COLUMBIA THREADNEEDLE INVESTMENTS

Your success. Our priority.

TACKLING FINANCIAL EXCLUSION THROUGH THE FINANCIAL MARKETS

JUNE 2018

Gareth Davies
Head of Responsible Investing Solutions

Rose Beale
Thematic Analyst
Responsible Investment

A global issue

We have never lived in a more interconnected society. We can communicate with friends and colleagues on the other side of the planet in the blink of an eye, and have more access to more information than ever before. In 2017 alone, more data was captured than in the previous 5,000 years of history[1]. Yet more than two billion people worldwide do not have access to basic banking services[2]. Principally, the "unbanked" are concentrated in a handful of countries. Indeed, just 25 countries represent 73% of the total, with India and China together accounting for 32%[3].

However, make no mistake, this is a global issue. The United Kingdom has more than a million unbanked people (http://www.financialinclusioncommission.org.uk/facts). In the United States, one in 13 households has no access to a checking or savings account (Financial Exclusion: Why it is more expensive to be poor (2017)).

It is for these reasons that the UN Sustainable Development Goals (SDGs) not only specifically refer to financial inclusion in developing markets, but include a global target to "encourage and expand access to banking, insurance and financial services for all" (SDG 8, Decent Work & Economic Growth).

[1] https://www.weforum.org/agenda/2018/04/the-data-trap-why-numbers-never-tell-the-full-story/
[2] http://www.worldbank.org/en/topic/financialinclusion/brief/achieving-universal-financial-access-by-2020
[3] https://globalfindex.worldbank.org/

A personal and economic problem

Having a bank account allows you to receive income as well as pay bills. In the west it is usually a prerequisite for getting a job. Being outside of the banking system thus forces people towards temporary, unofficial employment. This is not only a disruptive and inconsistent method of income, it is also outside of the national fiscal establishment, meaning there is an opportunity cost in terms of tax loss to the government and ultimately the country as a whole. This is why it is a global issue with consequences for economies and financial markets.

There are many and complex reasons for financial exclusion across the world, but one of the main causes is simple to identify: a lack of access to money. Poverty across the world is pervasive and financial exclusion is a consequence of this. Another barrier is geographical distance, with access to financial services for many in remote parts of the world restricted by virtue of distance to a provider. Finally, a lack of financial services that are specifically designed and appropriately priced for those on lower incomes is also a significant impediment to access.

Tackling financial exclusion by improving access to banking services, such as credit and insurance, will help individuals to establish businesses, and to save, invest and protect themselves financially for the future. This will drastically improve lives and economies.

Towards solutions

Governments and supranationals are coming together to set specific targets to address financial exclusion. At a high level, the UN Sustainable Development Goals have a number of targets focused at the global level – as in SDG 8, Decent Work & Economic Growth, mentioned above. But targets are also being set pertinent to particular groups underserved by virtue of social economic status or gender: hence the inclusion of access to finance considerations within SDG 1, No Poverty; SDG 5, Gender Equality; and SDG 10, Reduced Inequalities.

Specific global initiatives to address the issue also include those driven by the World Bank Group. Its Universal Financial Access 2020 initiative brings together different partners around the globe with the goal of giving a billion people the opportunity to open an instant access account by 2020.[4] Additionally, the G20 has committed to advancing financial inclusion worldwide through the implementation of the G20 High-Level Principles for Digital Financial Inclusion.[5]

The role of investors

Global initiatives will go a long way to helping tackle the root causes of financial exclusion, but investors can also play a crucial role. Organisations addressing financial

[4] http://www.worldbank.org/en/topic/financialinclusion/brief/achieving-universal-financial-access-by-2020
[5] https://www.gpfi.org/publications/g20-high-level-principles-digital-financial-inclusion

exclusion can provide attractive opportunities, both in terms of social impact and financial reward.

We have identified a number of organisations dedicated to ameliorating access issues, available via public equity and debt markets. Typically these do one or more of the following: address financial services provision for those on lower incomes; address financial services provision for underserved demographics such as women in some economies; or provide dedicated services for small-scale organisations on favorable terms.

Social and sustainability bonds provide a key mechanism for directing capital towards efforts to improve financial inclusion, for example, the Social Bond issued by the International Finance Corporation (IFC). Recipients of funding must either specifically target increased participation of those on low-incomes within their business models, or be small/medium-sized enterprises in emerging markets owned and run by women. Improving financial access for women in particular represents an enormous opportunity: McKinsey estimates that achieving gender parity in the workforce internationally could add as much as $12 trillion to global GDP by 2025.[6]

The companies benefiting from the IFC Social Bond are extremely diverse and include: a Romanian clothing business owned by two sisters and with 80% female employees; a Ugandan dairy business using small-scale farmers and suppliers; and a number of specific female-focused projects undertaken by larger companies. For instance, some of the funds raised are supporting the geographic expansion into India, China and Brazil of Essilor, a €115 million market cap company providing glasses and other visionware.[7]

This illustrates how larger companies, and their investors and financiers, can facilitate delivery of socially advantageous solutions. This also holds true for tackling financial inclusion. Newly listed Brazilian company PagSeguro enables micro-merchants to access banking services by interfacing with merchant smartphones, allowing for formalised payments usually reserved for larger merchants. Meanwhile, Bank Rakyat Indonesia, one of Indonesia’s largest banks, has since 2008 doubled its network of branches and outlets, partly to target underbanked customers in remote areas. The Bank is also collaborating with the Indonesian government to enhance the digitalisation of the sector by providing free domain facilities to a million small entrepreneurs. These efforts directly advance global sustainable development priorities – notably the target within SDG 8, Decent Work & Economic Growth, to “encourage and expand access to banking, insurance and financial services for all” – while strengthening the domestic economy.

---

[6] https://www.mckinsey.com/featured-insights/employment-and-growth/how-advancing-womens-equality-can-add-12-trillion-to-global-growth

[7] https://www.ifc.org/wps/wcm/connect/54dd263d-1097-42f0-8ce0-16e13b762c22/IFC+Social+Bond+Program+Presentation+final_Oct2016.pdf?MOD=AJPERES

The triple opportunity

We believe that tackling financial exclusion around the world is not just the right thing to do, it is something that will benefit economies and boost financial markets. More people entering the financial system will not only start up more businesses but also boost tax receipts.

As asset managers focused on long-term financial performance, companies and non-corporate issuers actively seeking to address financial exclusion present us and our clients with a compelling trio of opportunities: the opportunity for financial reward; the opportunity to contribute to delivery of the UN Sustainable Development Goals; and the opportunity to play a role in creating a more inclusive and enriched global economy.