Louis Kasekende: Opportunities and challenges of financial inclusion

Remarks by Dr Louis Kasekende, Deputy Governor of the Bank of Uganda, at the National Microfinance Conference, organized by the Association of Microfinance Institutions in Uganda (AMFIU), Jinja, 5 May 2011.

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Hon. Syda Bbumba,
Minister of Finance, Planning and Economic Development,
The CEO of Association of Microfinance Institutions in Uganda (AMFIU)
Distinguished representatives of the various members of AMFIU;
The representatives of the Donor Community;
Distinguished Guests;
Ladies and Gentlemen

I am very pleased to be here this morning to address the National Microfinance Conference organized by the Association of Microfinance Institutions in Uganda (AMFIU). I am indeed delighted that the theme for this year's annual conference "***Opportunities and Challenges of Financial Inclusion***" is something that is close to our hearts, and is a very topical issue in the current times.

The importance of this topic is underscored by the high levels of financial exclusion prevailing especially in the developing countries including Uganda. Although access to an array of financial services and tools is growing, the Alliance for Financial Inclusion (AFI) estimates that more than ***two billion*** adults around the world do not have access to financial services – whether formal or informal.

Financial services such as savings products, credit and loans, payment and money transfer services, insurance, and many others, provide poor people with greater capacity to stabilise and even increase their incomes, build assets and cope with shocks. These financial products have proven to be great tools that mitigate the effects of low, irregular and unreliable incomes which keep many people below the poverty line.

In Uganda, Financial Inclusion remains a challenge in spite of the many gains and successes we have achieved in the financial sector. The 2009 Finscope study revealed that only ***28%*** of the adult population above 16 years of age are served by formal institutions such as Commercial Banks, Credit Institutions and Microfinance Deposit-Taking Institutions (MDIs); while ***42%*** are served informally by Savings and Credit Cooperatives (SACCOs), Village Saving and Loan Associations, etc. The remaining ***30%*** of the Ugandan population is not served by either formal or informal financial service providers. The study also revealed that the most commonly used source of credit were; shops ***(54%)***, friends ***(25%)*** and informal groups ***(24%)***. Only ***7%*** were found to have borrowed from commercial banks while ***3%*** and ***2%*** were borrowing from MDIs and SACCOs respectively.

Financial inclusion is a central theme for all of us because most of those in poverty do not have access to financial services as already mentioned. Poverty alleviation is a top priority for the Uganda Government and financial inclusion is an essential component of the country's poverty alleviation strategy. It is our hope that greater financial inclusion will ultimately reduce poverty and inequality. This conference is, therefore, timely for AMFIU to regroup and discuss a contemporary issue of financial inclusion. I, therefore, thank the management of AMFIU for facilitating this conference.

Ladies and gentlemen, allow me to delve deeper into the pertinent issues which must be taken into account by all financial service providers in order to foster financial inclusion.

- ***Assuring savers of the safety of their member-savings.***

– The lack of such assurance can be a great source of suffering to savers whenever there is collapse of any service provider. This is mostly pronounced among the many semi-formal and informal service providers like SACCOs and Community Groups. Prudential regulation and other safety nets for service providers should always be in place to reduce on this risk. In that way, the country will be able to attract more savers into formal institutions.

- ***Reducing lending risk and risk perceptions inherent in lending to key productive sectors particularly Agriculture and SMEs.***

– While agriculture forms the backbone of the Ugandan economy and provides employment to the majority of Ugandans, there is little evidence that credit is churned into this sector in adequate proportions. Exclusion of agriculture in lending is indeed exclusion of many people especially in Uganda.

It is therefore crucial that service providers should design financial products suited for the agricultural sector, i.e. reasonable priced credit facilities and agriculture insurance. Innovation allows financial products and services to be customised to those who need it and it is crucial for creating a diversity of solutions to financial inclusion.

The Bank of Uganda is currently implementing an Agricultural Credit Facility set up by the Government of Uganda in partnership with Commercial Banks; Uganda Development Bank Ltd, Micro Deposit Taking Institutions and Credit Institutions. The facility is for the purpose of providing medium/long term loans to agricultural loans to agricultural sector. However, no single MDI has participated in the scheme as the bulk of their clientele are small scale farmers requiring loans of a short term nature.

- ***Expanding outreach***

– The cost of locating a financial institution branch in a rural set up where the road network is poor, electricity is non-existent, and the population is so dispersed is enormous. It is also expensive for savers who travel long distances to go and deposit small savings in their accounts. The cost of credit administration and borrowing becomes very dire in such situations. It is therefore important to explore the use of agents and the new technology such as mobile phone banking and points of sale as tools for financial inclusion.

- Harnessing the advantages that new technology offers may reduce the cost of opening outlets especially in hard-to-bank areas that may initially not be profitable for financial service providers. Technology will continue to offer low-cost solutions and opportunities that were never thought about in the past. Service providers need to harness these opportunities.

- ***Promoting alternative banking methodologies***

Methodologies such as group lending in microfinance and Islamic Banking & Finance which use ***collateral substitutes*** and other ***risk-sharing mechanisms*** that are not used by conventional bankers provide viable alternatives that should be critically assessed. This opportunity should be supported by a flexible (different laws and regulations for different sectors) and strong regulatory and supervisory framework that guarantees safety and soundness of institutions. Innovative financial inclusion works better when a strong legitimate framework balances International Standards and national conditions.

- ***Financial literacy and the improved financial capability within the majority of the population***

  – One of the issues limiting financial inclusion is paucity of information provided to clients and the lack of a good understanding or interpretation of that information. We need a national framework to address financial literacy and financial consumer protection. This framework should assign roles to different stakeholders within the financial sector plus providing for coordination among financial service regulators.

  – We should design and enhance twinning and financing arrangements with the Ministry of Education and Sports, the National Curriculum Development Centre and financial service providers to roll out a Financial Literacy and Financial Consumer Protection program to schools, colleges and universities, building on the recent launch of the publication on "***Towards an Effective Framework for Financial Literacy and Financial Consumer protection in Uganda by Bank of Uganda***".

For our part, the BOU has been actively involved in exchanges with the Ministry of Finance planning and Economic Development on the regulation of Tier 4 institutions. In addition, the Bank has reviewed the Financial Institutions Act (2004) and the Microfinance Deposit-taking Institutions Act (2003) to accommodate alternative banking methodologies (Bank assurance, and Islamic Banking and Finance). The Bank has also drafted ***Consumer Protection Guidelines*** for all licensed institutions and has, with support from GIZ, commissioned a consultancy to undertake a Regulatory Diagnostic to establish the suitability of Uganda's financial sector legal framework to branchless banking. The results of this study should result into roll out of branchless banking under a suitable regulatory framework and consequent reduction of cost of opening outlets in hard-to-bank areas. The Bank has also licensed three Mobile money network operators (MNOs), MTN, Airtel and UTL in partnership with Stanbic Bank, Standard Chartered Bank and DFCU bank respectively. By end March, the operators had 1,968,125 registered customers and in the period January to March 2011, the total number of transactions were 13,220,674 with a total value of Shs.551,010 million. It is our belief that a combination of the above initiatives will open new opportunities for financial intermediation and Inclusion in a safe and sound system.

In conclusion, the quest for Financial Inclusion should be complemented by safety and soundness to ensure that gains made in inclusion are not eroded by loss of savings or loss of confidence in financial institutions. The BOU will continue to support formalisation of innovative approaches through improvements in regulatory framework as well as working with other stakeholders. However, unlicensed institutions that take deposits from the general public under the guise of member-savings and those intermediating compulsory savings are doing so illegally and must stop.

I also wish to state, as I conclude, that new technology especially in the area of electronic money transfer and agency banking are destined to drive most of the future efforts aimed at financial inclusion. A lot of care must therefore be taken to build sufficient risk-mitigation and regulatory mechanisms that ensure safety of savers' funds but at the same time promoting further advances to avoid stifling technological development.

With these remarks I once again thank AMFIU for the foresight which led to the establishment of the AMFIU calendar at which very useful topical issues are discussed. It is my ardent hope that the conference will achieve its objectives as set out in the Agenda.

I thank you.