

**E.Bumsteinas. 25 October 2012**

**“Public goods approach to innovation in financial inclusion”**

Draft Concept Note

The title of our session is “Public goods approach to innovation in financial inclusion”. The idea is to debate the role and scope of organisations with a "public good" mission to promote innovation in financial inclusion.

Date and Venue:

16 November 2012, European Microfinance Week, Luxembourg

Speakers on the panel:

Moderator: Edvardas BUMSTEINAS, Senior Investment Officer, EIB

Ann MILES, Microfinance Director, MasterCard Foundation

Mary Ellen ISKANDERIAN, President and CEO, Women’s World Banking

Frederik J. VAN DEN BOSCH, *Manager Micro & Small Enterprise Finance (MSEF)*, FMO

Hermann BEYTHAN, Partner, Linklaters, LLC

Hypothesis:

In economics, a **public good** is a good that is both non-excludable and non-rivalrous in that individuals cannot be effectively excluded from use and where use by one individual does not reduce availability to others. Examples of public goods include fresh air, knowledge, lighthouses, national defence, flood control systems and street lighting. Some of the goods, such as primary education and basic healthcare, might not be public goods in the economic sense, but are treated as public goods since exclusion from such goods might no longer be considered as acceptable in most societies.

According to the economic theory, public goods provide a very important example of **market failure**, in which market-like behavior of individual gain-seeking does not produce efficient results. The production of public goods results in positive externalities which are not remunerated. If private organizations don't reap all the benefits of a public good which they have produced, their incentives to produce it voluntarily might be insufficient. Consumers can take advantage of public goods without contributing sufficiently to their creation. If too many consumers decide to 'free-ride', private costs exceed private benefits and the incentive to provide the good or service through the market disappears. The market thus fails to provide a good or service for which there is a need.<sup>i</sup>

One might ask to what extent financial inclusion can be considered as a public good? From an economic perspective, it is not a public good since individuals can be excluded from accessing financial services. However, just like with primary education and basic healthcare, financial inclusion is increasingly seen as public good, in the sense that exclusion is neither desirable nor justified, especially for basic services (e.g. savings). Moreover, when financial services are provided, the importance of public goods is manifested in a number of ways.

At the level of consumers, basic financial literacy is a prerequisite to avoid client overindebtedness and to ensure that clients are able to take a full advantage of financial products that are offered to them by banks and microfinance institutions. In reality, the private costs of investing in financial literacy are likely to exceed private benefits which can result in limited and biased financial education. **Master Card Foundation** is one of the key players in the area of financial literacy. Anne Miles, Microfinance Director at MCF, will share the main lessons and results of her programs in Africa.

At the level of the intermediary (e.g. microfinance institution), there might be under-investment in staff (for fear that they will leave to the competition) or financial institutions might be reluctant to disclose their interest rates in a transparent manner since this would render them non-competitive as they would be seen as expensive compared to the competition (hence, the prevalence of “flat” interest rates). Mary Ellen ISKANDERIAN, President and CEO of **Women’s World Banking**, will share with some of her experiences in promoting practices of a public good nature at WWB and its affiliates.

On the funding side, there is a need to provide seed funding to innovative projects, as well as to fund basic research and development, and to encourage entrepreneurship at all levels of society. **FMO** has accumulated vast experience in funding of various projects that are sometimes overlooked by private investors. Frederik J. VAN DEN BOSCH, *Manager Micro & Small Enterprise Finance (MSEF) at FMO* will share with us his experiences in providing funding for some of the smallest businesses in developing countries, and outline the role of FMO in such projects.

Finally, we will look at the limitations and possibilities of the provision of public goods from the legal side. The main emphasis of the presentation by Hermann BEYTHAN, Partner at Linklaters, is on the role of good governance and contracts in ensuring that the provision of public goods is not neglected. He will provide a number of examples from his recent cases in order to illustrate how funders can ensure that their investments promote public good and how this could be applied in financial inclusion.

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<sup>i</sup> Definitions from Wikipedia.org