



Bridging the gap: Advancing social and economic objectives through financial inclusion

Innovative finance providers are providing access and opportunity to previously underserved and non-served markets while exceeding investors' profit expectations.

THE DELOITTE CENTER FOR FINANCIAL SERVICES

Introduction

Companies and investors are beginning to recognize the social and financial opportunities inherent in financial inclusion and are acknowledging the long-term value in the pursuit of **a higher bottom line.**¹ In this report, we explore in detail Deloitte's Financial Inclusion Framework (figure 1), with lessons learned from a project that sought to identify inclusive and profitable financial offerings.

Figure 1. The Deloitte Financial Inclusion Framework



The double bottom line of financial inclusion

Financial inclusion² has the power to radically advance social and economic objectives.

Even the most basic financial products can translate to meaningful benefits for marginalized communities. Checking and savings accounts create pathways for wealth accumulation and income smoothing. Insurance products offer security and support in the face of unpredictable life events. Small-value loans buoy consumer demand and propel business and economic growth. In short, financial inclusion helps individuals, households, and businesses achieve improved quality of life, economic growth, and resilience.

With the right environment, innovation, and technological support, financial inclusion can lead to substantial profit opportunities for financial service providers and investors. With more than 1.7 billion **unbanked** individuals in the world and 20 million in the United States,^{3,4} banks and financial technology players have a great growth opportunity in the United States and globally. While this gap is starker in emerging markets, developed markets also face the same challenges: In the United States, a Financial Health Pulse Survey (2020) found that 42 million people are struggling with all, or nearly all, aspects of their financial lives.⁵

With a gap such as this, can institutions financially gain by helping to close it?

Can an institution's pursuit of financial inclusion promise both ***purpose and profits?***

In this report, we explore the key challenges that financial institutions face when trying to fulfil this double promise of financial inclusion. We summarize the lessons learned from a project that tried to discover profitable and inclusive opportunities to accelerate access to finance for women-owned businesses in Kenya, Indonesia, and Vietnam. While these lessons stemmed from research on a specific customer segment in emerging markets, we believe that these tactics are broadly applicable.

Financial inclusion is defined as the ability for individuals and businesses to access financial capital, products, and services in a responsible and sustainable way.

Unbanked are individuals who do not have access to traditional consumer banking products such as checking, savings, and money market accounts.

The market opportunity to serve women-led businesses

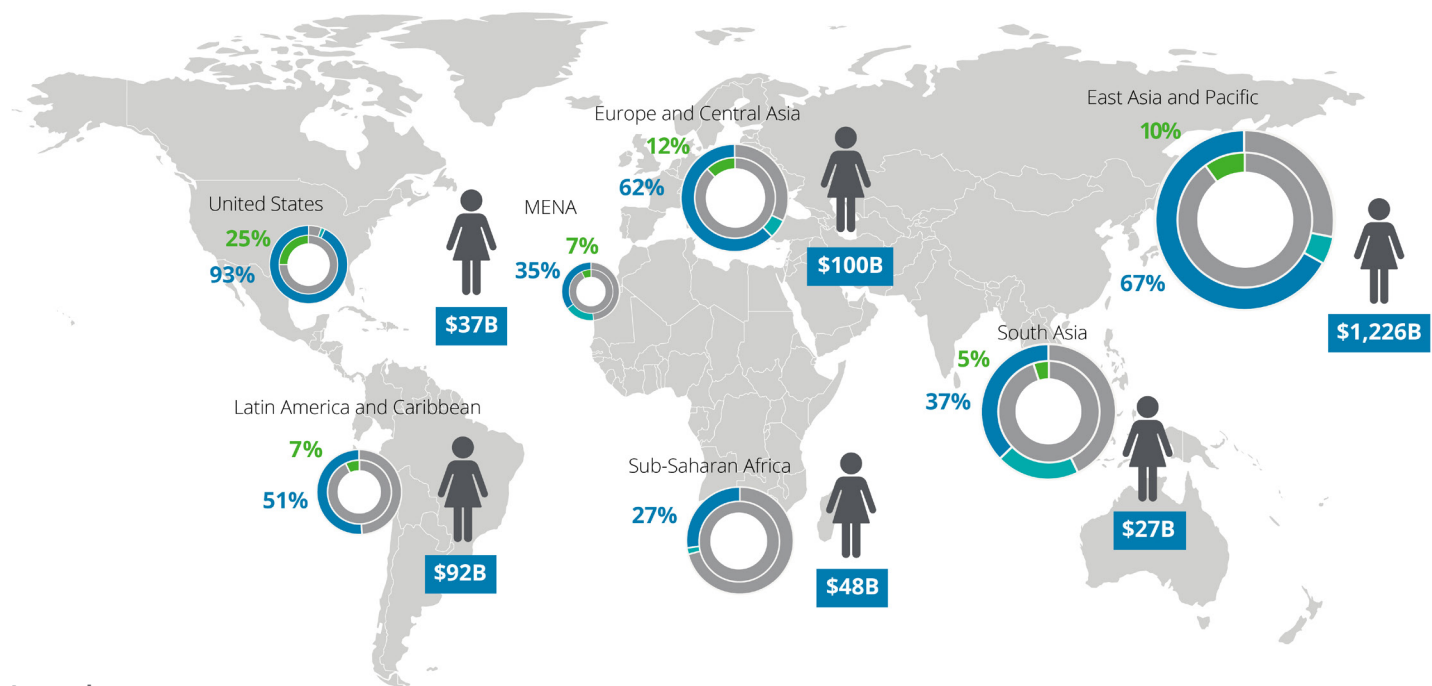
One of the areas that has the greatest long-term value for financial institutions and investors is serving women, and in particular, women-led businesses. According to the World Bank and the SME Finance Forum, the unmet financing needs of women-led businesses around the globe is more than \$1.5 trillion.⁶ Despite its apparently attractive scale, this market remains surprisingly nascent. With more than 1.1 billion women and 70% of women-led small businesses still unbanked globally, this gender gap has been persistently difficult to close due

a combination of cultural, legislative, or technological barriers.^{7,8} Even in the United States, women's access to finance still falls short compared with men: As of August 2020, just 28% of women were financially healthy, compared with 40% of men.⁹ Among business owners, the gap is also significant. For example, recent research found that the average size loan for women-owned businesses was 31% less than for comparable male-owned businesses.¹⁰

Figure 2. The global gap in women's access to credit: A \$1.5 trillion market opportunity

The global gap in women's access to credit

Women around the world are drastically underserved by the financial services sector. Catalyzing finance to these markets could sustainably jump-start women's economic empowerment and unlock a new market.



Legend

- % women w/ bank accounts
- % women w/ formal loans
- Additional % of men with bank accounts (for comparison)

Female population (16–64) = 200,000,000 people

\$1.53 Tn World Bank report on annual credit deficit to women-owned micro-, small-, and medium-sized enterprises (MSMEs)

Sources: \$ - SME Finance Forum data on Finance Gap for women-owned MSMEs, 2018–2019.
% - World Bank Global Financial Inclusion Index, 2017.

Profit barriers for inclusive finance

In order to better understand the types of barriers that financial institutions face to serve women-led businesses, a rigorous assessment* was conducted that included interviews with 188 stakeholders and assessments of 25 financial institutions offering lending products to women-owned businesses. This assessment resulted in the identification of a set of barriers that

are systematically affecting the profitability of financial products offered to women-owned businesses and unbanked individuals. These barriers can be organized into a set of **ecosystem-level factors** (figure 3) and **transaction-level factors** (figure 4) that influence the viability of financial inclusion products and services in an economy or market.

Figure 3. Ecosystem-level factors driving profit for inclusive products

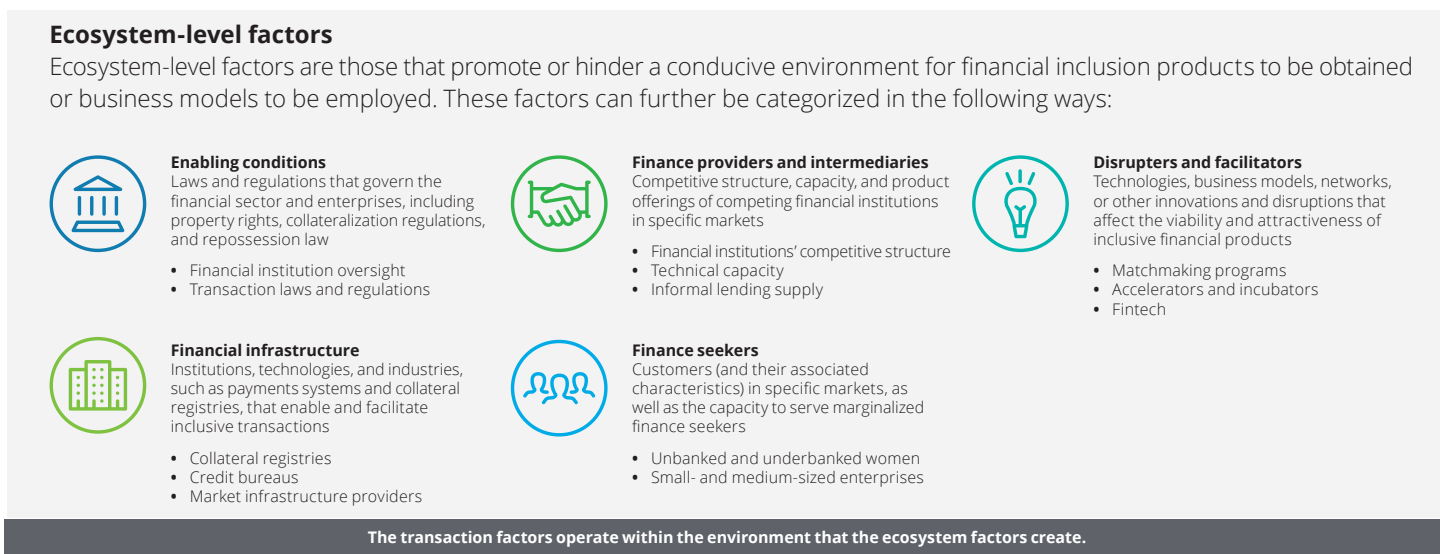


Figure 4. Transaction-level factors driving profit for inclusive products



* In 2020, USAID and the White House's Women Global Development and Prosperity (W-GDP) Initiative commissioned Deloitte Consulting LLP to conduct a thorough market study to understand the current state, challenges, and opportunities in the realm of using MPL (movable property lending) as a mechanism to drive access to finance for women-owned SMEs. As the Deloitte team is wrapping up the project, which produced exciting research findings, our client is encouraging us to publish our findings and lessons learned for both commercial and public audiences in order to increase the adoption of MPL and the impact of the efforts.

Achieving financial inclusion profitably

The following are some transaction-level and ecosystem-level tactics that have supported successful implementation of financial inclusion products in Kenya, Indonesia, and Vietnam. These tactics are also applicable to more developed countries, such as the United States. We will review risk mitigation, cost reduction, and revenue improvement tactics, as well as outline the optimal enabling factors and facilitators that support the business model.

Risk mitigation tactics

Finance providers use the following risk reduction strategies:

- **Leverage anchor companies:** Finance seekers (customers) who have close relationships with large buyers or suppliers can leverage the more powerful actor to provide cover (for example, in the form of a guarantee or evidence of future cash flow).
- **Reduce risk with group guarantees:**¹¹ Group guarantees occur when finance providers lend to a group of borrowers who on-lend to an individual group member. The lender receives the security of knowing the group trusts the borrower and that the group is jointly responsible for repayment.

Cost-reduction tactics

- **Embrace fintech solutions as a cost reduction strategy:**¹² Digital finance and electronic payment systems, including mobile banking, can improve finance provider business operations both by reducing process and “brick-and-mortar” costs and by providing transparency that can reduce costs further. Other fintech innovations, such as alternative credit scoring techniques, can give lenders more accurate measures of creditworthiness and bypass steep transaction costs needed to establish the creditworthiness of borrowers.
- **Leverage local networks:** Local networks, such as agents embedded in local communities, can reduce perceived risk for lenders and simultaneously bolster customer acquisition efforts.

Example: KWMA, a lender in Kenya, accepts guarantees from rural community savings groups as collateral for individual and small business loans.

Another large commercial bank in Kenya uses a distributor finance solution, where large suppliers guarantee small-business milk distributors.

Revenue-increasing tactics

An alternative innovative tactic to strengthen the viability of inclusive finance is to increase the potential for financial return on inclusive financial transactions. Public institutions, international donor organizations, and philanthropic entities can dedicate funds for this purpose:

- **Increase profit per transaction with external incentives:**¹³ External incentives such as “results-based payments,” in which a finance provider receives a payment for each inclusive loan made, can increase profit per transaction, thus incentivizing a finance provider to expand its portfolio of a certain loan type or for a particular customer segment.

Together, these tactics only address the transaction-level barriers. However, financial transactions do not occur in a vacuum, and there’s often room for finance providers to partner with other players in the financial ecosystem to build an environment that is more conducive to financial inclusion.

Example: In Indonesia, peer-to-peer lender Amarta uses a credit scoring algorithm that incorporates machine learning to dynamically adjust parameters over time.

Kenya’s Kopa Kopa uses field agents to monitor when shops change ownership, helping it to acquire new SME customers.

Transaction-level tactics in action: Use of nontraditional blended capital and covenant strategies to help decrease lenders' cost of finance and reduce risk

Investors are optimistic for opportunities to support inclusive finance businesses, as evidenced by the growing number of investment funds and other vehicles directed toward this sector. Investors can structure their support to encourage inclusive transactions, and ultimately realize return, by influencing transaction-level factors for providers—by reducing risk, reducing cost, or increasing revenues and thus profit.

- Providing a bank with some form of guarantee (e.g., first loss, second loss, partial, with conditionality, etc.) can help reduce risk and increase a bank's ability or willingness to invest in innovative financing approaches or focus on a segment that may be perceived as higher-risk. **Example:** One Vietnamese bank used a program where a donor provided funds with preferential interest rates and was responsible for 50% of losses.
- Blended finance or discounted money (such as concessional capital, philanthropic investment, or grants) can significantly reduce a finance provider's cost of funds or offset other transaction costs. **Example:** In Vietnam, the International Finance Corporation (IFC) recently announced a \$100 million investment into VPBank, with about 20% of the working capital line earmarked for women-owned or women-led small businesses.

Strengthen enabling conditions and financial infrastructure

Enabling conditions and the financial infrastructure constitute the systemic factors that influence financial markets and transactions. Though arguably not directly related to specific transactions, they are critical to consider as factors that influence the viability of inclusive finance, as they affect transaction-level revenues, risk, and costs. There's a growing number of innovations that have helped finance providers mitigate ecosystem-level constraints:

- **Increase the depth and availability of**

entrepreneurial data: Financial institutions need a better way to target and inform the individual credit decisions of the underserved. While standardized, high-quality credit information remains essential in the long term, a growing number of innovative finance providers are overcoming this constraint with a range of alternative credit scoring models, for example, based on information such as cell phone account payment rates and behavioral data.

- **Improve market regulation and oversight:**

In recent decades, the cost of regulatory compliance has generally increased, due to greater regulation introduced after (for example) the 9/11 attacks and the 2009 financial crisis. So, innovative lenders are finding ways of addressing this challenge themselves. Many nonbank financial institutions (NBFIs) have been able to develop successful business models addressing mainstream and inclusive finance markets largely outside of formal financial sector regulation, and others have made use of technology to reduce the cost of regulatory compliance.

- **Strengthen property rights and identification:**

In many developing countries, large, informal economies with insufficient forms of identification suggest a need to strengthen business registration and identification efforts. Alternative identification approaches and digital identifications are increasingly being deployed by both the public sector and individual finance providers to overcome aspects of this challenge.

Embrace disrupters and facilitators

As noted previously, many countries have seen growing success through a mix of traditional banking players and new, innovative nonbank finance providers.¹⁴ Many of these new actors are introducing novel approaches to bring together finance seekers and finance providers. As such, traditional financial sector players should embrace disrupters and facilitators in the system as a pathway to increased inclusive lending. In fact, many are—as commercial banks establish partnerships with peer-to-peer, crowdfunding, fintech, and other new players to deploy their capital to formerly unaddressable market segments.

- **Cultivate the fintech ecosystem:**¹⁵ Many developing economies' financial sectors have historically been dominated by commercial banks as lenders.¹⁶ Engaging nonbank actors, including traditional NBFIs such as leasing and more recent innovations such as crowdfunding, peer-to-peer, and other fintech business models, can encourage innovation and drive competitive efficiencies for traditional finance providers. Strengthening of the fintech ecosystem can take many forms, from incubating and accelerating specific companies to assessing regulations to improve the enabling environment for NBFIs and fintechs.

Example: Indonesia's fintech regulator, Financial Services Authority (OJK), has worked directly with fintechs to ensure they reach market segments unreachable by commercial banks.

- **Foster cross-sector partnership:**¹⁷ Due to the overlap of investment returns and social development goals, private and public institutions, government, donor agencies, and private investors can work together to achieve mutually beneficial goals. Specifically, private sector for-profit and social investors may use resources provided by government and philanthropic entities interested in providing risk mitigation mechanisms and concessions to increase the business viability of inclusive finance.

Example: The US International Development Finance Corporation (DFC) has a powerful toolbox of risk mitigation and transaction structuring approaches that can enable financial institutions and investors to increase their risk engagement in the provision of inclusive financial products and services.

Ecosystem tactics in action: Harness the local network of finance providers

Many viable investment opportunities are available through methods beyond normal transaction sourcing processes. Deloitte has found that existing global private investment funds often lack the "last mile" in their developing-country transaction sourcing processes and networks to identify a sufficient volume of socially beneficial investment opportunities. Limitations in investors' transaction sourcing infrastructure suggests that development of greater local partnership and intermediation relationships would be likely to identify more opportunities for investment in socially beneficial businesses, such as inclusive finance providers.

Conclusion

This study of market-based, profit-seeking finance providers using innovative business models to serve previously underserved, women-owned, and women-led businesses can guide finance providers as they respond to growing calls for businesses to proactively address social equity issues relevant to their sectors.

- **Increasing access to financial services is a substantial business opportunity:** The tactics, strategies, and inclusive lending examples described in this publication, and as exemplified by the following case study, illustrate that innovations in technology and business models are rapidly reaching a tipping point, where formerly underserved market segments are becoming profitable markets. Finance businesses and their investors are increasingly responding to the \$1.5 trillion global gender financing market opportunity.
- **Technology is changing the game:** Around the world, there are myriad examples of established and new financial service providers harnessing technology innovations to enable new business models and open up previously underserved markets, from mobile banking to eliminate the costs of brick-and-mortar branches, to the use of regulatory technology (regtech) to reduce the regulatory cost of compliance, through to fintech startups applying proprietary credit scoring and collections algorithms to improve customer acquisition and reduce risk premiums. No doubt technological advances and business model innovations will grow, and today's financial service leaders should consider embracing these new models.
- **Public and private collaboration will be key:** While ecosystem challenges have historically been addressed by government and public sector agencies and transaction-level barriers by financial businesses, there are a growing number of collaborations in which public organizations are playing a role in reducing transaction costs for investors (i.e., blended finance deals) and finance providers (e.g., a philanthropic foundation supports a bank to amplify its profit incentive for serving marginalized communities). Finance providers that embrace and pioneer these partnerships stand to gain an early advantage in the growing financial inclusion market.
- **Not every inclusive finance venture is a profitable one:** There are problems that the free market cannot yet solve with profit. Marginalized communities in extreme poverty are not likely to be an attractive market segment in the near future and should be served by other institutions with different missions. Therefore, it's important to use thoughtful, rigorous tools to assess which opportunities should be prioritized as inclusive and profitable. Financial inclusion at scale will only happen if for-profit companies are, indeed, making profit.

Building into these rapidly growing, undertapped markets with the support of abundant public and philanthropic resources will not only drive **a higher bottom line** for finance providers and investors looking to invest in these companies, but also help accelerate access to finance for millions of underserved individuals and businesses with consequent economic growth, resilience, and social benefits.

Case study: Accessing a new market through movable property lending

The questions

Recognizing the potential scale of the inclusive finance market and recent innovations in financial services provision that might serve it, Deloitte collaborated with USAID to answer two questions.

1. Can a significant number of successful private, for-profit lenders providing inclusive finance to women-owned and women-led small businesses (W-SMEs) be found in developing countries?
2. Are these finance providers formalized to the extent that they are “investable” and able to attract finance from international investors interested in funding their growth and scaling their inclusion benefits?

The approach

To answer these questions, a team of Deloitte consultants embarked on a journey to identify commercial finance providers in developing economies that are serving a traditionally unbanked segment of the population to understand the challenges they faced and the tactics they used to profitably overcome them. In parallel, the team reached out to a wide range of private sector investors to understand their needs and criteria for investing in developing-country finance players. The goal was to bring these two groups together to test the hypothesis that developing-country financial sectors and the global private investment community are at a point of readiness for markets to scale financial inclusion.

What is movable property lending, and why is it significant to inclusive finance?

Movable property lending (MPL) is the use of movable or intangible assets, such as vehicles, equipment, inventory, receivables, or livestock, as collateral for loans. Given that movable property makes up the vast majority of assets for MSMEs in developing countries, these reforms hold the promise to dramatically boost liquidity and growth in the SME sector. While potentially benefiting all kinds of MSMEs, MPL can play an especially critical role in enabling women’s access to finance, as millions of women (and thus women-led SMEs) are legally and/or culturally barred from owning real estate. Unlocking new credit to SMEs can have an even broader impact on women’s financial inclusion, as SMEs are often a key source of employment opportunities, helping women build credit histories and thus access borrowing opportunities themselves.

In determining the optimal markets to study for this project, the team began by screening 30 countries using a variety of criteria, focusing on the W-SME gap and the vibrancy of the inclusive finance market. Kenya, Indonesia, and Vietnam were ultimately chosen as the focus for this study by an advisory group of women’s finance experts and social investors. Each of these markets provided diverse enabling conditions for comparative learning and for attractive investment opportunities.

Kenya	Indonesia	Vietnam
<p>GDP \$95B WSME finance gap \$2B</p> <p>There is potential to scale use of MPL for inclusive finance by increasing use of existing asset financing and asset-backed lending products, especially for banks and non-banking lenders facing liquidity issues.</p> <p>For example, the bank NCBA expressed interest in scaling its current MPL products to better serve women.</p>	<p>GDP \$1.1T WSME finance gap \$21B</p> <p>There may be an opportunity to scale inclusive methods powered by fintechs and nonbank lenders, with the possibility to add MPL to existing approaches.</p> <p>For example, peer-to-peer lender Amarta expressed interest in piloting unconventional MPL methods, such as a supply chain finance scheme.</p>	<p>GDP \$262B WSME finance gap \$5B</p> <p>There may be potential to assist nonbank financial institutions to expand offerings to unbanked markets or to incentivize financial institutions already offering MPL to expand the scope of assets they lend against.</p> <p>For example, nonbank financing company F88 expressed interest in creating a gender-specific MPL pilot.</p>

The answers

Through engagement with inclusive lenders and investors in these markets, Deloitte identified four key factors that allowed inclusive finance to grow sustainably and attract follow-on investors.

- **Asset specialization:** Refers to a practice in which a lender only offers loans for specific assets that they are experienced with and can value, repossess, and resell easily. For example, Kenyan microfinance institution Juhudi Kilimo lends against specialized agricultural and pastoral assets, including livestock. This specialization enables an efficient business model that can profitably serve market segments unaddressable by traditional broad-based financial services business models.
- **Lending against productive assets:** Default risk associated with funding nonfixed business assets can be mitigated by including mechanisms that finance productive assets (assets with the ability to directly generate cash flow and profits). Example productive assets used by SMEs in developing economies include motorbikes, boats, and automobiles. In Indonesia, the startup Crowde partners with agro-dealers to provide farmers with asset-based inputs that are likely to increase crop yields and thus income for repayment.
- **Incorporating repossession or repayment into operations:** Employing creative ways to repossess collateral in the case of default can reduce a finance provider's risk and operational costs (e.g., by employing technology that makes an IT asset financed by the lender inoperable when a borrower is late on payment or has defaulted). Kenyan fintech Kopo uses its digital payments software to collect repayment on loans by taking a direct cut of payments made by customers to its SME borrowers.
- **Conveying future income as security:** Lenders can accept invoices, other business commitments, or expected revenue as collateral to reduce risk. Future income as collateral can be especially appealing to lenders because it eliminates collateral valuation costs. One large bank in Kenya, for example, has trade and supply chain finance offerings that allow SMEs to borrow against accounts receivable.

The impact

The Deloitte team was able to unpack this complex topic well enough to accomplish the following:

- **Identified "positive deviant" financial institutions** in developing economies that are successfully pursuing commercial, for-profit business models that provide inclusive lending; researched their market environment and business models to ascertain their viability for outside investment and identified lessons for the broader inclusive finance community.
- **Created a pipeline of these financial institutions as viable opportunities for investment tailored to increase financial inclusion of women-led SMEs**, and introduced these businesses to commercial, social, and development investors to establish whether private finance can scale these businesses and their inclusive finance benefits.
- **Developed and shared insights** about the process, framework, and key takeaways to help better understand how an organization would conduct MPL, as well as to shed light on how to identify and prioritize profitable and inclusive growth opportunities for other nontraditional finance products. The outputs of this project would also provide broader insights on how to take a for-profit approach toward development issues through the identification and prioritization of future opportunities.

As of December 2020, project insights were shared in multiple forums and audiences, including with leadership at USAID and the DFC and in business conferences. Also, several investors are evaluating potential investment opportunities in the inclusive lenders this project identified.

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Endnotes

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