Financial Inclusion, Tool for Poverty Alleviation and Income Redistribution in Developing Countries: Evidences from Nigeria

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ABSTRACT

Financial exclusion is a major socio-economic problems countries, including Nigeria, are facing. Nigeria has achieved a phenomenal economic growth, but this growth has not been inclusive. Mobile phones, E-mail, E-commerce, internet facilities and 24-hour banking through ATMs have great improved in the country. The Central Bank of Nigeria (CBN) and other stakeholders are presently implementing National Financial Inclusion Strategy (NFIS) in Nigeria. The study examines financial inclusion as a tool for alleviating poverty and redistributing income in developing countries, with special reference to Nigeria. It explores the financial inclusion efforts made at the global level, and highlights the financial inclusion strategy developed in Nigeria to decrease the number of Nigerians that are excluded from financial services. The findings indicate that financial inclusion constitutes important tool for alleviating poverty and redistributing income in developing countries, particularly in Nigeria. The implication for practice is that continuous efforts on the part of stakeholders in financial sector is necessary to decrease the number of people that are excluded from financial services, thereby alleviating poverty and facilitate income redistribution in developing countries.

Keywords: Financial inclusion, poverty alleviation, income redistribution, Nigeria

INTRODUCTION

An effective financial system is essential because it offers savings, credit, payment, and risk management products to people with a wide range of needs. Inclusive financial systems are of great benefit to poor people and other disadvantaged groups as it facilitate broad access to financial services, with-out price or non-price barriers to their use. Without inclusive financial systems, poor people must rely on their own limited savings to invest in their education or become entrepreneurs. Likewise, small enterprises must rely on their limited earnings to pursue promising growth opportunities. Research shows that a total of 39.2 million adult Nigerians representing 46.3% of the adult population of 84.7 million were financially excluded in 2012 (EFIna, 2012). 54.4% of the excluded population was women, 73.8% were aged less than 45 years, and 34% had no formal education, while 80.4% reside in rural areas (EFInA, 2012). Financial inclusion can improve contribute to persistent income inequality and slower economic growth (Beck *et al*., 2000, 2007; Klapper et al., 2006; World Bank, 2008; Demirguc-Kunt and Levine, 2009; Demirguc-Kunt and Klapper, 2012). Hence, the Central Bank of Nigeria and other stakeholders are presently implementing National Financial Inclusion Strategy (NFIS) to decrease the number of Nigerians that are excluded from financial services (CBN, 2012). This is in accordance with the Maya Declaration[*]. The paper highlights scope, objectives and significance of the study; outlines the study

[*] The Maya Declaration is a statement of common principles on the development of financial inclusion policy made by a group of developing nation regulatory institutions during the 2011 Alliance for Financial Inclusion (AFI) Global Policy Forum held in Mexico. Nigeria is a signatory to the declaration.

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methodology; explores the study theoretical framework; examines current state of financial inclusion in Nigeria; outlines financial inclusion initiative in Nigeria; and highlights the study conclusions and implication for practice.

SCOPE, OBJECTIVES AND SIGNIFICANCE OF STUDY

The study explore financial inclusion as a tool for alleviating poverty and income redistribution in order to decrease the number of people that are excluded from financial services in Nigeria. Specifically, the paper examines:

1. The meaning of financial exclusion;
2. Efforts taken at the international level regarding financial inclusion;
3. The current state of financial inclusion in Nigeria; and
4. National financial inclusion strategy adopted in Nigeria.

Developed countries have realised that there are complex and multi-dimensional factors that contribute to financial exclusion; hence, variety of providers, products and technologies that best suits the socio-economic, political, cultural and geographical conditions in these countries have been introduced accordingly. In developing countries, access to formal financial services for the poor majority population remains limited. Reasons responsible for limited available financial services in developing countries include: high levels of government debt which constrained access of credit to firms and individuals; high inflation which discouraged savings; poor physical and institutional infrastructure; poor access by most poor people due to lack of collateral or credit record; and lack of national credit which deter lending (Ellis, 2007; Cali *et al*., 2008). The study is significant as it contributes to a growing knowledge by broadening the scope of literature on financial inclusion.

METHODOLOGY

The researcher adopts secondary data for the study. It is a case study of developing countries; with particular reference to Nigeria. The study explores relevant literature; Central Bank of Nigeria (CBN) data; and international organisations data. International organisations data used for the study include: European Union (EU); World Bank (WB); World Saving Bank Institute; Enhancing Financial Innovation and Access, Consultative Group to Assist the Poor; and World Trade Organisation (WTO). The study findings obtained from through the literature, CBN and international organisations data are deemed sufficient to establish that financial inclusion constitute an important tool role of alleviating poverty and redistribution of income in developing countries. Moreover, to underpin the implication of the study findings for practice, China is used as a case study.

THEORETICAL FRAMEWORK AND REVIEW OF LITERATURE

Defining Financial Inclusion

Financial inclusion refers to timely delivery of financial services to disadvantaged sections of the society (United Nations, 2006; Ramji, 2009). Financial inclusion ensures that customers have access to a range of formal financial services, from simple credit and savings services to the more complex such as insurance and pensions. Financial inclusion also ensures that customers have access to more than one financial services provider that promotes a variety of competitive services. This suggests that ‘financial exclusion’ mean the inability of the disadvantaged to access financial services. Conversely, financial exclusion refers to a process whereby people encounter difficulties accessing and/or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal

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social life in the society in which they belong (Sinclair, 2001; Devlin, 2005; Anderloni and Carluccio, 2006; Kempson, 2006; Carbo *et al*., 2007; EU, 2008). Obstacles to financial exclusion include: unfriendly business environment, lack of sustainable growth; insufficient infrastructure; geography e.g. rural area - limiting physical access; psychology - fear of financial institution's staff, structures, complicated financial products, etc.; information - lack of knowledge regarding products and procedures; low income and poor financial discipline; and poor business practices (Gamji, 2009; Gardeva and Rhyne, 2011; Shafi and Medabesh, 2012). Financial services encompass financial intermediation offered by financial services firms (FSFs) including: investment firms, leasing enterprises, credit institutions, insurance and pension funding firms and other auxiliary services such as the financial markets administration, security broking, and fund management (DFID, 2004; Fadun, 2013). Financial services are fundamental to economic growth and development (WTO, 2012). Moreover, the expansion of financial services that can be accessed by the public can increase income growth thereby reducing the direct impact of poverty (Jalilian and Kirkpatrick, 2001; DFID, 2004; Beck and De la Torre, 2006; Fadun, 2013).

Why is Financial Inclusion Important?

Research shows that a well-functioning and inclusive financial system is linked to faster and equitable growth (Honohan, 2004; Ellis, 2007; Demirguc-Kunt and Klapper, 2012). Qualitative evidence from financial diaries demonstrates that poor people juggle complex financial transactions every day and use sophisticated techniques to manage their finances, whether they use the formal financial system or not (Collins *et al*., 2009; Dupas, 2009). People with access to savings accounts or simple informal savings technologies are more likely to increase consumption, productivity and income, increase investment in preventive health, and reduce vulnerability to illness and other unexpected events (Dupas and Robinson 2009, 2011; Ashraf *et al*., 2010). Likewise, increase access to microcredit enhances investment and entrepreneurship for households with existing businesses (Karlan and Zinman, 2010; Banerjee and Duflo, 2011; Karlan and Valdivia, 2011). The Global Financial Inclusion (Global Findex)[†] data also show sharp disparities in the use of financial services between high-income and developing countries, thereby confirming findings of previous studies (see, for example, Beck *et al*., 2006, 2007; Cull *et al*., 2013).

In the Nigerian context, financial inclusion is achieved when adults have easy access to a broad range of formal financial services that meet their needs and are provided at affordable cost (CBN, 2012). There are five basic pillars of financial inclusion. These are: (1) access to a full suite of financial services, including credit, savings, insurance, and payments; (2) services must be convenient, affordable, suitable, provided with dignity and client protection; (3) services must be provided to everyone who can use financial service including both excluded and under-served populations, with special attention to rural, persons with disabilities, ethnic minorities, and other often-excluded groups; (4) in a diverse and competitive marketplace consisting of a range of financial service providers, supported by robust financial infrastructure and a clear regulatory framework; and (5) clients financial literacy and capability to promote best use of financial services (Gardeva and Rhyne, 2011; CBN, 2012). To facilitate financial inclusion, access to four key services are essential – transaction banking, savings, credit and insurance (World Bank, 2005; EU, 2008).

Financial Inclusion Efforts at the International Level

The World Bank report (2006) reveals that access to finance has been as low as 13% in the rural areas of the poorest households, which implies that 87% of these marginal households

[†]The database and questionnaire are available at: http://www.worldbank.org/globalfindex

lack access to credit with as much as 100% interest rates on these lending, making them even more vulnerable. It has also been found that people borrow at exorbitant rates in case of emergency from local money lenders as formal system of banking and finance is not within their reach. Thus they remain in the vicious circle of poverty always and forever. Financial Access 2010 survey also found that out of 142 countries included in the study, nearly 60 percent experienced a contraction in real per Capita income as a result of the deepening of the global financial crisis during 2008-09 (CGAP, 2010). The absence of financial inclusion keeps the disadvantaged and poor away from the growth parameters (World Bank, 2008). Consequently, all countries in the world took active steps in their financial systems to include all sections of population within the ambit of financial inclusion.

The U.K government tackles financial exclusion in three major ways, by facilitating: access to banking services, access to affordable credit and access to money advice. In this regard, access to banking services includes a basic no-frills account and Post-Office Card Account (POCA) and advisory services will be provided by the advice bureaus, NGO's, Community Development Groups, etc. Besides, a financial inclusion fund has been set up to tackle financial exclusion under the supervision of financial inclusion task force.

The United States government adopts various developmental initiatives to address complex situation of financial exclusion, including enactment of a civil rights law - Community Re-investment Act (CRA). This Act prohibits discrimination by banks against low and moderate income neighbourhoods and imposes an affirmative and continuing responsibility on banks to cater to the credit needs of the excluded sections in the areas where they are allowed to do business.

In Germany, the voluntary undertaking by the banking industry endorses to provide current accounts on demand to everyone. In France, the Banking Act, 1984 made access to a bank account a legal right. In Indonesia, the Microfinance Institution (MFI) mode of operation has developed to its full extent and MFI's operating at regional levels are now out numbering the number of commercial banks in the country. In Bangladesh, the MFI and NGO tie-ups has done wonders which works under prudent regulations of the Govt. and the steering Committee headed by the Governor of the Bangladesh Bank. Meanwhile, it has been estimated that about 2.5 billion people worldwide are currently without access to basic formal financial services (Chaia *et al*., 2009). However, financial exclusion in advanced economies tends to be low as compared with developing countries. In Germany, for Example, 4% and in United States 9% of the population are without basic access to financial services (Peachy and Roe, 2004). But in developing countries financial exclusion is exorbitantly high. 88% of the financially excluded live in Latin America, Asia and Africa. As a matter of fact financial inclusion poses policy challenges that are unique in developing countries, including Nigeria (Chaia *et al*., 2009).

CURRENT STATE OF FINANCIAL INCLUSION IN NIGERIA

The banking industry in Nigeria has improved significantly during the last few decades. Despite making significant improvements in all the areas relating to financial viability, profitability and competitiveness, Nigerian banks have not been able to include vast segment of the population. The nation's existing banking infrastructure has the capacity to promote expansion of Financial Inclusion. The Nigeria banking industry has not less than 5,797 bank branches, 9,958 ATMs and 11,223 POS terminals (CBN, 2012). Although the banked population has grown faster than the bank branch network, the infrastructure is operating below its potential and has the capacity to serve more clients – the average number of clients per branch was 3,882, compared to 3,922 in Kenya and 8,595 in Tanzania (CBN, 2012). To

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reach best-in-class levels, the average branch should serve more than double the number of clients it serves today. Hence, Nigeria lags behind some of its peer African countries with regards to the provision of financial services. This poses serious challenges to nation's economic growth and development. In 2010 for instance, only 36% – roughly 31 million out of an adult population of 84.7 million were served by formal financial services (Table 1), compared to 68% in South Africa and 41% in Kenya (EFInA, 2010).

Table 1. Current state of financial inclusion in Nigeria

	Percentage (%)	*Total Number (Million)*
Adult Population	100	84.7
Financially Served	53.7	45.5
Financially Excluded	46.3	39.2
Formally Served (Included)	36.3	30.7
Informally Served (Included)	17.4	14.7
Banked	30.0	25.4
Other Formal Institution	6.3	5.3

Source: EFInA Access to Financial Services in Nigeria, 2010 Survey

Meanwhile, between 2008 and 2010, the percentage of "completely excluded" fell from 53% to 46%, while those served by the "informal sector" fell from 24% to 17% (EFInA, 2008, 2010). Similarly, "formal other" doubled from 3% to 6% and "formally banked" rose from 21% to 30% (EFInA, 2008, 2010).

Geographical Difference of Financial Inclusion in Nigeria

Financial inclusion is most progressed in the urban areas of Nigeria, especially in the southern parts of the country (Table 2). Northern Nigeria is particularly disadvantaged as 68% of adults in the North East and North West zones respectively are excluded from financial services as against 33% and 32% for South West and South East respectively. Rates of formal inclusion range from 49% in the South West Region to only 19% in the North West Region. 'Informally included' are more in the North Central region, where 23% of the adults have access to only informal services.

Table 2. Financial inclusion in Nigeria by region

Zone	*Formally Banked (%)*	*Formal Other (%)*	*Informally Served (%)*	*Financially Excluded (%)*	*Total*
North West	13	6	13	68	100
North Central (Inc. FCT)	27	6	23	44	100
South West (Inc. Lagos	42	7	18	33	100
North East	15	6	11	68	100
South East	41	6	21	32	100
South South	39	6	19	36	100

Source: EFInA Access to Financial Services in Nigeria, 2010 Survey

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Furthermore, majority (80.4%) of those who are fully excluded from formal and informal financial services live in rural areas; while the remaining 19.6% live in urban areas (EFInA, 2010). Three potential explanations are possible: Firstly, the physical distance to bank branches in most rural areas is long and this poses high cost for accessing financial services. Secondly, the lower economic activity in rural areas limits the profitability of financial institutions. Thirdly, a commonly lower degree of education and financial literacy in rural areas decreases the probability for clients to makes use of financial products and services.

Characteristics of the Financially Excluded

A total of 32 million adults, representing 46.3% of the adult population, are currently financially excluded**.** Out of this**,** women account for 54.4%, while youths (below 45years) account for 73.8%. The uneducated, those without formal education, are about 34.0%, while 80.4% of the rural residents are financially excluded. Furthermore, two key demographic trends that have implications for financial inclusion are: (i) relatively young population that is rapidly urbanising; and (ii) fertility in Nigeria remains high and unchanged over almost two decades – 5.9 births per woman in 1991 and 5.7 births in 2008. On the average, rural women have two children more than urban women (6.3 versus 4.7 children). Nigeria is the world's tenth most populous country. According to the National Population Commission, Nigeria's population grew from 140.4 million in 2006 to 167.9 million as at the end of October 2011. Out of this, 82.1 million were females and 85.8 million were males. Using a population growth rate of 3.2%, which is the same rate that the Commission used in 1991 and 2006, respectively, Nigeria's population is expected to reach 221.4 million by 2020.

FINANCIAL INCLUSION INITIATIVE IN NIGERIA

The Central Bank of Nigeria and other stakeholders are presently involved in the implementation NFIS in Nigeria. The purpose of NFIS is to decrease the number of Nigerians that are excluded from financial services from 46.3 % to 20% by 2020; and increase the number of Nigerians that are included in the formal sector from 30% in 2010 to 70% by the year 2020 (CBN, 2012). The stakeholders in enhancing the nation's financial inclusion are: banks, other financial institutions, insurance, regulators, technology/telecommunications firms, public institutions and development partners/experts (CBN, 2012). Meanwhile, EFInA (2010) survey identified five major barriers to financial inclusion in Nigeria: low and irregular income, physical access, financial literacy, affordability and eligibility. Out of these, the three key barriers are accessibility, eligibility and financial literacy. Financial literacy awareness and understanding of financial terms differ according to complexity of the product and product features, as well as commonality of product use within population. There are five major sources of financial information in Nigeria: family and friends; someone trusted in the community and religious leaders; bank, employer and work colleagues; and electronic and print media by relevant stakeholders (EFInA, 2010).

The NFIS goal in Nigeria is being pursued through a broad range of coordinated interventions, with high priority as highlighted below (CBN, 2012):

1. Transformation of the existing uniform **Know-Your-Customer (KYC) regulation** into a simplified Risk-based Tiered Framework that allows individuals that currently do not have the required formal identification measure to enter the banking system.
2. Articulation and implementation of **Regulatory Framework for Agent Banking** to enable financial institutions to bring banking services to the currently unbanked in all parts of the country.

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3. Definition and implementation of **National Financial Literacy Framework** to increase awareness and understanding of the population on financial products and services with the goal of increasing sustainable usage.
4. Implementation of a comprehensive **Consumer Protection Framework** to safeguard the interest of clients and sustain confidence in the financial sector.
5. Continued pursuance of **Mobile-Payment System and other Cash-less Policy** efforts to lessen the cost and enhance the ease of financial services and transactions.
6. Implementation of **Credit Enhancement Schemes/Programmes** to empower micro, small and medium enterprises:
   a. Micro, Small and Medium Enterprises Development Fund, 60% of which will support the on-lending activities of microfinance banks and institutions to women enterprises and clients.
   b. Nigerian Incentive-based Risk Sharing System for Agricultural Lending (NIRSAL)
   c. Entrepreneurship Development Centres (EDCs)
   d. Restructuring and Refinancing Facilities for SMEs
   e. SME Credit Guarantee Scheme

CONCLUSION

The study has examined financial inclusion as a tool for alleviating poverty and redistributing income in developing countries, with special reference to Nigeria. It explores the financial inclusion efforts made at the global level, and highlights the financial inclusion strategy developed in Nigeria to decrease the number of Nigerians that are excluded from financial services. We concluded that increasing attention is given to financial inclusion by countries of the world are focusing on inclusive growth and poverty alleviate. Considering low levels of financial penetration and deepening in developing countries, including Nigeria, financial exclusion remains an area of concern. This is obvious as the study revealed that 39.2 million adult Nigerians representing 46.3% of the adult population of 84.7 million were financially excluded in 2012**.** Further analysis also revealed that 54.4% of the excluded population were women, 73.8% were aged less than 45 years, 34% had no formal education, and 80.4% reside in rural areas. The findings indicate that financial inclusion constitutes important tool for alleviating poverty and redistribution of income in developing countries, particularly in Nigeria. The implication for practice is that continuous efforts on the part of all stake holders in Nigeria is necessary to decrease the number of Nigerians that are excluded from financial services, thereby alleviating poverty and facilitate income redistribution.

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