A Systems Approach to Financial Services

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Introduction

In its infancy and made famous by such institutions as the Grameen Bank, microfinance functioned as a product-driven approach. It has a single aim: move people out of poverty via group-based microenterprise loans. But more recently, a “systems” thinking approach has populated the financial landscape with a rich variety of stakeholders. Instead of microfinance being the sole purview of microfinance institutions (MFIs), it has expanded to include such diverse actors as global payment and transfer providers, retail banks and small, client-friendly savings groups.

As stakeholders in the microfinance industry have broadened, so too has the meaning of quality. Where quality once meant that could clients enjoy the timely delivery of credit, it now means they can choose from a wide range of reliable, transparent and flexible options. Delivering high quality services, however, is not always easy. Providers and policy makers must understand a wide array of social, cultural, economic behaviors that, together with individual needs and preferences, define demand and shape thinking about a more inclusive financial ecosystem.

Three major shifts

As the industry has matured, many events have reshaped thinking about early single-institution approaches to financial services for the poor; but three stand out as key. The first has been a shift from a narrow focus on the institution and its performance to a much broader focus on clients—understanding their behavior, financial service needs, and how various providers can better meet these needs. No longer limited to investing in microenterprises, microfinance now encompasses all financial services and how to provide them in a way that improves the quality of life of poor women and men. The second important shift, has been from a narrow supply-led view to a broader focus on the financial ecosystem. In addition to a renewed focus on consumers (demand), proponents of the “systems” approach acknowledge the variety of providers and services, including the substantial role of the informal sector. The third shift has been the massive opportunity to expand outreach through new business models deploying technology and agent networks.

Trends, findings and lessons

CLIENTS, PROVIDERS AND PRODUCTS MAKE UP THE CORE OF THE FINANCIAL SERVICES SYSTEM. Understanding client needs and behaviors aids in the design of cost-effective, convenient and appropriate solutions. Clients may find a range of providers useful from community-based providers offering simple savings, loan and investment services to larger institutional providers offering savings, credit, insurance, and remittance services. The key is to provide products that are uncomplicated, flexible, convenient, safe and affordable.
RULES GOVERN THE NATURE OF INTERACTIONS WITHIN THE FINANCIAL ECOSYSTEM. These rules can be formal or informal, self-imposed or externally mandated. They dictate the types of services that are offered, as well as the costs of accessing and providing financial services. Whether efforts to expand financial inclusion succeed or fail depends largely on these rules.

INFORMAL RULES CAN ENHANCE OR IMPEDE THE EFFECTIVENESS OF FORMAL RULES. Social norms and local value systems motivate the behaviors of the clients. For example, the success of Islamic finance illustrates the importance of cultural norms in driving demand for financial services. However, informal rules can also change in response to new influences. The rise of mobile money and the increasing participation of women in microfinance are both examples of how informal rules have been reshaped by new influences.

FORMAL RULES ARE SET BY GOVERNMENTS AND INDUSTRY BODIES. They affect access to markets, the range of available products and the competitive landscape. They can range from the enforceability of contracts and registration of assets, to the existence of a national identification system and the protection of public deposits. Government regulations seek to protect consumers, and include standards of transparency and disclosure, rules for the fair and ethical treatment of clients and effective systems for consumer recourse.

GOVERNMENTS SHOULD PROMOTE EDUCATION THAT STRENGTHENS FINANCIAL LITERACY AND CAPABILITIES OF CLIENTS. They should build and coordinate financial inclusion strategies at the national and international levels. Some initial successes have been achieved through the formation of the Alliance for Financial Inclusion and the Global Partnership for Financial Inclusion, both of which promote effective and cohesive policy making.

INDUSTRY BODIES HAVE EMERGED TO SELF-REGULATE THE FINANCIAL SECTOR. Examples include the Social Performance Task Force, the Smart Campaign and Microfinance Transparency. These organizations address issues of product design and delivery, transparency, pricing, client indebtedness, client treatment, privacy and complaint resolution. In addition, they provide a link between industry and governments, which helps to harmonize laws and practices.

SUPPORT ORGANIZATIONS PROVIDE RESOURCES, INFORMATION AND SERVICES THAT STRENGTHEN THE CORE. Their contribution includes capacity development for stakeholders, coordination services, advocacy, research and reporting. Some organizations also provide support in the form of credit bureaus, deposit insurance and accounting services.

BETTER DATA PROMOTES FINANCIAL INCLUSION AND REDUCES THE COST OF SERVICES. Extending access to financial services requires data from supply and demand side surveys, financial landscape studies and databases that measure important indicators of financial inclusion.

DONORS MUST SHIFT THEIR FOCUS TO NEW GEOGRAPHIES AND INSTITUTIONS WHERE PRIVATE CAPITAL IS SCARCE. Most donors remain entrenched in certain regions and continue to fund large MFIs. Their money should instead flow to areas where private funding is scarce, such as information exchanges, capacity building for stakeholders, and incentives for providers to increase financial outreach.

BRANCHLESS BANKING CAN SCALE FINANCIAL INCLUSION MODELS. While community-based MFIs have adopted a largely branchless model, more formal financial institutions have been
following suit through the introduction of ATMs, mobile branches and the use of third party agents.

AGENT NETWORKS CAN PROVIDE CASH-IN AND CASH-OUT SERVICES ON BEHALF OF FINANCIAL INSTITUTIONS. Formal providers are already making the investments in infrastructure necessary to serve target markets. But while electronic devices such as mobile phones, computers, and POS devices are effective in extending banking services, agents are also an important component. In many cases, agents are able to provide a greater range of services than electronic solutions.

MOBILE BANKING SERVICES HAVE EMERGED IN SOME COUNTRIES. Equity Bank in Kenya has introduced Iko Pesa, a fully integrated bank account accessible via the Orange network. In Pakistan, a similar service called EasyPaisa has developed through a partnership between Pakistani telecom Telenor and Tameer Bank.

Conclusion
Together, these three drivers—a focus on understanding clients better; acknowledgment of the multiplayer, multifunction nature of the financial ecosystem; and the opportunities technology presents—support increased financial inclusion.