The *Financial Inclusion Compass* 2022

The e-MFP Survey of Financial Inclusion Trends

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EUROPEAN MICROFINANCE PLATFORM
ADVANCING FINANCIAL INCLUSION

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Foreword

When the last *Compass* was being written during Summer 2021, the world was facing yet another wave of yet another variant of Covid-19. While life looked something like 'back to normal' in the developed world, the same was not true everywhere else, with households, businesses and financial institutions all suffering. A bit over a year on, it's difficult to know what to make of that situation. In Europe, there's often little visual evidence of the pandemic, but its effects - on supply chains, on staffing, on travel and of course on inflation, remains significant. And there are new economic and geopolitical storms gathering as well. All these uncertainties are even more profound for the stakeholders in the financial inclusion sector working in low-income countries.

The *Financial Inclusion Compass 2022* comes out soon after the latest (but delayed) Global Findex, 60 Decibels' Microfinance Index and other studies that together provide insights into different parts and perspectives of the financial inclusion sector. e-MFP believes that giving a range of sector stakeholders the opportunity to evaluate curated lists of selected trends and new priority areas and then share their own observations is of real and enduring value. It also means that putting this paper together requires honesty and impartiality. e-MFP sees its job to report, as best as it can, on what the sector currently thinks - no more, no less. In this, we are rapporteurs. It's a job that has become more complex each year since the series launched in 2018.

Once again, the results are intriguing. On behalf of my colleagues, I'd like to thank the survey respondents for generously giving their time to participate, and for providing such extensive and rich insights in doing so. Obviously, this project would not be possible without their time and expertise.

And I would also like to thank the entire e-MFP team - Camille Dassy, Fernando Naranjo, Daniel Rozas, Joana Silva Afonso, and Niamh Watters - who supported *Compass* project lead Sam Mendelson in the task of running this survey and pulling together the many thousands of words from survey respondents into a paper which, we hope, continues to provide valuable insight to those working in financial inclusion.

Christoph Pausch
Executive Secretary
European Microfinance Platform

Introduction

"The future has already happened.
It just isn't very well distributed"

William Gibson

Doesn't the present – the *current* present – feel uneasy and surreal? There has been a shared global experience which has left behind a sort of conceptual break with the past, which makes that past – the *past's* present – seem naïve, and the future daunting and more uncertain than ever.

Re-reading the 2019 *Compass* is to peer backwards into that past present, of a sector with contributions from respondents (and an author) who had no idea of the scale of what was coming. The introduction says, "*we hope that in years to come, this will serve as a time capsule from the past*". It does so, already.

Some of the challenges and opportunities described by respondents in that paper endure. Client protection remains under threat from the relentlessness of digitalisation; agri-finance and SME finance are among the focus areas of the future. And the "*collective soul-searching for financial inclusion's purpose*", an overarching theme in 2019, remains germane, but perhaps one of the outcomes of Covid is the emergence of an answer to that question of *purpose*: financial inclusion is at its core about resilience – of clients, certainly, but also of institutions and of investors in the face of risk.

The *Financial Inclusion Compass 2022* isn't about Covid *per se,* but the pandemic looms over much. The process of recovery – the pivot back to some 'normality' – is beginning, but there are scars everywhere we look. In the developed world, inflation, supply chain and staffing issues and the collapse in logistics systems is a reminder of the shock to the economies this all involved. In low-income countries the challenges go far beyond inconveniences; there may be a 'perfect storm' coming – how many households have been pushed back into poverty in the last couple of years? And how many, faced with runaway inflation that central banks cannot control, and food insecurity exacerbated by geopolitical events, have that future ahead of them?

This makes it difficult to know what to make of where the sector is today. As Christoph Pausch notes in the foreword, this *Compass* comes on the back of the recently published Global Findex 2021. That report shows much of which to be proud: account ownership is up, the gender gap in account ownership is narrowing, the share of adults making or receiving digital payments has even outpaced growth in account ownership.

But Gibson's epigram about the future being here, but not well distributed, has never been truer. There are many challenges ahead – perhaps deeper and broader than ever before. Collaboration between stakeholders was crucial during the pandemic, but can it endure? Is there space for innovation if an acute crisis is replaced by a chronic one?

This *Compass* is a bit different than previous editions. It's shorter, and there are new trends and future focus areas introduced – among them food security, financial health, strategic responses to climate change, machine learning and blockchain, and mainstreaming gender equity. Once more, we ask for respondents' thoughts on challenges and opportunities ahead.

As ever, my colleagues and I are struck by the richness and variety of insights from those who participate in this survey. Picking what to include and where in this paper, while sticking to reporting and not editorialising, never gets easier. I'm enormously grateful to everyone who helped, and we at e-MFP hope that the contributions within it provide tangible value to the financial inclusion sector.

Sam Mendelson
Financial Inclusion Specialist
European Microfinance Platform
September 2022

Executive Summary

The *Financial Inclusion Compass 2022* is the fifth in the annual series. It included a mandatory, quantitative part I – split into **Trends** and **Future Priority Areas** (both sections with space for optional qualitative comments) – and an optional part II with **three open-ended questions**.

This year there were some new trends and future focus areas introduced, including food security, financial health, strategic responses to climate change, machine learning and blockchain, and mainstreaming gender equity.

There were 112 *complete* responses to the survey, from 46 countries. There was a record representation of FSPs (41%), and an increase in researchers (12%). There was a smaller proportion of consultants (24%), funders (11%) and infrastructure organisations (10%) compared to 2021.

Top 5 Trends

Current Importance of Financial Inclusion Trends

1. **Expansion of digital transformation (institutional-side)**
2. **Expansion of digital innovations (client-side)**
3. **Strengthening of client resilience**
4. **Innovation in financial product development**
5. **Development of client protection**

Among the list of 20 trends, **Digital transformation** is back in 1st place, after sliding down to 5th last year, when the new entrant **Strengthening of client resilience** was rated most important by respondents. This year it stays in the top three - as does **Expansion of client-side digital innovations**. There are rises up the rankings for **Innovation in financial product development** and **Development of client protection**, and there are three new entrants in the top 10.

There are significant differences between respondent groups:

- **Expansion of digital transformation (institutional-side)**, while 1st overall, is only the 7th highest score among Infrastructure Organisations, and only 9th among Researchers. It holds top spot largely through its very high importance for FSPs.
- **Expansion of digital innovations (client-side)** is 2nd overall, but only 9th among infrastructure organisations, perhaps reflecting a growing scepticism among FSP networks, observers and commentators that low-touch models can meet clients' real needs.
- **Innovation in financial product development**, 4th overall, is only in 11th place among Consultants and Support Service Providers, and 10th among Infrastructure Organisations. The many FSPs put it in 2nd - enough to pull it to its high overall position.
- **Increasing social/environmental and/or impact measurement and reporting** is only 10th among FSPs, versus 5th overall. It is ranked 1st among funders.

- **Development of non-financial services** is only 13th overall, but 6th among FSPs. This is a huge change - they rated it only in 17th place in 2021.
- **Increase in new categories of financial service provider** is rated much higher among funders than the overall respondents who put it in 14th place. FSPs themselves rank it almost bottom.
- **Support of HR and institutional capacity development** is rated much more important by FSPs (7th) than the overall group (16th), a revealing difference as FSPs are those with most of the experience and responsibility in this field, and who largely bear the costs of turnover and recruitment training. They had this only in 15th spot in 2021.

Top 5 Priority Areas

Respondents' Medium-Term 'Future Priority Areas'

1	2	3	4	5
Small and medium enterprise (SME) finance	**Agri-finance**	**Green and climate-smart finance**	**Women's empowerment and gender equality**	**Financial inclusion for the very poor**

Overall, the top three (from the list of 16) stays the same as for the last three years – although in a different order. Green and climate-smart finance continue (re-framed from **Change adaptation/mitigation** in 2021) continues its high priority for respondents, something reflected in the qualitative sections as well. **Women's empowerment and gender equality** is in an effective tie for 3rd place, with two new entrants (**Financial inclusion for the very poor** and **Food security**) both in the top six.

As with the trends, there are clear differences between respondent groups.

- **SME Finance** was clear top among all respondents, strongly influenced by Consultants and Support Service Providers.
- Consultants rated **Food security** very low, but they put **Services for refugees/displaced persons** higher than respondents overall.
- Financial Service Providers were the only respondent group to rate **Water, sanitation and hygiene (WASH)** anywhere above the lowest rank. Funders have almost no interest in WASH at all (although they are very keen to see significant developments in **Disaster resilience)**.
- Infrastructure organisation respondents are the group most interested in **Green and climate smart finance** and **Food security**. By contrast, they have low interest compared to other respondent groups in **Financial inclusion for the very poor.**
- However, researchers (outliers, always) gave **Financial inclusion for the very poor** the highest of any group for any area, but gave low priority to **Green and climate-smart finance** (which otherwise would have been in 2nd spot overall). Researchers also have high interest in **Financial literacy** and **Food security**.

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The following are some selected messages from the qualitative responses to the three final questions:

Challenges facing the financial inclusion sector today

- Always perceived as a twin challenge and opportunity, the **digitalisation** of the sector is seen as having been catalysed by the pandemic, both **accelerating innovation but exacerbating risks as well**. The sector must address barriers of fear and distrust still widespread among some clients and strengthen their digital capabilities and skills to change the culture of using cash for digital money and the adoption of digital applications.
- Financial institutions must take up the challenge of transforming their customers into their own bankers by allowing them to carry out their operations 24/7 without having to travel. To do so, they will have to find ways to invest in **technological tools** and **support research** in the areas of technological innovation.
- But a **supply-side response, while necessary, is not sufficient** – top-down innovation must be matched with bottom-up preparedness and support. This must include financial education so that clients can make the best use of all the products that have been created. Training in financial education is critical to avoiding over-indebtedness, something increasingly relevant as the upheavals and financial stresses of the pandemic on low-income households are still not fully understood.
- **The Covid-19 pandemic** looms large among respondents' concerns. The recovery is non-linear and uneven, and there are real concerns that there is increased vulnerability among poorer segments, and that FSPs are choosing not to serve them (because of their own vulnerabilities and sustainability challenges), becoming more and more risk averse.
- The pandemic has had an outsized adverse impact on **women**. Redressing this downturn while seeking to re-establishing momentum in what was a longer-term positive trend towards **gender inclusion**, equity, and institutional mainstreaming, is an immense challenge.
- For FSPs, a major challenge is **growing and burdensome reporting requirements**, with the unintended consequence of reducing outreach by smaller and more socially focused providers. But it's not just Tier 2/3 MFIs that are affected; this is a much broader challenge. Indeed, regulatory trends such as SFDR in Europe may place an increased burden on the whole industry.
- **Client protection continues to dominate attention of respondents, who ask** how can the sector protect clients from unscrupulous new entrants, from fraud, or privacy invasions, and how can sector stakeholders ever juggle their claimed social mission with the need to grow and consolidate; somehow keeping existing funders and enticing new ones; and welcoming new actors without making traditional providers obsolete?
- **Global risk and uncertainty** are increasing rapidly. The pandemic has been the ultimate **transversal challenge** – with knock-on effects on human resources, client protection, supply chain challenges and household debt, and its inflationary effect on food and fuel prices. The increase in negative externalities affects economic growth, and in turn affects the confidence, outlook, and strategic freedom for providers.

> "Increased costs in fuel and food for our clients leading to increased hardship. We will need to be more aware of over indebtedness and unforeseen outcomes for our clients"

CFO of Microfinance Bank

- The most significant new addition to this list of risks, however, is not a single challenge but a **group of densely related issues caused by geopolitical and macroeconomic shocks**. The supply chain and food security challenges in an already-inflationary environment have been rapidly accelerated by **Russia's invasion of Ukraine**, leading to what many respondents think of as a perfect storm: a cost-of-living crisis combined with **food insecurity** right on the back of an unprecedented public health, economic, financial, and mental health shock.

- The **challenges are more diverse and complex and interdependent than ever**. There are some clear externalities - the pandemic and its recovery; the Ukraine war – and longer-term internalities as well, fundamental trade-offs on what financial inclusion means, for whom, and how, that will require hitherto untapped levels of collaboration to respond.

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Biggest opportunities ahead…

- **Digital finance** is widely seen as the common thread between many positive outcomes. Respondents give examples of reductions in information asymmetries, agent banking, incorporation of fintechs, rural spread of connectivity, human resources management and support to small entrepreneurs as among the ways digital finance can be such an opportunity. But they are clear as well, that all these lofty goals only work if technology is seen as a **means and not the end**; a tool for inclusion not a goal in itself.

"Increasing connectivity, big data, digital channels and procedures - if applied with responsibility, then this should be a large opportunity"

TA Provider

- **Green and climate-smart finance** continues to be seen as a real opportunity (despite it being a response to what is acknowledged as an immense challenge. Green finance is a way to educate customers on best practices in environmental care, and there's a chance to build **climate-smart financial inclusion strategies that improve resilience of end-clients** towards climate change and help them develop climate adaptation strategies.

- There are opportunities too in **stakeholders' understanding of clients' lives and needs,** and the segmentation of clients that helps develop solutions to meet those needs. Understanding clients better has knock-on effects, too – especially when combined with **demand-driven digital innovations** – from contactless financial services to delivery of financial literacy.

- Some respondents argue that the largest group of beneficiaries when these opportunities are taken is **women**; but only if the leveraging of digital technologies is done to bring **benefits to all segments in a gender-inclusive way** rather than adding more layers of barriers to the financial inclusion ecosystem. Addressing bias in data is one big issue to tackle in addition to gender inequities in relation to digital literacy as well as access to mobile and digital infrastructure.

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Changes in sector-wide infrastructure

- There is concern that, whatever the new initiatives being launched, the disappearance of some of the more venerable entities risks a **vacuum of leadership and guidance.** This includes *confusion in the sector*, a degradation of institutional memory, and the loss of SEEP of particular concern and sadness to many respondents.

- Yet not all news is bad news, and some respondents are phlegmatic, pointing to the natural cycles of **creative destruction within any sector or industry.** These organisations' roles are often framed as collaborative or even collegiate, with their sharing of ultimate objectives – inclusion, access, poverty alleviation, literacy, etc. But the truth is, infrastructure organisations are **competitors** – for projects, talent, funding, and influence. In this sense, according to some respondents, it is natural that there should be attrition and churn.

"There is a time and season for all initiatives. However, it is key that we fight the tendency to discard old initiatives, but rather, new initiatives should build on what were, once, new initiatives themselves"

Director at global network of FSPs

- Specifically, there is now a **better understanding** of how to improve **client protection** and the customer experience, and the end of the Smart Campaign and its quasi-reincorporation via the CP Pathway is seen by some as positive – even an improvement.
- This positive outlook based on the **natural evolution of the sector** is a widely repeated theme, and among the respondent group really drowns out any hand-wringing over the disappearance of certain entities.
- But that's not to say there aren't risks. **Continuity** must be ensured to guarantee that progress isn't lost or that there is regression in client protection and SPM in particular. This is especially true considering the impact of Covid on clients and the general acceleration of digitalisation it brought about. And some respondents believe it'll be critical that the new players must **prevent the continued expansion of reporting burdens on FSPs.**

Background & Methodology

The *Financial Inclusion Compass 2022* is the fifth in the annual series and continues with a mixed-methodology structure including a mandatory, quantitative part I – split into Trends and Future Priority Areas (both sections with space for optional qualitative comments) – and an optional part II with three open-ended questions.

The survey (and this publication) continues to evolve. Certain questions stay each year, others will come and go periodically. To balance the goal of useful year-to-year tracking of trends with ensuring they are maximally relevant to a changing context, there are some other changes this year. Based on feedback from previous years and conversations with e-MFP members and other sector stakeholders, some old trends and future priority areas have made way for new ones.

As before, respondents were required to provide all their personal and organisation details, but to ensure the *Financial Inclusion Compass* remains useful and of manageable length, it was decided to keep all included respondent quotes unattributed, except in cases where the type of respondent making the quote is of great significance.

Finally, the survey, which was open for four weeks in early summer 2022, was available in English, Spanish and French.

Survey Respondents

There were 112 *complete* responses to the survey, from 46 countries – a slightly smaller but much more geographically diverse respondent group than in 2021. The top fifteen countries in terms of **respondent location** are France, the Philippines, India, Ecuador, USA, UK, Uganda, Peru, Netherlands, Luxembourg, Italy, Spain, Nepal, Ethiopia, and Bangladesh.

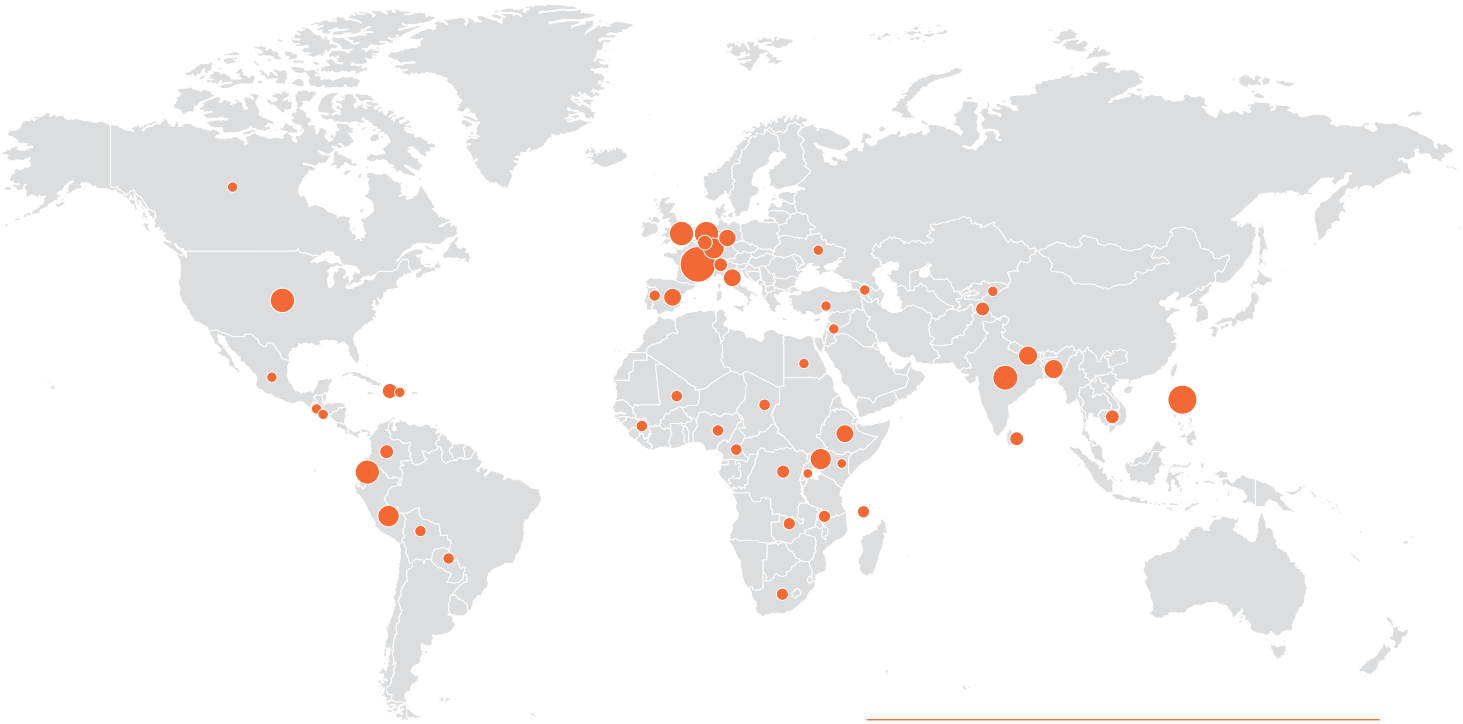


Figure 1

Location of *Compass* Respondents

Respondents were asked to provide their predominant geographical focus of work – however with a significant difference from previous years, which offered a single choice answer, and a plurality for the general (and not very useful) term 'global'. This year, respondents could select multiple options, which resulted in a more revealing insight into the geographical focus on their work. The distribution of respondents can be seen in Figure 2.

Respondents were once again asked to give the type of organisation they work for, both as a high-level category (FSP, funder, etc) and then within sub-lists (microfinance bank, think-tank, MIV Manager, etc). 'Infrastructure organisation' was used as an umbrella name for local or regional associations, or networks, regulators, credit bureaus or supranational organisations.

The distribution of respondents by organisation type (and sub-type) can be seen in Figure 3. There was a record representation of FSPs (41%), and an increase in researchers (12%). There was a smaller proportion of consultants (24%), funders (11%) and infrastructure organisations (10%) compared to 2021.

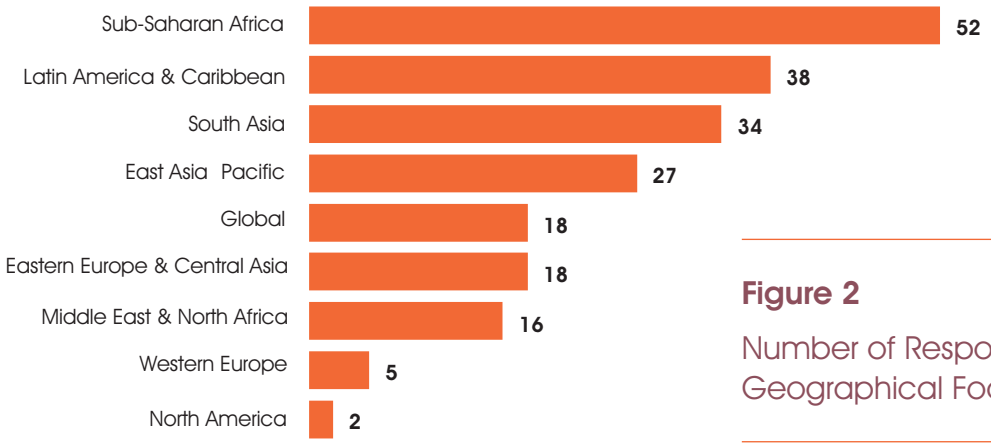


Figure 2

Number of Respondents by Geographical Focus of Work

Figure 3

Respondents by Type of Organisation (%)

The *Compass* Trends

Please look at the following list of trends that financial inclusion stakeholders may be experiencing, and give each one a score between 1 and 10 corresponding to their importance in the financial inclusion sector today.

"There are two kinds of forecasters: those who don't know, and those who don't know they don't know."

John Kenneth Galbraith

Figure 4

Importance of Present Trends - Overall Rankings

Rank	Trend	Score	2021
1	Expansion of digital transformation (institutional-side)	8.08	5
2	Expansion of digital innovations (client-side)	8.04	3
3	Strengthening of client resilience	7.97	1
4	Innovation in financial product development	7.71	6
5	Development of client protection	7.64	7
6	Increasing social/environmental and/or impact measurement and reporting	7.64	NEW
7	Emerging focus on clients' financial health	7.48	NEW
8	Acceleration of strategic responses to the effects of climate change	7.37	NEW
9	Promotion of good governance	7.34	10
10	Building institutional and sector-wide resilience	7.26	8
11	Mainstreaming gender equity within financial inclusion organisations	7.06	NEW
12	Innovation in financial inclusion regulation	6.97	11
13	Development of non-financial services	6.89	14
14	Increase in new categories of financial service provider (fintechs, consumer lenders, banks downscaling, etc.)	6.77	17
15	Development of new outreach/marketing channels (e.g. agents)	6.74	13
16	Support of HR and institutional capacity development	6.72	15
17	Improved availability and usage of institutional and market-level information (ratings, credit bureau data, etc.)	6.54	16
18	Increase in the relevance of financial inclusion research	6.45	20
19	Increase in new financial technologies and platforms (machine learning, cryptocurrencies, blockchain, etc.)	6.42	NEW
20	Entry of new investors and/or new investment vehicles	6.13	18

Responses by Geographical Focus of Work and Respondent Type

As always, respondents' assessments of the trends' importance varied significantly based both on the geographical focus of their work, and the role they or their organisation plays in financial inclusion. Figure 5 shows the Top 5 trends among the five main categories of respondents.

Figure 5

Top 5 Trends by Respondent Category

Consultants & Support Service Providers

1	Expansion of digital innovations (client-side)
2	Expansion of digital transformation (institutional-side)
3	Strengthening of client resilience
4	Increasing social/environmental and/or impact measurement and reporting
5	Development of client protection

Infrastructure Organisations

1	Strengthening of client resilience
2	Acceleration of strategic responses to the effects of climate change
3	Innovation in financial inclusion regulation
4	Increasing social/environmental and/or impact measurement and reporting
5	Promotion of good governance

Financial Service Providers

1	Expansion of digital transformation (institutional-side)
2	Innovation in financial product development
3	Expansion of digital innovations (client-side)
4	Strengthening of client resilience
5	Development of client protection

Researchers

1	Innovation in financial product development
2	Expansion of digital innovations (client-side)
3	Increase in the relevance of financial inclusion research
4	Strengthening of client resilience
5	Emerging focus on clients' financial health

Funders

1	Increasing social/environmental and/or impact measurement and reporting
2	Acceleration of strategic responses to the effects of climate change
3	Expansion of digital transformation (institutional-side)
4	Expansion of digital innovations (client-side)
5	Strengthening of client resilience

Figure 5 on page 17 compares the top five trends by category of respondent. However, there are other significant differences in how these respondent groups perceive the importance of trends.

- **Expansion of digital transformation (institutional-side)**, while 1st overall, is only the 7th highest score among Infrastructure Organisations, and only 9th among Researchers. It holds top spot largely through its very high importance for FSPs, suggesting that wherever their hesitance before the pandemic, 'digitize or die' is now a widespread mantra.
- **Expansion of digital innovations (client-side)** is 2nd overall, but only 9th among infrastructure organisations, perhaps reflecting a growing scepticism among FSP networks, observers and commentators (and definitely seen among the comments) that low-touch models can meet clients' needs.
- **Innovation in financial product development**, 4th overall, is only in 11th place among Consultants and Support Service Providers, and 10th among Infrastructure Organisations. The large respondent group of FSPs rate it in 2nd spot - enough to pull it to its high overall position.
- **Increasing social/environmental and/or impact measurement and reporting** is only 10th among FSPs, versus 5th overall. It is ranked 1st among funders, perhaps unsurprising since it is they who increasingly demand this data, and this is borne out by the comments as well.
- **Development of non-financial services** is only 13th overall, but 6th among FSPs, an interesting outcome considering they rated it only in 17th place in 2021.
- **Increase in new categories of financial service provider** is rated much higher among funders than the overall respondents who put it in 14th place. Curiously, FSPs themselves rank it almost bottom in 18th place, despite traditional FSPs being the most at risk from this trend.
- **Innovation in financial inclusion regulation** is only 12th overall, but rated very high – in 3rd place – by infrastructure organisations. They had it in 10th spot in 2021; what has changed?
- **Support of HR and institutional capacity development** is rated much more important by FSPs (7th) than the overall group (16th), a revealing difference as FSPs are those with most of the experience and responsibility in this field, and who largely bear the costs of turnover and recruitment training. Notably, FSPs had this only in 15th spot in 2021.
- Once again, **Increase in the relevance of financial inclusion research** is considered a trend of lowly importance overall – except unsurprisingly by researchers themselves, who place it in 3rd spot.
- **Researchers are generally an outlier group**, perceiving trends on governance, sector wide resilience and mainstreaming of gender equity all lower than respondents overall, but rating non-financial services and new technologies much higher.

The Top Ten *Compass* Trends What Respondents Wrote

1. Expansion of digital transformation (institutional side)

After a dip to 5th place in 2021, Expansion of institutional-side digital transformation is back in top spot again. Digital transformation is a broad term, an umbrella covering a growing range of technological innovations that improve efficiency, reduce costs, improve understanding of current and potential clients' needs and situations, and in theory at least, improve services and outreach to vulnerable groups. As a trend, therefore, it overlaps with other trends such as new categories of financial provider, new financial technologies, new outreach channels and product development.

What seems clear from respondents is that digital transformation has been catalysed by the pandemic, and is no longer a value-add, but a critical precondition to survival. Progress among MFIs is naturally uneven. It is an "*inevitable*" trend, writes a TA provider, and one *"that will seriously impact FSPs, particularly local grassroot institutions with lower capability to keep on track with technological changes".* It's "*a real need, those who postpone this trend will be left behind*", writes an FSP. It is "*important for MFIs to be able to keep up with new competition – and lower costs*", writes another respondent. It comprises opportunities beyond costs and outreach: *"Financial institutions and investors should leverage the digital transformation to include additional data on climate risk and green opportunities, in their process, products and activities"*, writes a researcher.

And there are considerable skill gaps to be filled to ensure the potential is reached. A funder writes that *"digitalization has indeed accelerated since the onset of the pandemic and this trend remains. As most FSPs have now embarked the digitalization train, we still observe very various degrees of digitalization progress and integration into the investment process"* adding that *"further skills need to be built on digital risk management, cyber security, client data protection, data management, credit algorithm, etc."*

> "Digital transformation is not a choice anymore … it is a necessity, with Covid providing the impetus"
>
> Consultant and TA Provider

2. Expansion of digital innovations (client side)

Staying in the top three as it has every year, Expansion of client-side digital innovations is in close second place this time. Yet in their comments, respondents tend to be much more equivocal than before. Has the pandemic shown the limitations of remote, low-touch and branchless models?

"*Results can be both positive and negative and depend on the FSPs' capability to make these innovations work for all types of clients*", writes one respondent. A funder observes that *"it is interesting how persistent bricks and mortar models are in microfinance - despite the COVID pandemic".* "*Digitalization and human values must go together*", cautions the head of an MFI. There's "*a lot of hype*", according to a funder, "*but bottom of the pyramid clients are also digitally excluded, so FSPs have to retain traditional face-to-face services*". After all, "*customers want to be served in a timely and efficient manner, not necessarily through digital innovations*, writes an FSP respondent.

There's also an opportunity cost inherent in digital innovation. "*Whatever donor funding is available under tight conditions tends to go to technology related areas rather than other even more important areas*", complains a financial services provider. Whatever digital innovations are yet to come, they need to actually address challenges, not respond to the vagaries of whatever is new, cool, and exciting. Digital innovation should mean "*not just shiny new things, but better designed digital tools*", says a consultant.

"Faster technological innovations are creating more and more 'modern illiterates' in our traditional societies, which is an additional cost for this education and the availability of technology requires huge financial means from both institutions and clients"

Financial Services Provider

3. Strengthening of client resilience

Strengthening of client resilience was a new entrant in 2021, a response to the clear sense from the special edition *Covid-19 Compass* that this would be of the highest importance to respondents. This sense was vindicated – it was in top place last year. This time it has edged down to 3rd spot as pre-pandemic reality slowly resumes, but it's clear from respondents' comments that the lessons have been learned; protecting vulnerable clients is every bit as important as empowering or including them.

It has many components. It is a primary goal: *"financial inclusion is not an end objective but a key means to achieving client resilience"*, writes one respondent. It's "*one of the main goals of the sector and will continue to be as challenges increase for the poorest segments across the world"*, writes another. It is "*vital for FSPs*", and "*should dictate product development*", claims a funder. It should be viewed expansively, too: "*apart from merely developing coping strategies, it's needed to develop adaptation strategies",* writes a consultant. And it's serious because the job is very far from done: "*Support for clients' resilience is also low. i.e low attention to offer flexible loan products, and very low attention to saving and insurance"*, according to a TA provider.

What's to be done? According to a funder, there needs to be *"continued support of clients and responsible lending practices aiming at preventing over-indebtedness". The "more financial education [clients] have, the more resilient they will be"*, writes an FSP. But identifying its importance is the easy part; necessary – but not sufficient: *"It is not easy to come up with good interventions, other than training*!" writes a consultant.

"Resilience goes hand in hand with health"

Researcher

4. Innovation in financial product development

This remains a highly-ranked trend – consistent, but with qualitative responses that, unlike some other trends, place it more on the 'important' than the 'urgent' side of the ledger. After all, innovating in financial product development is really a core part of any successful financial provider. It is, as a TA provider points out, a "*sort of 'cross-cutting' topic – green finance, SME finance, agri-finance"* that would mainly benefit from *"more interest in human-centred design*". There are certain areas where there is a dearth of innovation: "*I don't see much happening, especially in Muslim majority contexts there is still a lack of Sharia-compliant products leading to continuing financial exclusion"*, writes a funder. The trouble is that

product development seldom happens because of an external shock that forces adaptation, but needs long-term thinking, strategic planning and investment. This means inertia, and "*with few options, most clients take whatever is available in the market*", writes a support service provider. Put another way, "*a microfinance institution can survive for a long time with its current products, especially with group lending methodologies*", writes a respondent from an infrastructure organisation.

Development also doesn't need to mean revolution; often evolution is enough. "*It doesn't have to be something new, but better designed, more flexible*", writes a consultant. But there are areas ripe for innovation. A funder writes "*I'm very interested in what we call MFI+ models (micro asset leasing, SME financing, value chain financing) and think these will be significant in the future*". As long as product development isn't just synonymous with digital financial services: product development must work for those clients "*not well equipped to use smartphones*", writes a researcher.

"Innovation in product development is crucial as the excluded population has varied financial needs and cannot be seen through one lens alone"

Consultant and Support Service Provider

5. Development of client protection

Client protection has dominated commentary in every *Compass* - and this year is no different. Among respondents, there is a general sense of trepidation, that the investment and efforts made over the years might be eroded, both because of chronic and long-term trends (new entrants forcing traditional providers to move up-market and neglect low-income groups), newer emerging trends (data privacy), and the re-ordering of some sector-wide infrastructure (see p. 38).

For some respondents, it's a case of 'nothing to see here' – the important work has been done. "*Increasingly informed customers enable them to avoid abuses of position*", writes one respondent. "*It is developed! Tested! Retested and improved!*" writes another. *"We now need to globalise implementation and uptake!"* it's just "*more a matter of implementing than developing*", writes a TA provider.

But there's no doubt that there are new concerns, which suggest that, for many respondents, more is at stake than turning development into implementation. According to one, it's "*one of the main trends in the sector that has been made more relevant during the Covid-19 pandemic and in face of recent less positive media news on the sector".* The closure of the Smart Campaign and the launch of the Client Protection Pathway is noted by several as a critical juncture for the sector, with the full implications as yet unclear. A funder that contributed to the design of the new CPP certification notes the fallout of recent negative press and makes a promise*: "We shall not lower our guard and will continue applying the highest standards of client protection and ensure the smooth transition to new CP Pathway. We should make sure that this transition to a new model doesn't mean lower standards being applied".*

"[Client protection] is a sine qua non condition to balance the table in such a way that microfinance clients are more knowledgeable, and the knowledge inequality gap is narrowed"

Financial Services Provider

Selected Comments from the other Trends

Increasing social/environmental and/or impact measurement and reporting

ESMS is high on donors and investors' agenda, but I see quite a gap between the high-level aspirations and the execution

Consultant and Support Service Provider

This only happens if it is required by regulation or institutional investor

Financial Services Provider

Impact measurement's methodological issues are not resolved. Conceptually, how do you define poverty, and women's empowerment?

TA Provider

Emerging focus on clients' financial health

A lot of work needs to be done for the concept to be clear to a broad audience. Several components of financial health are reflected in other trends in the list

Infrastructure Organisation

This is an issue of good measurement of clients' ability to pay. If it refers to training and providing tools for clients to manage their finances well, the importance is very high

Infrastructure Organisation

Systemic shocks such as Covid have shown that if FSPs are not focusing on their clients' financial health, their own financial performance will suffer

Funder

Wasn't that why microfinance was needed in the first place?

Researcher

Acceleration of strategic responses to the effects of Climate Change

Clients of MFIs are among the most vulnerable sectors to climate change. Strategic response at sector level should be developed and implemented with short term benefit and long-term vision. Climate resiliency should be part of the key focus of financial inclusion for vulnerable and poor populations as well as MSMEs. Without generating sustainable resiliency socio-economic and financial inclusion will become more and more complex under the pressure of climate change

Researcher and Consultant

The topic is high on donors' agenda; I am yet to see 'strategic' moves (a lot of the initiatives, it seems to me, just attach 'green' to the usual TA-formats)

Consultant and Support Service Provider

Most FSPs lack scale or are too operationally focused for such strategic responses

Funder

This is important but the significance is not evenly distributed globally

Financial Services Provider

Promotion of good governance

Seems to have taken a backseat... there has been quite some progress, so maybe it is mainstream now

Consultant and Support Service Provider

Best corporate governance practice remains key to support a sustainable FI sector as it strengthens institutional financial performance and credit risk profile and reinforces trust with institutional stakeholders. Trust is key to ensure stability and sustainability, in good and bad times

Funder

Yes - as good governance should now also mean: to tackle the climate change issue and adopt measure in order for each organisation to be more virtuous and to support its clients

Financial Services Provider

Building institutional and sector wide resilience

Financial service providers have proven to be much more resilient to the pandemic and subsequent economic crisis. Yet the global spillover effects of the war in Ukraine may stress further some of the institutions that have been already awakened by several years of uncertainty, through a combination of shocks on global food security, global growth, inflation. Building institutional capabilities, replenishing solvency buffers and resilience remains critical to progress on financial inclusion

Funder

The current worldwide economic situation has emerged the importance of institutional and sector-wide resilience

Financial Services Provider

We have entered in a period of continued, long-term crisis - as we can see already

Infrastructure Organisation

Mainstreaming gender equity within financial inclusion organisations

The issue of gender equity is very important, but it should not be a condition for financial inclusion by seeking to impose it

Infrastructure Organisation

We have noted the proportion of women in our portfolio has been in decline in recent years. Clearly gender equity needs to be a key focus, particularly given climate change and COVID impacts, so interested in where this trend is emerging from

Funder

Many institutions do not offer tailored products. The main product remains micro-credit, but with no gender mainstreaming exercise (e.g. analysing potential implication of the new loan-financed business on women's time, or integrating business support, etc. Financial services (especially the group system) also offer an opportunity to introduce "gender transformative" approaches but very little is done to up-scale them

Consultant and Support Service Provider

Innovation in financial inclusion regulation

Often the regulatory sector impedes private sector development

Financial Services Provider

Regulation should address both access and use

Infrastructure Organisation

Financial inclusion regulation can continue to strengthen its client protection approach by expanding definition to household protection (concerns of negative unintended consequences, e.g. child labor, experienced by other household members)

Consultant and Support Service Provider

Regulation should support the transition toward a more climate and ecosystems resilient sector with higher positive impacts on most vulnerable populations and ecosystems. Support should be provided to manage physical and transition risks for financial intermediaries and investors, as well as to define what are the most suitable green practices and technologies financeable for the inclusive finance sector

Infrastructure Organisation

Regulation must go hand in hand with technological advances and customer needs, especially in terms of making rules more flexible.

Financial Services Provider

Development of non-financial services

Who should be leading these efforts if FSPs partner with other organisations, and/or to what extent is this the role of FSPs on their own?

Infrastructure Organisation

Very important although we notice less prominence is given to this in investment dossiers than we used to see (are MFIs becoming less anxious to showcase this to investors or is it a change in analyst practices?)

Funder

MFIs should be left to focus on their core competence - financial services for financial inclusion - rather than asking them to spread thin by doing everything. There are other stakeholders like NGOs or advocacy groups which can take up this

Consultant and Support Service Provider

Increase in new categories of financial services provider

This is an issue of great interest to be alert to for the protection of clients and to prevent or avoid over-indebtedness

Financial Services Provider

Financial landscape has changed already; many MFIs are too late

Researcher

Multiple financial services providers create unhealthy competition and none of the organisations would work effectively. So, putting all efforts in one basket will create more synergistic effect

Financial Services Provider

We observe the emergence of several new players, many of them are deemed yet 'immature' and still need to prove their business model (becoming sustainable) and create added value to the end customers

Funder

Development of new outreach/marketing channels

Linked to the digital transformation of the FSPs, without which is difficult to think how these new distribution channels can be managed

Infrastructure Organisation

To the extent that it assists greater inclusion in an appropriate and competitive manner, it is welcome

Financial Services Provider

We should be strengthening the existing network

Financial Services Provider

There indeed is great potential in using agents to reach out the majority. These agents could enhance outreach through front-line services to the poor in a decentralized scheme...Good orientation to serve poor clients will remain a key challenge

Consultant and Support Service Provider

Support of HR and institutional capacity development

Those investing in this field are rare

Financial Services Provider

Some institutions still don't get it right especially when innovative solutions have been deployed, staff are chasing KPIs and are deaf to what is going on around them

Consultant and Support Service Provider

The mainstreaming of ESG / Sustainability will (and already does) provide a big incentive for staff in our sector to switch to the private sector, that now has to provide social and environmental value in addition to pure profits, with often better pay and packages

Infrastructure Organisation

Improved availability and usage of institutional and market level information

This is a strength that has been capitalised on for several years and is constantly being maintained and strengthened

Financial Services Provider

Ratings are not making much impact except to institutional lenders

Financial Services Provider

As much transparent information as possible is imperative for sound portfolio management

Financial Services Provider

There are efforts to establish offices like credit bureaus organised under the Central bank... The issue is that Financial Institutions are not pro-actively taking part in such a system

Consultant and Support Service Provider

Increase in the relevance of financial inclusion research

It should be a more important trend in the sector, but it isn't. Academic research can bring an independent and different perspective on the sector's main topics and can explore topics that are not necessarily a priority to practitioners providing, when of good quality, unique insights to managers and policy makers. Academic and practitioner research should be complementary

Infrastructure Organisation

Not many take this seriously

Financial Services Provider

The academy is key to financial education, which is where the knowledge of the new generations of microfinance managers comes from

Financial Services Provider

We see a growing interest in benchmarking studies in the sector, with the recent launch of the Impact Performance Benchmark by the GIIN and the ATLAS platform for instance

Funder

Increase in new financial technologies and platforms (machine learning, cryptocurrencies, blockchain, etc.)

I would not take "cryptocurrencies" into consideration, whereas blockchain and machine learning could be of help

Financial Services Provider

A seriously emerging trend

Financial Services Provider

To compete with developed countries, it is essential

Financial Services Provider

There is still a lot of mistrust and/or ignorance on these issues

Infrastructure Organisation

Entry of new investors and/or new investment vehicles

Private social investors will become more relevant

Researcher

The greater the supply of funding, the greater the capacity for growth and coverage of adequate financial services

Financial Services Provider

Entry of new investors is required to turbocharge funding to the existing and new financial institutions. Also, for digital transformation, there is a requirement of new funding sources

Consultant and Support Service Provider

Future Priority Areas

In which of the following areas would you like to see the most significant developments in how the financial inclusion sector serves low-income clients in the next 5-10 years?

"You can achieve anything, but not everything."

Amit Kalantri

This year, the New Areas of Focus Index from previous *Compass* editions goes by a new moniker, to better reflect that it looks beyond current and imminent areas of development to the longer-term. And it framed more individually as well, asking not just what respondents forecast (i.e. what they think others think) but what *they themselves would like to see.* As before, this list continues to evolve, with new areas coming in, and others being removed – and a couple being amended to better reflect realities. Again, respondents

Overall Rankings

Figure 7

Future Priority Areas – Overall Rankings

Rank	Future Priority Areas	Index score	2021 rank
1	Small and medium enterprise (SME) finance	36.3	1
2	Agri-finance	31.6	3
3	Green and climate-smart finance	30.6	2*
4	Women's empowerment and gender equality	29.7	6*
5	Financial inclusion for the very poor	28.4	NEW
6	Food security	21.8	NEW
7	Financial literacy (incl. digital literacy)	21.2	4
8	Access to health care	15.8	9
9	Disaster resilience	14.7	12
10	Water, sanitation and hygiene (WASH)	13.7	11
11	Access to education	13.2	7
12	Financial inclusion for young people	12.4	8
13	Access to housing	10.5	13
14	Services for refugees/displaced populations	8.6	10
15	Financial inclusion for the elderly	6.2	NEW
16	Access to energy	5.3	15

* Formerly Climate change adapation/mitigation, and Services for Women

were asked to choose their top five Priority Areas from the (randomly ordered) list and rank them from 1st to 5th. The scores were adjusted to reflect the frequency with which they were chosen as well as weighted by ranking to produce an Index score on a 0-100 scale. These scores (as well as the 2021 rankings for comparison) are shown in Figure 7.

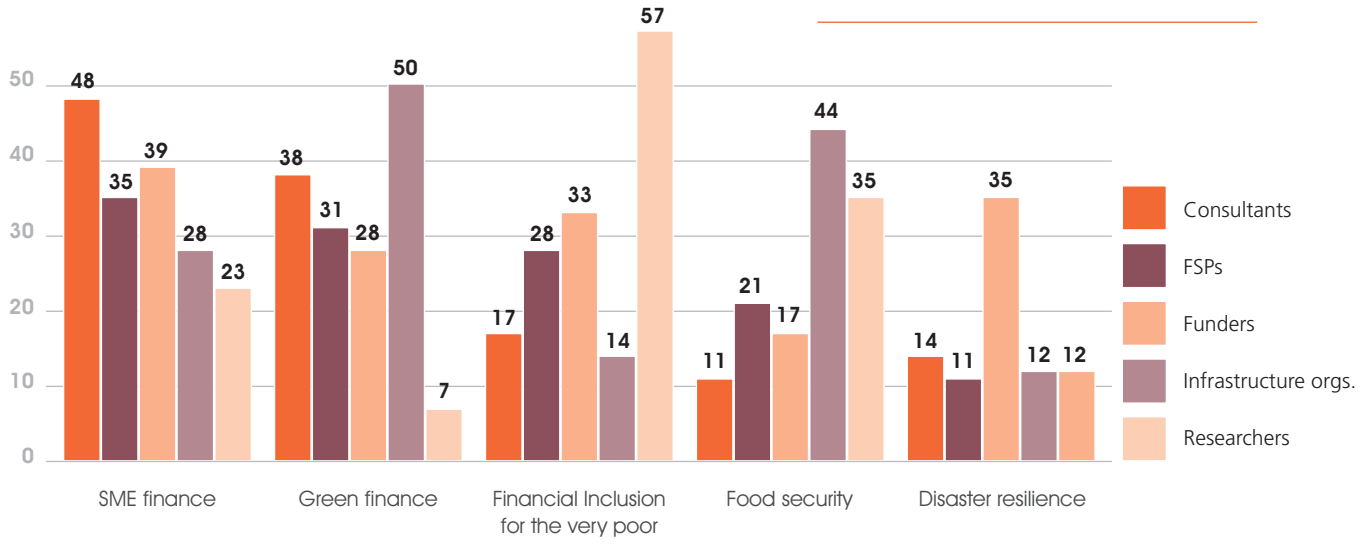
Overall, **the top three stay the same as for the last three years** (albeit in a different order). Women's empowerment and gender equality is in an effective tie for 3rd place, with two new entrants (Financial inclusion for the very poor and Food security) both in the top six.

- **SME Finance** was clear top among all respondents, strongly influenced by Consultants and Support Service Providers who gave it a very high score of 48.1.
- Consultants rated **Food security** very low (11.1), but **Services for refugees/displaced persons** higher than respondents overall.
- Financial Service Providers were the only respondent group to rate **Water, sanitation and hygiene (WASH)** anywhere above the lowest rank. That group's index score of 22.3 (compared to 13.7 overall) accounts for its position up in 10th place. Funders have almost no interest in WASH at all.
- By contrast, funders are very keen to see significant developments in **Disaster resilience**, with a score of 35.2 compared to 14.7 among all respondents.
- Infrastructure organisation respondents are the group most interested in **Green and climate smart finance** and **Food security**, both of which scores were very high. By contrast, they have low interest compared to other respondent groups in **Financial inclusion for the very poor.**
- However, researchers (outliers, always) gave **Financial inclusion for the very poor** a score of 56.7, the highest of any group for any area – and **Green and climate-smart finance** only 6.7 compared to 30.6 for all respondents (enough to prevent this from being in clear second place). Researchers also have high interest in **Financial literacy** and **Food security**.

Figure 8 shows some of these inter-group differences in Index score across 5 selected Future Priority Areas.

Figure 8

Selected Index Scores by Organisation Type



Selected Future Priority Areas - What Respondents Wrote

The following are some selected comments from respondents on the top six Future Priority Areas:

Small and medium enterprise (SME) finance

There is still very much a missing middle here and yet this has such a significant contribution to employment - this is also a good area to develop when micro markets become saturated - but care needs to be taken with methodologies and expertise

Funder

Agri-finance

I believe financial instruments could make a larger contribution than they do so far, and it could contribute to addressing other issues (energy prices, food security)

Consultant and Support Service Provider

Considering all the pressures associated with supporting agriculture (either for commercial purposes or self-consumption) – it links with climate change and climate disasters, ensuring food security, global trade conditions, war consequences, etc.

Infrastructure Organisation

The Ukraine war has put food security into stark relief and most food in developing countries are produced by small-scale farming which will require significant investment to enhance productivity. Plus, climate change has made small holders and livestock herders livelihood more unpredictable which also calls from more microinsurance

Funder

Climate change affects agri-producers in the utmost way and they should be supported & prepare to adapt their practices, and access financial resources to cope with this situation

Financial Services Provider

Green and climate-smart finance

Climate change being the most pressing issue and the catalyst of many other issues, the financial inclusion sector should continue its efforts on climate change mitigation

Funder

At the core of inclusion is the item of resiliency. Without a focused and transversal approach of climate resiliency, financial inclusion will become each year and decade more and more difficult. The inclusive finance sector should move towards a structural inclusion of climate change adaptation/ mitigation and ecosystems/biodiversity conservation and promotion as a key item to ensure sustainable financial, social and economic inclusion

Infrastructure Organisation

In order to provide practical and affordable solutions to microfinance customers to adapt to climate change

Financial Services Provider

Aligned with and overlaps with Agri-finance (my 1st choice) but not quite the same I think

Researcher

Women's empowerment and gender equality

The Economist has observed that it is one of the defining factors between modern and backward visions of society and economy

Consultant and Support Service Provider

This needs to continue to be a priority and build on some important advances especially in terms of awareness raising. Being a trendy issue is not enough to produce the necessary structural changes that will allow to effectively progress in terms of gender equality and fulfil all the untapped potential of women as contributors to their communities

Infrastructure Organisation

Financial inclusion for the very poor

The consequences of the pandemic crisis, war and deterioration of global trade will impact disproportionately the poorest and will increase the percentage of population across the world classified as extremely poor. Need for a re-evaluation of the strategies and the products/services to serve these populations

Infrastructure Organisation

The trend of microfinance in many areas is clearly to finance SMEs (for obvious and understandable motives, namely to cover costs) and to fill the market gap left by banks but the risk is to leave aside a huge portion of potential customers

Financial Services Provider

Really important because of the mission drift of microfinance which continues to pick haves over have nots because they are profitable

Funder

Food security

As many countries are facing growing levels of food insecurity and increasing poverty, reversing years of development gains, and threatening the achievement of Sustainable Development Goals by 2030, FSPs can play a key role in support agri-businesses, small scale farmer and micro entrepreneurs in rural areas

Funder

Think this is a key trend for the planet given growing population and increased political tensions - interested to see more value chain financing which will support this

Funder

Facing challenges

What are the most significant challenges facing the financial inclusion sector today, and what must stakeholders do to meet them?

We have nothing to fear but fear itself. Apart from pain. And maybe humiliation and obviously death. And failure. And the unknown. But apart from fear, pain and humiliation, failure and the unknown and death, we have nothing to fear but fear itself."

Arnold Rimmer

This is the one *Compass* question which has stayed in place for every edition of the survey (except the special Covid-19 edition in 2020) and asks respondents an intimidatingly large question. What are today's greatest challenges in the financial inclusion sector, and what must be done, and by whom, to address them?

Considering that digital transformation of providers and digital services for clients are the two most important sector trends according to respondents, it's not surprising that respondents would want to talk more about these when given the chance. Always perceived as a twin challenge and opportunity, the **digitalisation** of the sector is seen as having been catalysed by the pandemic, both accelerating innovation but exacerbating risks as well.

These challenges have several components. They include "*democratising access to technologies*", according to one FSP, while addressing the "*barriers of fear and distrust*" still widespread among some clients and "*strengthening their digital capabilities and skills to change the culture of using cash for digital money and the adoption of digital applications*", according to another FSP.

How? Financial institutions, writes a different FSP, "*must take up the challenge of transforming their customers into their own bankers by allowing them to carry out their operations in real time 24/7 without having to travel...to do so, they will have to find ways to equip themselves with technological tools and support research in the areas of technological innovation*."

That's the supply-side response – improving products, investing in new and efficient platforms that reduce travel burdens on staff and clients alike and thinking of clients as financial actors. But there is virtual unanimity among respondents that **while necessary, this is not sufficient** – top-down innovation must be matched with bottom-up preparedness and support. This means "*financial education of customers, so that they can make the best use of all the products that have been created*", writes one FSP. According to another, "*the most significant challenge facing financial inclusion is digital conversion and financial literacy. Any development in those areas will affect the development of financial inclusion positively*". But it has to be done for the right reasons, "*from the approach of ethical and solidarity finance… from a customer/user service perspective, not from a bank profit perspective*", according to a TA provider.

This has never been more important. Training in **financial education** is critical to avoiding over-indebtedness, something especially true as the upheavals and financial stresses of the pandemic on low-income households are still not fully understood.

Of course, **the Covid-19 pandemic** looms large among respondents' concerns. Several note the enormous uncertainty about the trajectory of recovery from a shock that has been both broad and deep. Respondents cite the "*non-linear economy resulting from the economic recovery from Covid*", and there are real concerns that there is increased vulnerability among poorer segments, and that FSPs are choosing not to serve them (because of their own vulnerabilities and sustainability challenges), becoming more

and more "*risk-resistant*", according to a funder, who adds that "*financing has a tendency to remain concentrated in certain communities resulting in saturation risk in some areas while other communities remain excluded*".

It's increasingly understood that the pandemic has had an outsized adverse impact on **women**. Redressing this downturn while seeking to re-establishing momentum in what was a longer-term positive trend towards **gender inclusion**, equity and institutional mainstreaming, is an immense challenge. *The sector has a major role to promote intersectional gender equity*", writes a gender consultant. "*It needs to equip itself to better understand the issue of gender inequality (with an intersectional lens) and to integrate this in all that it does institutionally (staff-facing, internal stakeholders-facing, governance, etc.) and operationally (client-facing, agent-facing, service-provider-facing, etc.)*"

Women are half the population, and the majority of clients, but they're not the only segment that needs tailored services to meet their needs. There is a **demographic evolution** underway, meaning more and more young people in developing economies, and more old people in developed markets. "*Keeping pace with this…and at the same time not relaxing on gender equality – despite the great attention being given to the issue at the moment, the task is gigantic and will be far from over at the end of 2022*", writes one respondent.

For FSPs, a major challenge cited by some respondents is **growing and burdensome reporting requirements**, with the unintended consequence of reducing outreach by smaller and more socially focused providers. "*There is a strong mismatch*", writes one respondent, *"between field practices (objective data collection possibilities) and investor/donor expectations; this leads to the risk of pushing out smaller organisations that do not have the capacity to meet the requirements".* And it's not just Tier 2/3 MFIs that are affected; according to one funder, this is a much broader challenge: "*Regulatory trends (SFDR in Europe) are likely to place an increased burden on the whole industry. It is important to ensure that the reporting is beneficial to all parties concerned and does not end up being purely a weight on the minds of everyone, but of benefit to very few*".

"The microfinance sector continues, despite some notable exceptions, to put profits before people in the name of sustainability. Investors and regulators therefore need to recognise that in order to fulfil its financial inclusion mandate, the microfinance sector should not and can not be measured by banking sector standards for profitability and even compliance. This will allow traditional and new MFIs to focus on working with hard-to-reach communities or refugees, especially if donor money can be drawn back into financial inclusion as the sector refocuses on pro-poor impact"

Head of international NGO

Client protection has dominated responses to this survey question since the first time it was asked in 2018. Respondents ask how we can protect clients from unscrupulous new entrants, from fraud, privacy invasions or from the inevitable proliferation of technologies and platforms that are designed to increase efficiencies and breadth of outreach, but may come at the cost of depth. How, they ask, can sector stakeholders ever juggle their claimed social mission with the need to grow and consolidate; keeping existing funders and enticing new ones; welcoming new actors without making traditional providers obsolete?

"The new wave of exploitative lenders, who use apps. If you can't shoot them, then at least regulate them!"

Researcher

Most of these challenges have been heard before in the Compass series, to one extent or another – and the consequences of the pandemic, while complex and serious, are no novelty. What *has* changed in the last year is **global risk and uncertainty** that can in part – but not entirely – be linked to Covid.

The pandemic has been the ultimate **transversal challenge** – with knock-on effects on human resources, client protection, supply chain challenges and household debt, and its inflationary effect on food and fuel prices - not to mention the unknown number of people suffering from 'Long Covid' and unable to work as they did before. It has meant the need to "*balance/[trade-off] human capital versus digital transactions due to the downsizing of FSP operations, to meet financial obligations to funders*", according to an FSP respondent. The "*negative externalities such as supply chain challenges [resulting from the pandemic] affects economic growth, especially in developing countries where the situation is aggravated by components such as informality*", writes a different FSP. This in turn affects the outlook and strategic freedom for providers, who therefore "*must be very careful when generating short-term expansion strategies and seek to maintain a healthy portfolio during this process*", according to the same respondent.

The most significant new addition to this list of risks, however, is not a single challenge but a **group of densely related issues caused by geopolitical and macroeconomic shocks**. The supply chain and food security challenges in an already-inflationary environment have been rapidly accelerated by **Russia's invasion of Ukraine**, leading to what many respondents think of as a perfect storm: a cost-of-living crisis combined with food insecurity right on the back of an unprecedented public health, economic, financial, and mental health shock.

"It's demanding and expensive to rapidly and meaningfully adapt to the challenges posed by adverse events (e.g., climate change, displaced populations, conflict, pandemic, etc.). Among several providers, only a few manage to develop products and customer-centric approaches worth replicating promptly. Understanding end clients' needs remains complex"

Consultant and Support Service Provider

"*The price of oil and the number of refugees*" is cited as a challenge by one FSP. "*Finance for forcibly displaced people either by war and conflicts, climate disasters, political instability, economic failures or a combination of these – this will be a growing issue in the future and as seen recently can affect any area of the world*", writes another. Several others are very worried about the impact of the war on the poorest groups: "*vulnerable sectors are often the hardest hit, which increases inequality and poverty… stakeholders should implement programmes focused on the most affected and excluded populations and have clear strategies to measure the impact of such initiatives*", writes a different respondent. A funder describes the perfect storm as such: "*The Ukraine crisis is likely to place pressure on food security globally…the very poorest are again likely to be most affected, at a time when both population growth and climate change also turn this into a high-risk area…financing directed towards agriculture and value chains therefore appears to be of increasing importance*".

One researcher forecasts the bifurcation of the world order – with sobering consequences. *"The disruption by the Russian attack on Ukraine deepens of course the disruption of worldwide value chains that have started to show [from] the pandemic. But more importantly, we will see a new era of ideological confrontation with two fundamentally different world views… the world is likely to be more volatile, with more poverty, more food shortages, and more descent of fragile democracies into autocracy. All that will affect the ability to pursue credible financial inclusion initiatives"*.

"Increased costs in fuel and food for our clients leading to increased hardship. We will need to be more aware of over indebtedness and unforeseen outcomes for our clients"

CFO of Microfinance Bank

Food insecurity is so critical because it is fundamental – and talking about financial inclusion as a solution overlooks that **food security has to come first.** In 1943, Abraham Maslow posited a Hierarchy of Needs. Within this pyramid, food is right at the bottom – a physiological need of first-order importance. Some respondents alluded to this idea. *"The last mile [segment] lives in areas where there are no enablers like electricity, network, some have no proper housing, food etc. It becomes very difficult to get someone in dire need of basic needs to be financially included unless they have somewhere to live and food"*, writes a consultant. *"Get them started on addressing basic needs, introduce income generating activities, financial literacy and only then formally include them financially. In the background, stakeholders should work to provide the enablers like [food], housing, sanitation, etc so that people are enabled to be financially included"*, she writes.

If there's a single takeaway from the many responses to this question, it's that the **challenges are more diverse and complex and interdependent than ever**. There are some clear externalities - the pandemic and its recovery; the Ukraine war – and longer-term internalities as well, fundamental trade-offs on what financial inclusion means, for whom, and how, that will require hitherto untapped levels of collaboration to respond. As the director of a global association notes, "*the pandemic and technology have ushered in sectoral sea change at such a rapid pace that the change needs to be led. It requires a genuine partnership starting with key stakeholders and spreading to the rest of the sector"*.

"There are many people excluded from the traditional financial system, the number to be reached is still enormous, the means (particularly for the MFIs that are called upon to intervene) are limited, investors are too demanding in their financing, and governments leave them to their personal efforts to intervene. Investors, donors, governments, the World Bank, etc. need to provide efficient MFIs with the financial means to do more financial inclusion in all its forms"

Financial Services Provider

Grasping opportunities

What are some of the biggest opportunities ahead in the financial inclusion sector?

"The reason opportunity is often missed is that it usually comes disguised as hard work."

Clifford Irving

It's been three years since a question about opportunities appeared in the *Compass* survey – the last two editions focused much more on resilience, the adverse impacts of the pandemic on the sector and the management of recovery.

Back in 2019, respondents cited the increased attention to impact and outcomes measurement, SPM, product diversification, outreach to the poor and – especially – digital financial services as the biggest opportunities for the sector. Jumping ahead to 2022, the overall mood is generally more bearish and cautious. *"I see no opportunities in the financial inclusion sector, only challenges to overcome"*, writes a consultant. But others do, and there are a wider range of opportunities cited.

As always, **digital finance** is widely seen as the common thread between many positive outcomes. Digital platforms, products and services can "*solve real problems, e.g. information asymmetries in access to credit*". There is promise in "*agent banking in conjunction with the rural spread of internet-access, as well as 'low-tech-innovation' (using USSD-codes etc)*", according to a TA provider. Digital transformation of financial inclusion services and the incorporation of fintechs are "*the biggest opportunities ahead in the financial inclusion sector as we can work for the young generation, agri-finance and economic development*", according to the head of a FSP. Small entrepreneurs can be accompanied "*in their own digitalization journey, helping them diversify their source of income*", writes a funder. And on the institutional side, a strong "*digital culture*" helps companies stay competitive in four ways, according to an HR manager: *"1. Adapt to a rapidly changing business environment; 2. Make effective use of new technologies; 3. Provide meaningful influence to key stakeholders; and 4. Transition to 24/7 operations"*.

"Increasing connectivity, big data, digital channels and procedures - if applied with responsibility, then this should be a large opportunity"

TA Provider

But all these lofty goals only work if technology is seen as a **means and not the end**; a tool for inclusion not a goal in itself. If so, it'll be *"much more than an opportunity, it'll be an imperative that can bring innovation valuable to the sector but implies keeping at the core of all sector stakeholders those activities that better serve client needs, and having as a pre-condition that digitalisation will not exclude some segments of the population or alternative mechanisms will be found for these segments"*, according to one respondent.

"In the medium term, if things do not go too badly, rising food prices open up opportunities in the field of agri-finance"

Consultant and TA Provider

Interestingly, **green and climate-smart finance** – notably thin in the responses on challenges – was more widely cited as an opportunity. The head of an FSP sees an opportunity "*to lead socially and entrepreneurially the race against climate change, the preservation of our ecosystems and the rethinking of the development model, through microfinance support for sustainable enterprises that put people at the centre of life*". Green finance is an opportunity to "*educate customers on best practices in environmental care*", writes a different FSP. There is now a huge opportunity, writes a fund manager, *to build climate-smart financial inclusion strategies that improve resilience of end-clients towards climate change and help them develop climate adaptation strategies*".

"Increased awareness of challenges posed by a rapidly changing world leads to more resources available for adaptation measures (e.g. blended finance, mainstream financial sector increase awareness, etc.)"

Independent Consultant

There are opportunities too in **stakeholders' understanding of clients' lives and needs,** and the segmentation of clients that helps develop solutions to meet those needs. The latest Global Findex and the Microfinance Index are complementing RCTs, diaries, and emerging methodologies to improve client-centricity. The director of an FSP puts the rationale and process well: "*Knowing the customer, carrying out a correct segmentation to identify specific needs, creating products, services and channels adapted to those needs and managing responsibly, to ensure the customer's financial health and, consequently, their permanence in the management models, until they reach decent living conditions*".

Understanding clients better has knock-on effects, too – especially when combined with **demand-driven digital innovations**. "*The increase in the demand for contactless financial services will give more opportunities for FSPs to develop innovative products and services. Inclusive finance opportunities and financial literacy will scale up even in very distant communities covered by FSPs as long as there is sufficient internet connectivity*", writes an operational director at an FSP. A funder goes further, describing this increased understanding as part of a grander opportunity that includes "*reconstruction of the value chain to a new normal, completing the shift to digital financial service [from] brick and mortar MFIs, with bundled products and services, while holding fintechs and insurtech accountable to affordable pricing*".

"The biggest opportunity is in reaching the farthest and deepest with the best!"

Director at Global Network

Of course, the largest group of beneficiaries when these opportunities are taken is **women.** "*Promoting gender financial inclusion is one the biggest opportunities ahead,* writes a gender expert, who sees the leveraging of digital technologies as an opportunity that will only bring benefits to all segments *"if done in a gender-inclusive way to achieve the aspired results (versus add another layer of barriers to the financial inclusion ecosystem*)". Addressing bias in data is one big issue to tackle in addition to gender inequities in relation to digital literacy as well as access to mobile and digital infrastructure, she adds.

What is clear from several respondents is that the high levels of **collaboration** across and within stakeholder groups during the pandemic can – and must – endure. For all the challenges ahead, there are transformative possibilities too. "*There are certainly more varied and sophisticated models coming out in MFIs: access to energy and micro asset leasing, perhaps being at the forefront. This is a very exciting*

trend and enables new services and improvements to quality of life to be delivered in ways that have not previously been possible" writes a funder. This is bolstered by increased capital flows into impact investing, which "*should be very beneficial in expanding the sector"*, as long as "*risk, return and impact expectations are appropriately aligned as a broader range of investors enter the sector, and this could be a cause of tensions".* This will need the *"increased collaboration among the MIVs during Covid to remain in place".*

Evolution of sector-wide infrastructure

The past two years have seen several sector-wide infrastructure initiatives closing (Smart Campaign, SEEP, MIX), while new ones were created (Atlas, Client Protection Pathway). What do you see as the likely effects of these changes and how will they influence your work over the medium term?

"Plus ça change, plus c'est la même chose"

Anon

The questions in the open-ended section of the *Compass* survey change somewhat from year to year. The last couple of years have seen considerable flux within the infrastructure of the sector, for reasons ranging from natural attrition to unsustainability to the effects of the pandemic. This restructuring poses significant consequences to the different stakeholders – FSPs, TA providers, funders, researchers, and others – who depend on these organisations or initiatives for knowledge creation, networking, data collection, or standard-setting. What does it mean for *Compass* respondents?

For some, there is concern that, whatever the new initiatives being launched, the disappearance of some of the more venerable entities risks a **vacuum of leadership and guidance.** This includes "*confusion in the sector, with for example investors using "old" models, requiring FSPs to follow old standards and thus distorting sector efforts towards coordinated development*", according to one respondent, and a degradation of institutional memory too, with the loss of SEEP cited by one respondent as a "*significant blow to the sector…the rich content which is still available on their website will not grow nor be actively curated, including through their R&D, training and development work*". The end of SEEP was bemoaned by several respondents, including one who describes it as *"a cruel twist of fate that such an important tool for financial inclusion was unable to raise the cash required for its survival whilst the financial services industry is again making record profits"*.

And the new players must **prevent the slow creep of reporting burdens on FSPs.** The new entrants need *"stable resources and sustainable business models"*, writes a TA provider. *"For institutions"*, he says, *"it represents an additional investment to adapt to new standards, especially when they are among the first to do so. These initiatives in terms of infrastructure are often perceived as too [burdensome] by the actors on the ground. To facilitate their acceptance, it is necessary that these initiatives deliver added value more quickly for the institutions, and not only for the "northern" actors who often dictate the specifications"*.

Yet not all news is bad news, according to others, who point to a sort of **creative destruction.** There is a better understanding of how to improve customer protection and customer experience, and the end of the Smart Campaign and its quasi-reincorporation via the CP Pathway is seen by some as positive. One funder writes that *"the Pathway aims at being more inclusive thanks to the tiered approach and different levels of certification. We hope that it will encourage more microfinance institutions to join the initiative and implement client protection best practices"*. A head of an INGO goes further, describing the end of the Smart Campaign as an "*improvement, as the industry coalesces around a single rather than two competing standards*", something which applies as well to the end of the MIX Market, which had "limited *applicability due to both the self-reporting methodology and very limited uptake by smaller MFIs"* and now has been *"combined with World Bank data to provide a more comprehensive picture of financial inclusion"*.

"Atlas and the Client Protection Pathway are well positioned to replace the previous sector initiatives"

TA Provider

These organisations' roles are often framed as collaborative or even collegiate, with their sharing of ultimate objectives – inclusion, access, poverty alleviation, literacy, etc. But the truth is, infrastructure organisations are **competitors** – for projects, talent, funding, and influence. In this sense, according to some respondents, it is natural that there should be attrition and churn. "*I do not expect negative effects, because each of the mentioned ones has always had competitors. (e.g. a staff of SEEP once told me that they see CGAP as their major competitor)"* writes one. "*I do not know exactly how much the Smart Campaign achieved, but I think the IFC-Performance Standards provide a comprehensive framework to cover client protection along with other topics such as environmental compliance etc."* writes another. "*In the end, it is all about value-based business models"* this respondent adds.

"I don't see any impact arising from the closure of some initiatives in the medium term due to the continuity offered by other on-going interventions"

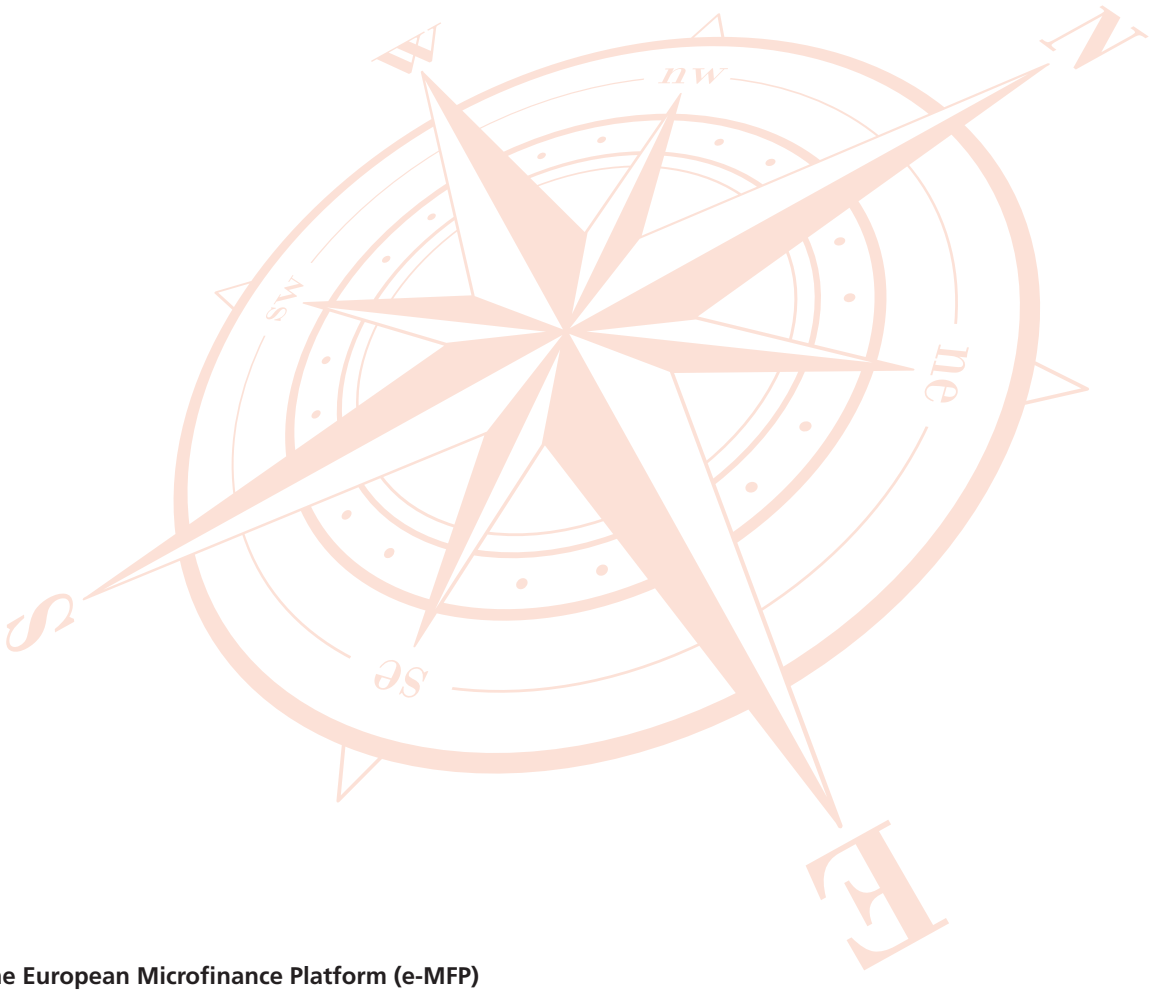
Consultant and TA Provider

This positive outlook based on the **natural evolution of the sector** is a widely repeated theme, and among the respondent group really drowns out any hand-wringing over the disappearance of certain entities. It's variously described as stemming from the "*constant effect on the market of change and innovation, which requires adaptability on the part of MFIs"*; with effects, according to another, that are "*all positive, in order to ensure responsible practices, a controlled environment and a healthy market, all for the benefit of the client and their satisfactory experience."* And according to yet another respondent, it's part of a "*natural process of adaptation to changes in the measurement of the sector. A clear example is the end of the Smart Campaign, which had a certification legacy derived from various organisations such as MFR. In view of this, we believe that it is relevant to be updating these initiatives from our institution according to the needs and demands of the sector".*

But that's not to say there aren't risks. **Continuity** must be ensured to guarantee that progress isn't lost or that there is regression in client protection and SPM in particular. This is especially true considering the impact of Covid on clients and the general acceleration of digitalisation it brought about. Says one respondent, "*It is therefore positive that SPTF+CERISE are giving continuity to the client protection issues and ATLAS is taking a leading role in collecting data in the sector. These transitions are complex and not easily done but they are also an opportunity for innovation and improvement".* To ensure they are recognised and well received "*with brand recognition*", writes another, *"will take a lot of work"*.

"There is a time and season for all initiatives. However, it is key that we fight the tendency to discard old initiatives, but rather, new initiatives should build on what were, once, new initiatives themselves"

Director at Global Network of FSPs



About the European Microfinance Platform (e-MFP)

The European Microfinance Platform (e-MFP) is the leading network of organisations and individuals active in the financial inclusion sector in developing countries. It numbers over 130 members from all geographic regions and specialisations of the microfinance community, including consultants & support service providers, investors, FSPs, multilateral & national development agencies, NGOs and researchers.

Up to two billion people remain financially excluded. To address this, the Platform seeks to promote co-operation, dialogue and innovation among these diverse stakeholders working in developing countries. e-MFP fosters activities which increase global access to affordable, quality sustainable and inclusive financial services for the un(der)banked by driving knowledge-sharing, partnership development and innovation. The Platform achieves this through its numerous year-round expert Action Groups, the annual European Microfinance Week which attracts over 400 top stakeholders representing dozens of countries from the sector, the prestigious annual European Microfinance Award and its many and regular publications.

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