on output achievement (83 percent rated successful) and on strategic relevance (75 percent rated successful). Performance drops when it comes to outcome achievement, for which only 62 percent of projects are successful – 10 percent lower than the average access to finance advisory service. Yet IFC advisory projects stand out for their high-impact achievement – at least in relative terms – and for their high level of efficiency.

Looking at the changes in financial inclusion during 2014 (based on the Findex data, financial inclusion went up for the bottom 40 percent in countries where the World Bank Group had more projects); however, there is no statistically significant relationship between financial inclusion going up and more financial inclusion projects. Further, IEG's analysis showed that there are payoffs in focusing on credit information and on deepening the financial sector, as it seems to enhance the World Bank Group's overall development effectiveness. There are payoffs in focusing on poorer countries as they showed an increased rise in financial inclusion rates (probably also because they had more to catch up). Fragile and conflict-affected situation countries remain more challenging.

The small number of countries with financial inclusion strategies in place during the portfolio period suggests a lot of potential for gaps, lack of complementarity and sequencing, and ad hoc-ism. The qualitative beneficiary assessment conducted in the context of this evaluation confirm the findings from the literature review, presented

in chapter 2. A quantitative and systematic assessment of the benefits to the poor of World Bank Group's entire portfolio is not possible. The Bank Group does not have in place the needed mechanisms and reporting tools to systematically collect data on the welfare effects of financial inclusion on the poor.

As the World Bank Group ramps up its support to client countries in their pursuit for the 2020 Universal Financial Access goal, M&E has become more important than ever. In view of the rather modest effects of financial inclusion determined to date and the nature of the policy options that the World Bank Group is likely to consider going forward, a sequenced approach would provide a sound alternative. Such a sequenced approach would focus on clearly delineated and evaluable interventions and ensure a constant feedback loop into project design. Current efforts to develop an M&E framework are important steps which would have to be complemented by research efforts on the welfare effects on the poor. Once implemented, these would enable understanding whether and under which circumstances access to, for example, digital or mobile payment systems lead to inclusion and how such inclusion improved the lives of the poor.

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<sup>1</sup> As opposed to IFC advisory work that addresses upstream or policy issues (see chapter 3).

<sup>2</sup> This paragraph reports the findings of IEG's statistical and econometric analysis of the relationship of the project portfolio and country characteristics to changes in financial inclusion of the bottom 40 percent as measured by Findex 2011 and 2014, and with respect to project development outcomes evaluated by IEG.

<sup>3</sup> This description is derived from the FPD website in 2013.

<sup>4</sup> See M. L. Melly Maitreyi, "New A.P. faces Rs.15,000-cr. Deficit," *The Hindu*, June 2, 2014.

<sup>5</sup> The Business Standard. "Banks Spent Rs 2,000 Crore for Opening Accounts under Jan Dhan Yojana: IBA chairman Says Opening an Account Costs Rs 140 against Estimates of Rs 80," *The Business Standard*, February 3, 2015.

<sup>6</sup> Prianka Singhal, "Making Jan Dhan Yojana Work," *The Financial Express*, December 19, 2014.

<sup>7</sup> Country features are unlikely to drive development outcome ratings. As we have seen in chapter 2, both IFC investment and – to an even greater extent – World Bank lending support countries with very low inclusion rates. Chapter 2 assessed to what extent the World Bank Group is focusing its support on countries that are in greatest need, that is, countries with low financial inclusion rates. According to the analysis presented there, World Bank Group, including IFC, is strongly gearing their support toward countries with very low inclusion rates and where markets reach the poor, as evidenced by a low average loan size. World Bank lending is even more concentrated in these countries, which likely pose specific challenges to IFC investment and World Bank lending. However, the level of inclusiveness does not lend itself to explain the differences in development outcomes: because World Bank lending is even more concentrated in lowest inclusion countries but at the same time exhibits higher development outcome ratings, it is unlikely that these country features drive development outcome ratings.



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<sup>8</sup> For example, IFC also invests into global or regional holding companies. These lend on to their local subsidiaries without issuing loans themselves and hence without reporting to MIX. Note that the local subsidiaries are captured in the MIX market data.

<sup>9</sup> Once these clients were identified, the average loan size for IFC Clients versus the rest of MIX Market clients was computed over a seven year period (2006–2012). To obtain a complete and balanced dataset, any clients that had missing values for the variable of interest were excluded and then any clients that did not have data for period of interest were also excluded. Given these specifications, the number of clients observed was reduced to just over 450 from over 2,200 clients that had reported average loan size at least once within the period 2006–12. Also on the IFC side, the number of MFIs reporting such a balanced data set over 2006–12 was limited and shrank the number of observations to between 20 and 30. The analysis is hence not statistically representative.

<sup>10</sup> That reported data consistently during FY06–12.

<sup>11</sup> Using a mobile device such as a mobile phone, a tablet, or a point-of-sale (POS) terminal

<sup>12</sup> China is not included in this list because since Groupe Spécial Mobile Association currently researching this market to understand the nature of the services offered and the underpinning regulation. More information on China will be presented in the 2014 Mobile Financial Services State of the Industry Report.

<sup>13</sup> Forty-two markets with existing regulatory barriers include Argentina, Armenia, Bangladesh, Botswana, Cambodia, Cameroon, Chad, Chile, Congo-Brazzaville, the Dominican Republic, the Arab Republic of Egypt, El Salvador, Gabon, Georgia, Ghana, Guatemala, Guinea, Haiti, Honduras, India, Indonesia, the Islamic Republic of Iran, Jordan, Mauritania, Mauritius, Mexico, Mozambique, Myanmar, Nepal, Nigeria, Pakistan, Panama, Qatar, Serbia, Solomon Islands, South Africa, Sudan, the Syria Arab Republic, Tunisia, the United Arab Emirates, and República Bolivariana de Venezuela.

<sup>14</sup> Members are Committee on Payments and Market Infrastructures central banks, non-Committee on Payments and Market Infrastructures central banks active in the area of financial inclusion, the International Monetary Fund, and international development banks.

<sup>15</sup> The Partnership for Financial Inclusion states its objectives as follows: (i) bringing financial services to 5.3 million people in Sub-Saharan Africa; (ii) developing sustainable microfinance business models to deliver large-scale, low-cost banking services; (iii) helping to accelerate the development of mobile financial services; and (iv) sharing lessons learned in Sub-Saharan Africa with the rest of the world.

<sup>16</sup> As per Groupe Spécial Mobile Association posting on January 15, 2015, of the 89 markets where mobile money is live, only 47 have an enabling regulatory approach, while in the other 42 markets regulatory barriers still exist.

<sup>17</sup> As per the survey and qualitative research conducted by InterMedia for The Financial Inclusion Insights program, 94 percent of the respondents out of 428 mobile money users in Pakistan have not registered their own accounts, and preferred to conduct over-the-counter transactions through an agent's account (September 2014).

<sup>18</sup> Mexico—Strengthening the Business Environment for Enhanced Economic Growth Development Policy Loan (P112264).

<sup>19</sup> As per 2014 Market Monitoring Unit Stats of the Industry Report, at least 11 providers reported generating more than \$1 million in revenue during the month of June 2014, compared with 8 providers in 2013. This is still a small percentage, since 255 mobile money services are available in developing countries.

<sup>20</sup> Mid-Term Evaluation of the MasterCard Foundation and International Finance Corporation Partnership for Financial Inclusion for Sub-Saharan Africa, Oxford Policy Management, and PHB Development, April 2015.

## 5. Conclusion and Recommendations

### Conclusions

3. This evaluation reviewed the experience of the World Bank Group in supporting financial inclusion over a six-year period. A key purposes of this evaluation is to inform the World Bank Group about their experience in supporting financial inclusion at a time when it is designing a road map for its future work program that should help client countries achieve the Universal Financial Access goal by 2020. The access goal has become of highest strategic relevance to the World Bank Group as its President, Jim Yong Kim, committed his organization to this goal in 2013. The evaluation also informs the strategic discussion in and outside of the World Bank Group regarding the role of financial inclusion in the post-2015 development agenda and the ways the World Bank Group can support it.

4. The poor face enormous financial challenges and require access to financial services to meet essential needs. Providing the poor with access to financial services, such as affordable transaction accounts, reliable payment systems for national or international remittances, and safe opportunities to deposit their funds, has the potential to benefit the poor. Recognizing the benefits for the poor, a microfinance industry grew over the last 20 years; its growth was even dramatic in the last three to five years when looking at assets of the microfinance institutions (MFIs).

5. World Bank Group spent about 2–3 percent of its annual commitments on financial inclusion-related projects, based on the rationale that its support for financial inclusion would improve how markets work by overcoming limitations to market demand and supply so more and better financial services could be provided to the poor. With a growing realization that poor households and small firms need broader financial services than just credit, the World Bank Group's inclusive finance support gradually embraced other services, such as payments and savings, which are known to have higher potential to improve the lives of the poor. Along with this development, an increase emphasis on upstream work to create the enabling environment in client countries.

### STRATEGIC RELEVANCE

Despite its global efforts to promote financial inclusion, the World Bank Group's contribution is rather small given the access gap—requiring the World Bank Group to be strategic about what it supports. Over six years (FY07–13), World Bank Group support to financial inclusion grew by about 20 percent; however, it was outpaced by the growth of the MFI industry, which grew by 80 percent during the same

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period. Still, the fact that the International Finance Corporation (IFC) supported (either through investments or advisory services) MFIs that jointly make up 39 percent of the global microloan volume exemplifies the World Bank Group's leadership role.

But despite the World Bank Group's growth and relative reach, its support to financial inclusion is relatively small given the large number of unbanked (2.5 billion globally) and the microcredit gap (\$1.3 trillion). These contrasting figures call for a highly strategic allocation of the World Bank Group's scarce resources, devoting them where they are needed the most and where they can be expected to have the highest impact either in terms of creating new markets or in scaling up existing markets.

The Independent Evaluation Group (IEG) found that, globally, the World Bank Group's allocation of its resources for advancing financial inclusion are strategically well aligned with countries' needs, that is, they reach primarily countries with low inclusion rates and where markets actually reach the poor. In particular, World Bank lending, IFC advisory, and analytic and advisory activities (AAA) are strongly geared toward the lowest-inclusion countries. But IFC's investments are also well in sync with client countries' needs. Given the self-sustaining nature of IFC investments, the presence in lowest- and low-inclusion countries is remarkable, as these are typically service MFIs that rely on subsidies.

Overindebtedness of microfinance clients is perceived as a risk facing the industry. But, this evaluation found that, broadly speaking, World Bank Group strategic resources allocation to client countries reflects market saturation levels, proving markets at risk of overindebtedness rather with AAA work than with funding.

At the country level, the World Bank Group support for financial inclusion was relevant in as much as it addressed a clear development priorities; however, consumer protection and financial literacy have thus far rarely been addressed. The most frequently addressed constraints are lack of capacity and financing of financial institutions along with financial infrastructure (credit reporting) and regulations. Other important constraint, such as consumer protection and financial literacy have, however, been almost never addressed during the evaluation period, even though the World Bank Group supports the Global Survey on Consumer Protection and Financial Literacy. Increased efforts in this space that the World Bank Group undertook in FY15 point at an encouraging shift of focus

Although most projects identify beneficiaries, the World Bank Group lacks appropriate definitions for what it calls "microenterprises" and often takes a

shortcut when specifying the constraints of their beneficiary groups. Across the portfolio, most projects identified target beneficiaries, such as microenterprises, albeit most lacked a definition. This is important because projects may end up supporting larger companies under the heading of microfinance. Of those projects that mention women beneficiaries, a minority of projects provide an in-depth description of this target population. However, financial inclusion projects fail to spell out the constraints specific to these beneficiaries.

The Bank Group's public commitment to a specific measurable goal contributed to sustaining an international dialogue to reach consensus and advance the financial inclusion agenda. However, despite its public commitment to the Universal Financial Access Goal 2020, there appears to be little guidance on how to operationalize this goal. The Bank Group's current approach delineates principles of actions and key building blocks, but it remains to be seen how this goal will be translated into practice. Conceptually, it is difficult to refute the argument that some sort of access to financial services is needed to enable inclusion; but whether access results in inclusion eventually depends on the quality, design, and utility of this initial access.

For example, the promotion of access through government-supported programs to digitalize cash payments via mobile phones or to roll out no-frill accounts for a large share of the population, may not necessarily lead to inclusion – and the current evidence base proving this is thin. A focus of the international development community – including the World Bank Group – to drive up headline numbers of financial access hence bears the risk of investing in the “plumbing” with no water flowing through later on. Moreover, the current World Bank Group's strategy of focusing on 25 priority countries may have to be adjusted going forward, as the excluded will increasingly be broadly distributed among many countries.

#### **WORLD BANK GROUP SUPPORT FOR POLICY REFORM**

6. The Bank Group substantially contributes to global knowledge, standards, and policy norms to expand financial inclusion. A key means by which the World Bank Group advances reform efforts is through international partnerships. The Bank Group has been able to leverage its impact at the country level through global partnerships. Partnerships clearly extend the reach, resources, and influence mobilized to promote access to financial services by the poor and microenterprises. Organizations like the G20, the Global Partnership for Financial Inclusion, the Consultative Group to Assist the Poor (CGAP), the Alliance for Financial Inclusion, and the Center for Financial Inclusion have a strong standing with relevant stakeholders and can provide opportunities for knowledge sharing, policy influence and piloting, and disseminating innovative approaches.

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7. For example, the World Bank's exercised intellectual leadership in the area of global remittances through the Global Working Group on Remittances, whose work was credited with reducing the cost of remittances, resulting in tens of billions of dollars of savings to migrant workers and their families. Sector leaders in the World Bank and IFC make clear that partnerships play a large role in the World Bank Group's goal of universal financial access and longer-term inclusion goals as well. At the 2015 Spring Meetings, President Kim stated that to promote financial access, the World Bank Group's role is to convene and energize a coalition of partners – and also to step up its work.

8. At the same time, these partnerships bear costs and risks: they require resources and senior staff of the World Bank Group, can inhibit or dilute its own “branding,” and may at times pursue goals or methods not squarely aligned the World Bank Group's own strategy. Partnerships involve compromise and coordination. In absence of results frameworks or rigorous quality control, there can be reputational risks. Recognizing the necessity of such partnerships to achieve its objectives, the World Bank Group should nonetheless encourage its partner organizations to adopt high standards, especially with regard to their accountability and learning systems of the partner organizations. CGAP has only recently developed a clear results framework, and IEG did not come across results frameworks, independent reviews, or evaluations of other partnership bodies, beyond a progress report. Given the different types of partnerships, advocating for such systems is likely to gain more traction in partnerships where the World Bank Group is a major stakeholder, hosts the secretariat, or contributes resources.

9. With regard to the World Bank Group's country-level engagement on policy reform, IEG concludes that the World Bank Group plays a significant role, but that its approach to identify and tackle constraints to financial inclusion is neither sufficiently systematic nor comprehensive. The World Bank Group played an important role in identifying major legal and oversight gaps and most project were also executed with good work quality. AAA work delivery an important and often successful contribution to the policy reform process, based on World Bank's own self-rating scheme. IEG also concludes that the identification of legal and oversight gaps was not part of holistic assessment of the adequacy of the various elements of the financial inclusion framework; however, it also found that the World Bank Group did play a significant role in this space, in particular with regard to payments. In select countries, payment systems, remittances, and financial infrastructure were covered through assessments at the country level. The World Bank is also in the process of ramping up its support through advisory services and analytical support in the areas of consumer protection and financial literacy. This

global program of 27 projects with completion dates FY15–18 will be important as the World Bank Group is advancing its diagnostic work.

10. Despite these efforts, the lack of a systematic diagnostic continues to be a concern in areas where prudential regulations would not be applied, for example, stability and consumer protection issues related to mobile network operator–led mobile banking systems or savings and credit cooperatives, which are of particular importance for the rural poor. In summary, the World Bank Group does not yet have a mechanism within its financial inclusion tool kit to provide a comprehensive and systematic assessment of the various aspects of financial inclusion, although it is developing potentially important instruments such as the Financial Inclusions Support Framework and a new template for the financial inclusion module of Financial Sector Assessment Programs.

11. IFC advisory interventions that foster the establishment of elements of an enabling environment for financial inclusion are very relevant and important, despite IFC's more limited role compared with the World Bank. In view of the recent restructuring, it is assumed that these interventions be executed by the World Bank Global Practices and no longer by IFC Advisory Services. IFC Senior Management envisages IFC Advisory Services mandates be linked to investment opportunities, which for upstream interventions is difficult to argue. Going forward, it appears hence warranted that such mandates not be dropped but rather adequate funding mechanisms be found. At the same time, the integration of IFC's Access to Finance Advisory Services into the Finance and Markets Global Practice and IFC Financial Inclusion Group also has the potential to strengthen synergies and overall effectiveness.

#### **DID FINANCIAL INCLUSION INTERVENTIONS DELIVER SERVICES TO THE POOR?**

The World Bank Group supports MFIs in the delivery of their services through funding, either through lines of credit, direct investments, or advisory services, that is, downstream technical assistance. Of World Bank's entire lending portfolio, only 2 percent in volume and 6 percent in terms of numbers of projects focused on financial inclusion. For IFC, the share of investments in MFIs represent a larger share of its portfolio – 10 percent in numbers and 4 percent in volume (in dollar terms).

Overall, the World Bank lending activity heavily focuses on the most excluded countries. Its work focuses on credit, even though a significant share of its downstream technical assistance focused on payments, savings, and insurance – a promising trend given that noncredit service are reported to have equal, if not higher, benefits for the poor. A recurring challenge in World Bank lending projects is excessive complexity, often manifested in too many components and

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subcomponents. With regard to the sustainability of World Bank financial inclusion interventions, even though technological progress may eventually allow MFIs to reach the lower end of the retail market, some level of subsidization is likely to remain going forward, in particular in the areas of rural financial services and mass rollouts of no-frill accounts. The latter may generate savings to governments where they are used as vehicles for public payments schemes but will nonetheless require up-front subsidy. To date, the World Bank has not reconciled its approach to subsidization nor adopted a uniform philosophy across networks (now the global practices) and activities.

IFC's investments in financial inclusion are small on average, but they occur in markets where they matter; that is, they reach countries that have high exclusion rates. IFC typically supports fully licensed banks, but also nonbank MFIs. The investments by IFC in MFIs struggle with achieving adequate business performance, but exhibit remarkable private sector development effects and good economic sustainability. The root causes for the low profitability of IFC's MFI investments were higher start-up costs and slower loan growth. Microloans are a relatively small services line of IFC-supported banks, accounting for only 5–10 percent of their mixed loan portfolio, with the rest supporting client taking out larger loans, including SMEs. This is not necessarily a bad thing as, at least, SMEs are likely to benefit from such loans – and eventually microenterprises may benefit from the strengthening and deepening of the smaller end of the commercial finance market.

IFC work quality was found to be high and is hence not to blame for the low business success. This raises the question of whether IFC's approach of relying on self-sustaining MFIs as their main business model has found its limits – beyond which catering to the very low retail end of the market would only be feasible with subsidies. Important for the poor, IFC-supported MFIs (that reported data systemically on savers and borrowers) managed to increase resource mobilization by growing the number of savers among their clients – more so than their peers. This is a potentially promising development given that savings was found to have more positive effects for the poor than credit. Given that many IFC-supported MFIs are reluctant to expand into the rural space, in particular in Africa, innovative business models, products and technologies are needed to expand into the rural space, as IFC scales up its MFIs business and tries to lower transaction costs.

It will be important for such an approach that IFC reports on the share of the microloans reaching the poor by using loan sizes, cognizant of the country-specific income situations and granularity of the economies. The current practice of labeling investments as “in support of microenterprises” causes confusion and may raise

undue expectations about IFC's reach and the number of microenterprises it is helping.

IFC's experience in supporting MFIs suggests the value in supporting *new* clients and investing in small and relative pioneering projects that take longer to turn profitable but have a tremendous development impact. IFC's greenfields are good example of partnering with new clients that resulted in projects with large private sector development impact. At the same time, these greenfields illustrate that supporting projects that do not necessarily provide quick profitability may still be worthwhile – noting the deviation between business success and development impact. They also underscore the necessity for IFC to support relatively small projects, some of which can be quite transformational in that they establish industry leaders in the provision of financial services.

IFC advisory projects build capacity with local MFIs, help client MFIs develop products and services, and improve risk management processes. Measured by their development outcome rating, about two-thirds (64 percent) of these projects are successful, corresponding roughly to the remaining access to financial advisory portfolio. IFC advisory projects rate high on output achievement (83 percent rated successful) and on strategic relevance (75 percent rated successful). Performance drops when it comes to outcomes achievement, for which only 62 percent of projects are successful – 10 percent lower than the average access to finance advisory service. Yet IFC advisory projects stand out for their high-impact achievement – at least in relative terms – and for their high level of efficiency.

With regard to working as “one World Bank Group,” this evaluation found that the small number of countries with financial inclusion strategies in place during the portfolio period suggests a lot of potential for gaps, lack of complementarity and sequencing, and ad hoc-ism. Country case studies, while documenting some instances of collaborative synergies, further indicate the existence of such gaps, as well as simple ignorance on the part of each institution (or even practice) about what the others are doing.

The qualitative beneficiary assessment conducted in the context of this evaluation confirmed the findings from the broader literature, that is, that the expectations of microcredit pulling millions out of poverty have not been fulfilled; yet credit can help the poor manage their day-to-day struggle and provides choices and options that did not exist before. Even though microenterprises visited during missions barely grew, these MFI clients still found the funds obtained through credit useful in paying school fees or paying for emergencies. Findings, as well as IEG's literature review, point at the higher potential of noncredit financial services, that is,



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payments, savings, and insurance. A more systematic and quantitative assessment of the benefits to the poor is not possible, as the World Bank Group does not have in place a mechanism to systematically collect data on the welfare effects of financial inclusion on the poor. The Bank Group is in the process of developing monitoring and evaluation (M&E) concepts to track direct outcomes and impacts of its financial inclusion interventions, in particular under the Financial Inclusion Support Framework. These steps are important and need to be complemented by research efforts that study the actual welfare effects by the poor.

#### **IMPLICATIONS FOR THE WORLD BANK GROUP'S FINANCIAL INCLUSION STRATEGY**

The Universal Financial Access Goal 2020 is central to the World Bank Group's strategy in financial inclusion—focusing attention on providing financial access through transaction accounts. Given the potential of noncredit financial services, payment systems may indeed be a good entry point for the poor to get connected to the formal financial system. The Bank Group's public commitment to a specific, measurable goal contributed to sustaining and expanding an international dialogue to reach consensus and advance the financial inclusion agenda. However, despite its public commitment to the Universal Financial Access Goal 2020, there appears to be only limited guidance on how to operationalize this goal. The Bank Group's current approach delineates principles of actions and key building blocks, but it remains to be seen how this goal will be translated into practice.

Conceptually, the link between access and inclusion (active use) of financial services is clear, but empirically, nonutilization rates in some schemes raise questions. A lot depends on the quality, design, and utility of this initial access. For example, the promotion of access through government-supported programs to digitalize cash payments via mobile phones or to roll out no-frill accounts for a large share of the population may not necessarily lead to inclusion. High dormancy rates and low usage of newly opened accounts offer additional caution, in particular in countries that implemented mass rollout programs, but also in low-income and lower-middle-income countries in general. Instead of focusing on “head-count numbers,” the relevant goal may instead be providing services to everyone with a productive and beneficial use of them.

Given the uncertainties of whether the poor benefit and under which circumstances they benefit the most, and whether access to financial services leads to inclusion, adopting a sequenced approach to program implementation provides a sound way forward. The current state of knowledge indicates that financial inclusion does not transform the lives of the poor, at least for credit, and effects of other financial services appears modest overall as well. The proposed sequenced approach could focus on clearly delineated and evaluable interventions and incorporate lessons

from past and ongoing interventions into the design of new interventions. Having a well-established M&E system in place is of particular importance as the World Bank Group experiments with new ways to achieve the envisaged Universal Financial Access goal, such as rollouts of no-frill accounts or digitalizing government-to-people payments. The World Bank Group will need to closely monitor outcomes to ensure that financial services are rolled out to the people who can make good use of them – and that these services make their lives better. In this context, the increased efforts of the World Bank to launch advisory services and AAA work that is geared toward better understanding reform measures or which type of account best facilitates the access to and usage of a range of services are important steps.

Lowering transaction costs – not only initiation costs – of financial services through innovation is important in this context. Delivery models such as mobile or correspondent banking, and agent and “branchless” banking and innovations in underlying technology platforms fall in this area, as well as initiatives such as India’s use of the universal ID as a satisfaction of the know-your-customer requirement. A potential way forward appears to lie in advancing these innovations, in partnerships with other agencies, through the suggested “sequenced approach” where the benefits for the poor are continuously monitored.

The potential of traditional financial sector deepening to lift people out of poverty should not be overlooked. Financial sector deepening – though not directly providing the poor with financial services – strengthens the financial sector so that financial intermediation occurs in an effective and efficient manner. Efficient intermediation helps the private sector prosper, allowing small and medium-size enterprises and larger companies to grow and expand employment and opportunity, including for the poor.

These findings suggest that clarifying the World Bank Group’s approach to financial inclusion may be warranted. The current World Bank Group’s strategy of focusing on 25 priority countries may also have to be adjusted going forward, as the remaining excluded will increasingly be broadly distributed among many countries. The Bank Group will also have to decide what it will do to close the remaining access gap in 2020. Recent extrapolations conclude that, taking population growth into consideration, by 2020 just over 1 billion people may still be unbanked. Will the World Bank Group’s support boost access to such an extent that these 1 billion will be reached? Will it be more costly to reach this “last billion” of unbanked? Financial inclusion – if pushed to the very low retail end – is likely to require subsidization, as indicated by recent research. Moreover, closing the access gap of the last billion is likely to be increasingly difficult as the more accessible citizens have been reached. Striking a balance between the costs and benefits of providing universal access and

weighing these against the cost and benefits of other competing priorities will be essential as the World Bank Group provides support to its client countries in achieving the Universal Financial Access Goal by 2020 and further financial inclusion goals beyond this.

## Recommendations

The following recommendations are intended to contribute to the design of the World Bank Group's road map to support the Universal Financial Access Goal 2020.

**Recommendation 1: Clarify approach.** The World Bank Group should adopt an evidence-based and comprehensive approach to financial inclusion that aims at enabling access to a range of financial services with benefits for the poor in a sustainable manner. This should be reflected both in broader strategies (such as that for the Finance and Markets Global Practice) and in its detailed business plan. As part of this approach, the conditions and business models under which subsidization is a useful tool to achieve sustainable services should be specified and consistent, and coherent guidance should be provided to staff on when and how to apply subsidy to financial services versus when a focus on markets can suffice. Also critical to this work is how the World Bank Group systematically finds and replicates innovations that lower transactions costs and improve financial inclusion (Recommendation 2).

**Recommendation 2: Find and replicate innovative delivery models of financial services to the poor through sequenced and evidence-based approaches.** To deliver sustainable, low-cost services, the World Bank Group and its partners should research, pilot, and scale up innovative business models and approaches to reach underserved (especially rural) clients. Such an approach would focus on delineated and evaluable interventions and ensure a feedback loop in the design of new projects. A key part of this is to ensure that the World Bank Group effectively applies its research and evaluative resources to better understand the extent to which its interventions actually support poor households and microenterprises (as well as other excluded groups), and how best to adapt its interventions to different country conditions.

**Recommendation 3: Strengthen partnerships.** Recognizing the value of partnerships as a central instrument of its financial inclusion work, the World Bank Group should strengthen its partnerships by advocating clear strategies, results frameworks, and M&E arrangements for partnership arrangements it has joined or will decide to join.

**Recommendation 4: Implement new tools in country-based diagnostics and strategies.** In countries with a substantial current or planned engagement in financial inclusion, the World Bank Group should implement an appropriate, holistic, and systematic diagnostic tool and, based on such diagnostics, develop country-level strategies for financial inclusion to guide its work. Special attention is appropriate for frontier customers and market segments in countries where there is already substantial engagement. These could inform the Systematic Country Diagnostics and Country Partnership Frameworks. Connected to this, M&E systems should take account of results frameworks established in country financial inclusion strategies, and take a practical and cost-effective approach to improving measures of beneficiary impact.

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