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**Swiss Agency for Development
and Cooperation SDC**

Swiss Agency for Development and Cooperation

Financial Sector Development Guidance



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Acronyms

AML	anti-money laundering
ASCA	accumulating savings and credit association
ATM	automatic teller machine
BDS	business development services
CBS	core banking system
CFT	countering the financing of terrorism
CGAP	Consultative Group to Assist the Poor
CRM	client relationship management
CVECA	caisses villageoises d'épargne et de credit autogérées (self-managed village savings and credit banks)
DFI	development finance institution
DFS	digital financial services
ESG	Environmental, Social and Governance
FI	financial institution
FPCSs	financial products, channels, and services
FSA	financial service association
FSD	financial sector development
FSDG	Financial Sector Development Guidance
ICT	information and communication technology
KYC	Know-Your-Customer
LNOB	leave no one behind
MFI	microfinance institution
MIS	management information system
MNO	mobile network operator
MSD	market systems development
MSEs	micro and small enterprises
NBFIs	non-bank financial institutions
NFS	non-financial services
NGO	nongovernmental organisation
POS	point of sale
ROSCA	rotating savings and credit association
SACCO	savings and credit cooperative
SCBF	Swiss Capacity Building Facility
SDC	Swiss Agency for Development and Cooperation
SDGs	Sustainable Development Goals
SECO	Swiss State Secretariat for Economic Affairs
SHG	self-help groups
SIFEM	Swiss Investment Fund for Emerging Markets
SIINC	Social impact incentives
SMEs	small and medium enterprises
SPTF	Social Performance Task Force
TA	technical assistance
TDA	term deposit account
UN	United Nations
USSPM	Universal Standards for Social Performance Management
VSLA	Village Savings and Loan Association

Executive Summary

Financial inclusion as an enabler to reach the Sustainable Development Goals

Financial inclusion means that individuals, households, and businesses have opportunities to access and the ability to use a range of appropriate financial services that meet their needs and are delivered in a responsible and sustainable way. **Financial inclusion is not an end in itself but is highlighted as a target in many of the Sustainable Development Goals (SDGs). Hence, financial inclusion is positioned prominently as an enabler of the SDGs** ([→ see Chapter 3.2](#)). Broad economic development depends on well-functioning financial systems. The Swiss Agency for Development and Cooperation (SDC) promotes universal financial inclusion and equal access to financial services as an essential pillar of sustainable and inclusive economic growth. **SDC's more than 40 years of engagement and efforts in promoting financial sector development (FSD)** have, in this regard, evolved toward improving the sustainable financial inclusion of low-income households. SDC's FSD interventions conjunct with complementary fields like private-sector development, vocational skills development, and agriculture and food security. They **address all dimensions of financial inclusion: access to financial services, quality and use of financial services, and the welfare impact of financial services.**

The goal and structure of SDC's Financial Sector Development Guidance

SDC's Financial Sector Development Guidance (FSDG) defines the basic principles underlying its international cooperation activities in the area of FSD. **The guidance is an internal SDC document** that offers strategic and operational advice to decision-makers at SDC headquarters and cooperation offices, operational staff, partner project executing agencies, as well as international and national consultants. Through the FSDG, SDC aims to foster a broad understanding of the versatile topic, and to facilitate feasible designs and efficient implementation of coherent and effective cooperation programmes and projects in SDC partner countries. Given strong interlinkages and complementarities between FSD and thematic areas like gender equality, education, health care, migration, and climate change, the FSDG targets professionals in a broad range of thematic fields.

The FSDG starts by introducing the **market systems development (MSD) approach as SDC's main approach to FSD** ([→ see Chapter 1](#)). The FSDG further provides **explanations on the functions and set-up of financial systems, the systems' actors and levels, and sets the complex system in context with the overarching idea of promoting financial inclusion** ([→ see Chapter 2](#)). In this context, digitalisation and the role of digital financial services (DFS) providers is highlighted. [Chapter 3](#) digs deeper into the relevance of the financial sector for poor populations. Building on this common understanding, the FSDG presents the context of SDC's thematic priorities in FSD, as well as its objectives, strategic orientation, and principles in strengthening and facilitating financial systems ([→ see Chapter 4](#)).

SDC's operational principles and instruments to engage in FSD

SDC's interventions and actions in FSD target the demand side, the supply side, financial system support services, and the regulatory/supervisory environment. As [Chapter 4](#) explains, actions on each intervention level follow distinct operational principles and can make use of a variety of instruments and approaches. **On the demand side**, SDC's operational principles follow a focus on supporting those who demand financial services and products to become more financially capable by improving their financial literacy and bankability – also a crucial aspect of client/consumer protection. To **strengthen the supply financial institution (FI) side**, SDC can use a toolbox of technical assistance (TA) approaches like greenfielding, down- and up-scaling, and transforming financial institutions; and financial assistance approaches including refinancing loans, risk-sharing mechanisms, structured funds, impact bonds, and social impact incentives. **SDC targets the financial system's infrastructure and its supporting functions** in cooperation with partners, for example, through the establishment of national and international partnerships with industry associations/chambers; organising best practices exchanges; knowledge sharing and cross-country peer exchanges; and the overall improvement of information flow between financial institutions, their clients, and other actors. **On the regulatory and supervisory side**, financial sector reforms for the achievement of ambitious financial inclusion objectives and related SDGs are needed – and claimed – in many SDC partner countries.

SDC can support this process by engaging in policy dialogue to support innovation and reforms or by supporting the improvement of the legal framework for financial transactions. SDC can support the development of a conducive regulatory and supervisory framework for financial systems through the provision of quality research and analytical work, the organisation of exchange formats, as well as through bilateral technical assistance, capacity building, and organisational development of regulatory and supervisory authorities. It is not SDC's objective to engage in broader financial sector interventions on a macro level. However, when targeting the regulatory and supervisory framework, SDC's focus always lies on inclusiveness and the financial inclusion of its target beneficiaries, namely rural households, micro and small enterprises (MSEs), and smallholder farmers. SDC engages where it can provide adequate support to regulators and supervisors based on relevant experience on a micro and meso level in SDC priority countries.

Outlook and Priorities

Future FSD will have to react and find answers to global developments like the increasing pressure on vulnerable households, smallholder farmers, and MSEs related to climate change, and the increasing importance of creating equal economic opportunities and economic inclusion for women and young people in the global south. In addition, continuous or increasingly high migration activity and refugees and the implications for economic development in origin and receiving countries will require new approaches and solutions in FSD.

Derived from its competitive advantage, SDC's operational principles and intervention tools in FSD allow the organisation to address emerging and accelerating future developments and challenges toward responsible inclusive financial systems, in cooperation with international development institutions and partners on the local level. Emerging innovations and technologies, such as the exponentially progressing diversification and expansion of the [digital financial services \(DFS\)](#) ecosystem or the emergence of technological innovation in previously low-tech sectors, represent unseen potential for enabling [financial inclusion](#) and sustainable growth.



FSD GUIDANCE

**RATIONALE FOR
SDC'S FINANCIAL
SECTOR DEVELOPMENT
GUIDANCE**

1.1 Rationale and goal of the guidance

In 2015, the United Nations General Assembly adopted the 2030 Agenda for Sustainable Development, along with the Sustainable Development Goals (SDGs) as the new set of development goals. As stipulated in the 2016 Consultative Group to Assist the Poor (CGAP) publication, «Achieving the Sustainable Development Goals: The Role of Financial Inclusion,»¹ **the SDGs cannot be achieved without a focus on financial inclusion.**²

SDC has been active in FSD since the 1970s, acknowledging the fact that a functioning, stable, and dynamic financial system is indispensable to improving the living conditions of the population and is a key driver for sustainable economic development and the reduction of global poverty. SDC focuses its activities on people living in poverty, giving special consideration to the poorest of the poor and the excluded, and recognizing the multiple dimensions of poverty in line with the «leave no one behind» (LNOB) approach – the central pledge of the 2030 Agenda. SDC anchors LNOB in all its strategic documents and programmes and strives to introduce it in the strategies of its partners, including multilateral organisations.

Equal access to financial services and universal financial inclusion is essential for sustainable and broad-based economic growth. SDC activities in FSD do not work as stand-alone interventions, but mostly work in conjunction with complementary domains (e.g., private-sector development, small enterprise development, agriculture, rural development) since successful global and country programmes and projects increasingly depend on a well-functioning financial system. Interlinkages and complementarities between FSD and thematic areas like gender equality, good governance, education, health care, and migration, as well as climate change and natural resource management, have and will become even more relevant. This is why SDC seeks synergies for maximum impact and efficiency. For the same reason but on a more aggregated level, SDC aims to coordinate activities and interventions with the Swiss State Secretariat for Economic Affairs (SECO)³, other donors and international organisations, the private sector, and civil society. SDC thereby follows a bottom-up approach with a focus on poverty reduction.

Presented in the form of a guidance document, the FSDG defines the basic principles orienting SDC's international cooperation activities in the area of FSD. It presents the context of SDC's thematic priorities, as well as its objectives, strategic orientation, and operational principles for its interventions in the facilitation of financial systems. As an internal SDC document, the guidance is intended to acquaint the reader with **SDC's «way of thinking», as well as its methods and practices regarding FSD** in partner developing countries and regions. The guidance is subject to periodic updating through SDC internal and external experts, based on regular analyses of global and institutional developments related to FSD. The update process builds on institution-wide interviews, and takes up changing industry standards/concepts and international best practices, as made available by relevant actors and think tanks such as CGAP, the World Bank Group, the United Nations, the Toronto Centre, and the Social Performance Task Force (SPTF).

The FSDG is meant to guide current and future SDC interventions in FSD, in line with Switzerland's Strategies for International Cooperation and the Federal Council's 2030 Sustainable Development Strategy. This guidance is directed toward decision-makers at SDC headquarters and cooperation offices, partner implementing agencies, as well as to international, Swiss, and national experts in partner countries and regions.

1 Klapper, L., M. El-Zoghbi, and J. Hess. 2016. «Achieving the Sustainable Development Goals: The Role of Financial Inclusion.» Washington, D.C.: CGAP. Available at: https://www.cgap.org/sites/default/files/Working-Paper-Achieving-Sustainable-Development-Goals-Apr-2016_0.pdf

2 Before the adoption of the SDGs, the development of the financial sector featured an important reference framework for international cooperation. The role of the financial sector in its own right has been acknowledged internationally since the 1989 World Development Report and continuously has been highlighted as key to development in the UN Millennium Declaration in 2000, the UN Monterey Conference in 2002, and numerous policy white papers over the years.

3 There is close cooperation and coordination of activities in countries where both SDC and SECO are active.

SECO: Swiss State Secretariat for Economic Affairs

Since SDC and SECO both operate in the financial sector, their actions in this field are closely coordinated. SECO **supports efforts to reform** international framework conditions, for example, in the area of financial sector stability and regulation, market development, integrity, Environmental, Social and Governance (ESG) standards and climate finance.

SECO works at the national and subnational level on both the supply and demand side:

(i) by strengthening regulatory and supervisory frameworks for the banking and [non-bank financial sector](#), monetary policy and central banking operations, strengthening foundations for financial sector development, and deepening of financial markets, as well as respective oversight. It particularly focuses on strengthening domestic capital markets and their provision of long-term finance. This includes ensuring that financial products are safe and transparent for consumers. SECO also focuses on strengthening financial sector integrity ([anti-money laundering \[AML\]](#) and [counter-financing of terrorism \[CFT\]](#)), with a particular focus on balancing the need for innovative digital solutions and ensuring the integrity of markets with a view to fighting illicit financial flows.

(ii) by providing credit infrastructure and payment systems and creating new financial products that take into account innovative financial technologies, ESG, and climate finance aspects. Through its instruments, SECO promotes access to financing for small and medium enterprises (SMEs) so they can invest, tap into new markets, grow, and create decent employment opportunities. SECO **promotes gender equality** by promoting financial products tailored to the specific needs of female entrepreneurs and businesswomen. SECO is committed to **mobilising private capital to achieve** the SDGs and has been committed to impact investments since the 2000s. It does so mainly through the Swiss Investment Fund for Emerging Markets (SIFEM) – the development finance institution (DFI) owned by the Swiss Confederation and supervised by SECO – as well as through the SECO Start-up Fund. In addition, SECO **mobilises knowledge and capital for sustainable infrastructure services** in areas such as mobility, water, and energy.

1.2 SDC's approach to FSD

SDC applies the [Market Systems Development approach \(MSD\)](#) to its work in FSD. With this approach, SDC aims to support the development of inclusive, self-sustaining [market systems](#) in partner economies to become more independent from external aid. Financial systems form a crucial element and enabler of complex market systems. By catalysing [systemic change](#), SDC aims to reach large-scale results.

The MSD approach emphasizes the following premises:

- ▶ A recognition that institutions operate in systems, and that systems are complex and unpredictable: They are made of the complex and ever-evolving interactions of individuals and institutions. The different functions and actors of financial systems are further explained in [Chapter 2.2](#).
- ▶ A thorough analysis of market systems to identify underlying causes for exclusion rather than just the superficial symptoms.
- ▶ A facilitative role for funders and implementers who need to facilitate systemic change, which requires understanding the dynamics of the system then playing a temporary role to nudge the whole system toward a new equilibrium that works better for the target group.



FSD GUIDANCE

DEFINITION OF KEY CONCEPTS



2.1 Financial sector as a system

In this guidance, the term «financial sector» is used synonymously with the term «financial system». The financial system is illustrated in *Figure 1*. It consists of the totality of functions as well as individual and institutional actors in the financial sector:

- ▶ **Demand for financial services:** clients seeking financial products and services (e.g., MSEs, individuals, poor households, women, smallholder farmers, etc.)
- ▶ **Supply of financial services,** including:
 - savings products that help individuals and households keep their funds safe;
 - **microcredits** for low-income households and MSEs to support their cash flows;
 - loans and other credit products and services to MSEs to boost productivity and increase competitiveness;
 - payment services to ensure the fast and secure processing of domestic and international payment transactions;

- inclusive insurance to protect low-income (and rural) populations against life's adversities, such as weather effects, natural disasters, disease, or death.

- ▶ **Supporting functions** are a range of functions that support, shape, inform, and enable transactions between demand and supply. Actors that often play a role in providing such supporting functions include training institutes, business development services (BDS) providers, market information providers, etc.
- ▶ **Rules** include both formal and informal norms that shape incentives for **market actors** and determine who can participate in financial services markets and under what conditions. Besides the concrete examples of rules listed in *Figure 1*, it is important to note that rules are not just financial-sector related. A set of given rules such as social assistance and digital transformation policies affect the development of the financial system as well.

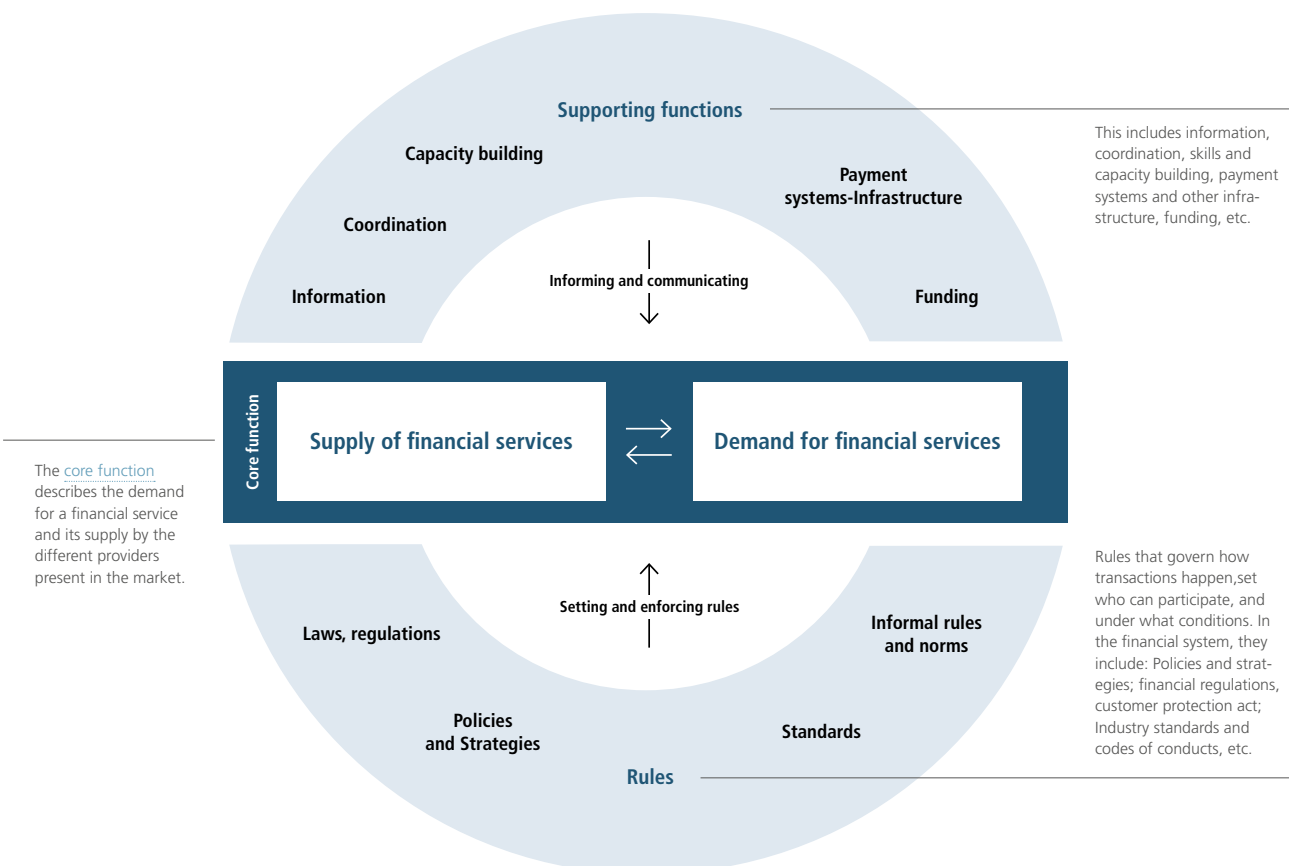


Figure 1 The Financial Market System. Adapted from CGAP

4 Burjorjee, D., and B. Scola. 2015. "New Funder Guidelines: Market Systems Approach to Financial Inclusion." Washington, D.C.: CGAP. <https://www.cgap.org/research/publication/new-funder-guidelines-market-systems-approach-financial-inclusion>

Formal vs. informal financial systems

Figure 2 illustrates the spectrum of financial institutions according to level of formality. The presence of responsible financial institutions alongside a reliable financial infrastructure and appropriate financial regulation and supervision – assured, implemented, and monitored by bank and non-bank financial regulators – characterise the formal financial sector. Following different gradations, there are semiformal financial institutions and the informal financial sector. Semiformal financial institutions are, for instance, [microfinance](#) institutions (MFIs) that are registered as banks with a special charter or as nongovernmental organisations (NGOs) that serve those who have been excluded from the formal banking system. The [informal financial services supply](#) consists of local financial institutions, savings and loan associations, moneylenders, and self-help groups. The informal sector is not (or is only partially) regulated or supervised, which creates a number of challenges and risks. **The informal financial services supply – through credit and saving groups, small-scale value chain finance, or lending from relatives/friends, for instance – often builds upon a deeply rooted tradition, mainly due to customer proximity and physical presence in underserved regions.** These informal providers play a key role in poor people’s lives. There are opportunities to connect informal mechanisms with formal providers, thus creating a stepping-stone for people to gain trust in formal providers and access more diverse and better suited financial services.

Digital transformation and digital financial services providers

Digitalisation has become a leading driver of inclusion for the unbanked around the world. The transformation that digital technology is creating has deep implications for the traditional financial services providers. It is reshaping financial sectors, institutions, and product/service offerings, and is creating opportunities through digital financial services. Today’s DFS providers can be broadly divided into four main groups: (i) full-service financial institutions offering transactional accounts for payments, transfers, and value storage via mobile device, online banking, or payment cards – in combination with point of sale (POS) terminals; (ii) limited-service financial institutions offering transactional accounts via mobile device or payment card, plus a POS terminal; (iii) mobile network operators (MNOs) operating as e-money issuers; and (iv) non-bank [e-money](#) issuers. All of these groups build on three main concepts: a digital transactional platform, [agent](#) networks, and the customer’s access devices. Digital transformation in financial institutions can further entail innovation and development in banking software application, process automation, and product development/delivery. It could help expand inclusion in various ways⁶:

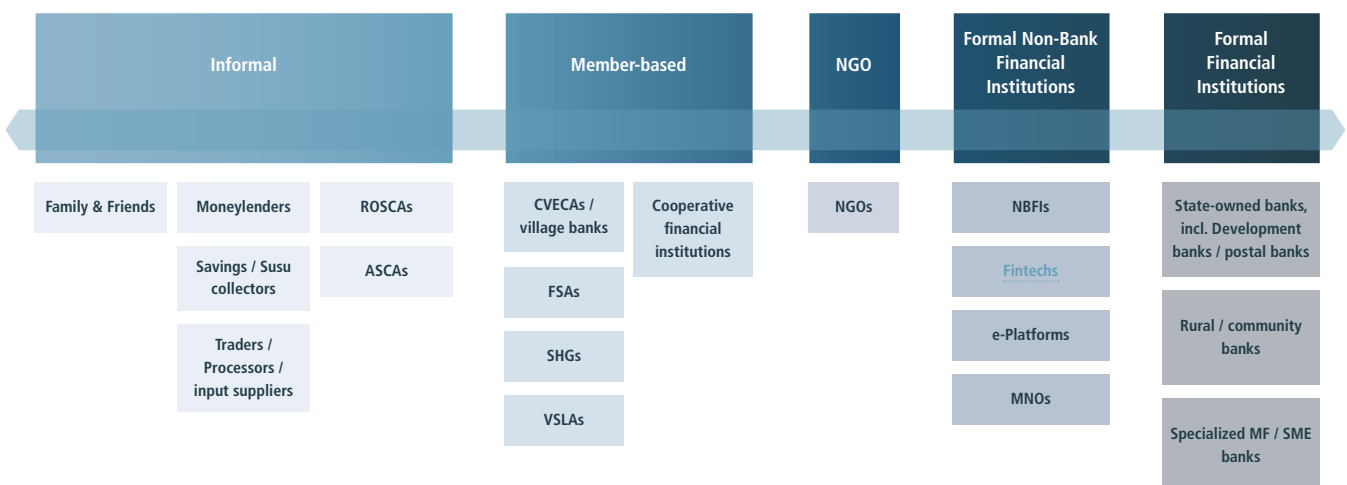


Figure 2 Spectrum of Financial Institutions According to Level of Formality⁵.

5 Adapted from CGAP (2006). Access for All: Building Inclusive Financial Systems. Washington, DC: World Bank. : http://www.cgap.org/gm/document-1.9.2715/Book_AccessforAll.pdf and: Plaitakis, Ariadne, and Stefan Staschen. 2020. "Open Banking: How to Design for Financial Inclusion." Working Paper. Washington, D.C.: CGAP.

- ▶ **Cost:** Financial products or services are more [affordable](#) for providers to offer and for underserved customers to use.
- ▶ **Access:** Financial products or services are more accessible and useable to underserved customers.
- ▶ **Fit:** Financial products are better suited to the needs and wants of underserved customers.
- ▶ **Experience:** Automatically learn from customer experience (with regard to access and usage) to further tailor financial services to the needs and wants of underserved customers.

However, digitalisation may also bring new risks such as new forms of exclusion, the digital divide, [data privacy](#) and security risks, and algorithmic biases.

The policy and regulatory framework of financial systems

Governments play a crucial role in setting policies that allow and support sustainable intermediation of financial services and products. Besides macroeconomic stability and liberalized interest rates as covered by a country's monetary policy, the facilitation of an appropriate regulatory, supervisory, and legal framework is key to a well-functioning financial system. Focusing on the regulatory framework, diverse regulating authorities (e.g., central banks, bank and non-bank supervisory authorities) regulate financial institutions, markets, and products through means such as licensing, registration, and rulemaking, as well as supervisory, enforcement, and resolution powers. As previously stated, broader rules such as digital transformation policies impact the financial system. For example, telecom regulators may need to be brought in early to ensure the healthy development of [mobile financial services](#).

The different types of regulation include prudential (safety and soundness), disclosure, standard setting, competition, and price and rate regulation. Prudential regulation aims to ensure the financial soundness of regulated financial institutions to prevent system-wide financial instability and to protect depositors from losing their savings. It includes capital adequacy and reserve and liquidity requirements. **Non-prudential regulation** includes measures like registration with authorities for transparency purposes, adequate accounting and bookkeeping, active and documented prevention of fraud and financial crimes (e.g., AML/CFT), and various types of [consumer protection](#) measures (e.g., the World Bank's Good Practices for Financial Consumer Protection, Client Protection Standards).

SECO Best Practice: Financial Sector Development and Reform Programme (FSDRP II), South Africa

A successful first programme phase (FSDRP I, 2014–2018) contributed to key financial sector reforms in South Africa, like the adoption of the Financial Sector Regulation Act through which prudential regulation and market conduct oversight were strengthened and achieved. Building on these achievements, SECO continues to support the South African government in its efforts to strengthen financial stability and improve financial inclusion. The second programme phase (FSDRP II, 2018–2023) aims at making financial sector reform efforts effective to serve the development needs of the economy, as well as contribute to the country's medium-term growth and poverty reduction goals. While Phase I placed strong emphasis on building a sound regulatory and supervisory financial framework, Phase II will further consolidate and strengthen the government's financial inclusion agenda. To advance the soundness and inclusiveness of the financial sector, the programme builds on three pillars: (i) transforming the market structure, (ii) safeguarding the financial system and consumers, and (iii) increasing finance for the real economy.



2.2 Financial inclusion

Financial inclusion means that formal, tailor-made, and responsible financial services – such as deposit and savings accounts, payment services, loans, and insurance – are readily available to consumers, and that these customers are actively and effectively using these services to meet their specific needs⁷. These services are prerequisites for enabling people to build up reserves, make investments, transfer money, and protect themselves against risk. They give them the means to pay for purchases, education, and health care. Micro-entrepreneurs and small businesses, in turn, are able to obtain the necessary capital required to create jobs, income, and prospects for the future. Hence, financial inclusion is key to enabling low-income households (SDC's main target group) to build economic resilience and progress.

Still, only a small proportion of the economically active yet poor population in a vast number of developing countries has access to [formal financial services](#) and relies on informal financial services providers. Informal financial services are as diverse as they are ubiquitous, range from simple to complex, and may or may not be “traditional.” Informal financial services providers usually emphasize interpersonal relationships, hence allowing facilitated access to financial services on the one hand, while being characterised by high interest rates and lack of transparency and supervision on the other hand. Great strides have been made toward financial inclusion, and 1.2 billion adults worldwide have moved from informal finance to formal access to finance (e.g., have opened an account) since 2011. It seems that moving from access to an account to regular account

7 Global Partnership for Financial Inclusion 2011.

8 World Bank, Global Findex Database 2017.

usage is the next logical step. However, close to one-third of all adults – 1.7 billion – are still unbanked, and about half of them are women and low-income households in rural areas. The gender gap in account ownership remains stuck at 9 percent in developing countries, hindering women from being able to effectively control their financial lives⁹.

There are four core dimensions of financial inclusion (see *Figure 3*). SDC considers the multidimensional character of financial inclusion as paramount, and accordingly attempts to design and implement its programmes and projects (interventions).

► The **access** dimension encompasses parameters like the network of a financial institution’s physical access points. This includes branches and outlets, but also the existing agent network, POSs, and ATMs – in other words, the supply and availability of financial products and services offered by formal financial institutions (proximity, convenience, affordability, and equality of access).

► The **use** dimension covers the extent of usage of formal, and in specific cases, informal financial services by individuals (and businesses). Formal financial services include any count of accounts (physical or mobile/digital) that allow the user to make and receive payments and store money, savings accounts, and loans. The dimension includes thus the levels and patterns of use of different formal financial products and services (multiple use cases, increased uptake, and regularity).

► The **quality** dimension of financial inclusion is not as straightforward an attribute as access and use. On the contrary, many factors can affect the quality of financial services, such as the cost of services, consumer awareness, effectiveness of redress mechanisms and consumer protection services, security of funds, transparency and competition in the market, and intangible features like consumer trust (transparency, reliability, responsibility, and relevance).

► The **welfare** dimension captures the impact of financial products or services on the livelihoods of consumers, including their changes in consumption, business activity, and wellness (resilience and risk mitigation).

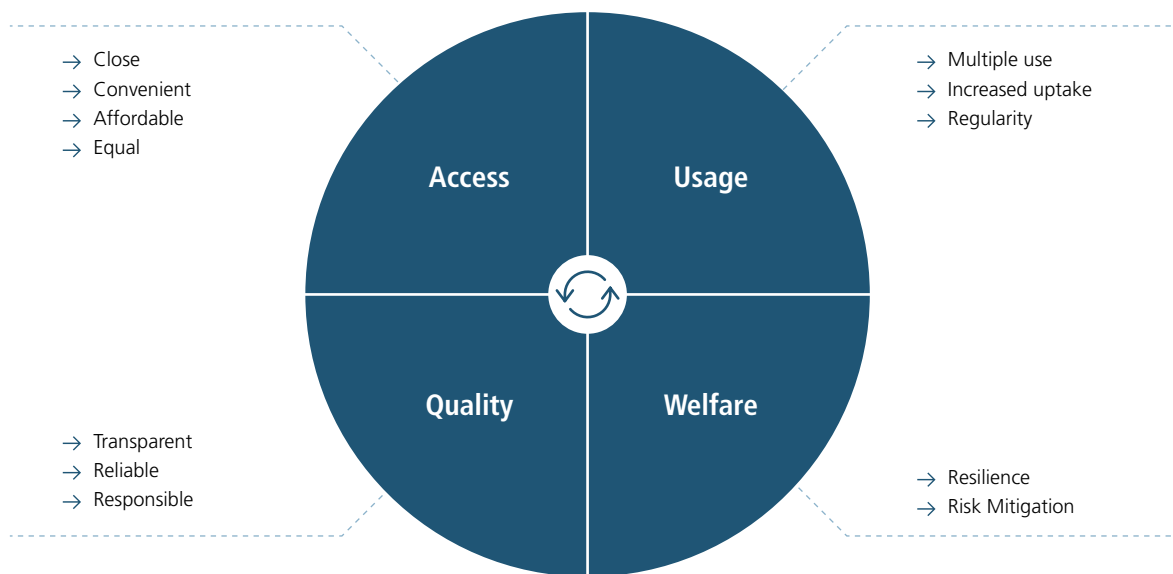


Figure 3 The Four Core Dimensions of Financial Inclusion⁹

⁹ Adapted from Pearce, Douglas; Ortega, Claudia Ruiz. 2012. Financial inclusion strategies: reference framework. Washington, D.C.: World Bank Group. <http://documents.worldbank.org/curated/en/801151468152092070/Financial-inclusion-strategies-reference-framework>



FSD GUIDANCE

**RELEVANCE OF
THE FINANCIAL
SECTOR
FOR THE POOR**

3.1 The developmental significance of the financial system

There are many ways in which FSD contributes to development. The most important aspects are further explained and summarized in *Figure 4*.

By financing MSEs, the financial system supports employment promotion and job creation. In fragile contexts¹¹ these income and employment effects can contribute to a country's stability and thus may prevent conflict and crises. The financial system is also of fundamental importance to the expansion and deepening of an economy. It transforms small deposits into larger loans for investments and diversifies and manages risks.

A financial system that is aligned with the needs of women and men positively impacts economic growth, which allows poverty and economic inequality to reduce. At the same time, access to responsible and sustainable financial products and services contributes to greater stability of national and international financial systems.

The relevance of the financial sector is most prominently shown through its interdisciplinary importance in the (design and) implementation of development projects and programmes. Most of the critical areas relevant to developing countries and hence supported by international cooperation initiatives (e.g., gender, rural development, migration, education, as well as energy and climate action) require financing and/or financial solutions and answers. Besides its government, it is a country's financial system that becomes increasingly relevant to offering those initiatives.

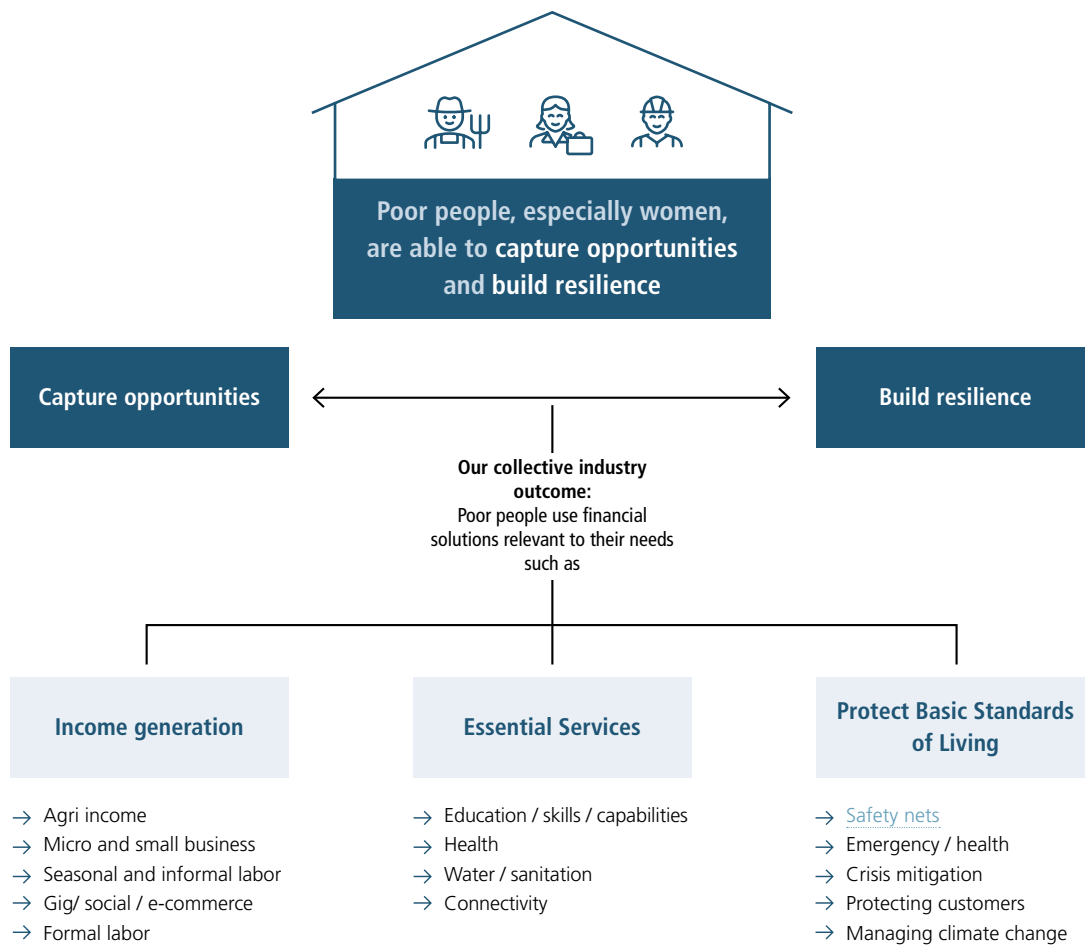


Figure 4 Financial inclusion¹⁰

10 Adapted from: Storch, Silvia, Emilio Hernandez, and Elizabeth McGuinness. 2020. "A Research and Learning Agenda for the Impact of Financial Inclusion." Focus Note. Washington, D.C.: CGAP.

11 SDC uses the Organisation for Economic Cooperation and Development (OECD) definition of fragility. OECD defines fragility as the combination of exposure to risk and insufficient coping capacity of the state, system, and/or communities to manage, absorb, or mitigate those risks (OECD, 2016).



For people in the lower segments of the income pyramid, access to and use of [basic financial services](#) can improve family incomes, increase resilience to shocks and risks, and sustainably improve their lives. In line with the LNOB pledge, excluded and underserved groups, especially women, can benefit from deepened inclusive financial sectors, if all dimensions of financial inclusion are coevally enhanced.

According to the World Bank¹², more than 65 percent of adults in the developing world lack access to even the most basic formal transaction account that would allow them to safely and easily send and receive payments, much less access the savings, insurance, and credit services that would help them expand their businesses, mitigate risks, and plan for their future. The financial sector in many SDC partner countries fulfils a specific development function by mobilising often substantial, locally available funds and encouraging their reinvestment in the local economy. In this context, a properly functioning financial sector is a precondition for effective poverty alleviation.

3.2 Financial inclusion as an enabler

Financial inclusion is prominently positioned as an enabler of the SDGs. Contributing to development goals through financial services **is not an end in itself but highlighted as a target in thirteen of the seventeen SDGs, which are explained below**^{13,14}. Further, it has a notable indirect role in most of the other SDGs.

12 Pazarbasioglu, C., A. Garcia Mora, M. Uttamchandani, H. Natarajan, E. Feyen, and M. Saal. April 2020. "Digital Financial Services." Washington, D.C.: World Bank Group. <https://pubdocs.worldbank.org/en/230281588169110691/Digital-Financial-Services.pdf>

13 Office of the United Nations Secretary General's Special Advocate for Inclusive Finance for Development (UNSGSA), UNCDF, and the World Bank. 2019. "Igniting SDG Progress through Digital Financial Inclusion."

14 Klapper, L., M. El-Zoghbi, and J. Hess. 2016. "Achieving the Sustainable Development Goals: The Role of Financial Inclusion." Washington, D.C.: CGAP. Available online at https://www.cgap.org/sites/default/files/Working-Paper-Achieving-Sustainable-Development-Goals-Apr-2016_0.pdf



Inclusive finance allows people to climb out of poverty by investing in economic activities or education. At the same time, it prevents low-income people from falling into poverty by softening the blow of unexpected expenses. For example, having access to savings instruments allows families to increase their capacity to absorb financial shocks, [smooth consumption](#), accumulate assets, and invest in health and education. Digital financial payments products allow people to receive money or [remittances](#) from faraway relatives and friends during times of crisis or on a regular basis, thus supporting the cash flow of entire households.

SDC and the Importance of Savings Mobilisation as the First Step toward Financial Inclusion for Low-Income People

SDC's long-lasting interventions in and around the promotion of savings mobilisation as a key first step of financial inclusion for low-income people will continue to play a central part in its future FSD activities. Savings products can improve people's ability to meet daily household and business expenses and strengthen their resilience against exogenous shocks. They mark the first step toward successful financial inclusion, since saving builds an economic base for investment and resilience. Savings product availability and ability to make use of products are key pillars: A lack of access to basic financial services for saving makes it difficult for the poor to take control of their economic lives. Financially capable people who are included in the financial system are better equipped and able to climb out of poverty by making informed saving and investment decisions (e.g., into business or education).



About 795 million people globally are undernourished. Most live in rural areas neglected by the financial system and lack access to credit and insurance. This missing access prevents farmers from making investments that could increase crop yields and strengthen food security. Access to agricultural insurance products can embolden farmers to become less risk-averse and to increase their levels of investment in their farming systems, which can lead to increased earnings and greater food security. Savings accounts can support this effect and allow farmers and rural populations to manage their expenses during the agricultural off-season. Digital financial services make it easier to access and manage these types of financial services and products (e.g., the saving of time, money, and effort by not having to travel far distances to physical outlets).

SDC Best Practice: Improved Access to Useful Financial Services at Fair Prices in Bolivia

With SDC support, thousands of farmers and small entrepreneurs in rural areas of Bolivia have been able to gain access to savings accounts, [microinsurance](#) schemes, micro-leasing facilities, and loans. The strengthening of the country's financial sector has resulted in more savings and loan cooperatives and institutions opening branches in rural areas, and support for product innovation has led to the development of useful financial products at fair prices. This has enabled farmers, for example, to increase their production and protect their investments through insurance schemes. SDC experience in this field has also been put to use in the creation of a national agricultural insurance scheme.



Financial inclusion improves health by giving people the ability to manage medical expenses and rebound from a health crisis. Financial services like medical insurance can provide a formal channel for mitigating the risks of health emergencies. Women especially are in need of health insurance products to address the common health concerns associated with pregnancy and childbirth. Savings are also an important tool for managing medical expenses, whether planned or unplanned.



Achieving quality education depends on people having the financial ability to invest in learning opportunities and training. Savings products can enable households to sustainably manage education expenses. Credit products and national/international remittances also support households in paying for education-related expenses like tuition fees and learning materials. Digital payments products can enable direct payments to education institutions, hence providing for better planning and household expense accounting.



Financial services contribute to achieving the SDGs by helping women assert their economic power, which is key to promoting gender equality. Financial inclusion of women can contribute to gender equality by giving them greater control over their finances. Savings accounts can provide women with a safe and formal platform to build a credit history and to accumulate their earnings for future investments. Digital payments products can equally assess the creditworthiness of women's traditional credit assets or a financial transaction history. Gender-sensitive digital financial services support women-owned businesses in various ways (e.g., by reducing the risks of theft and lowering administrative and disbursement costs).



Digital financial services particularly offer the potential to enable previously excluded people access to basic services and to be included in the climate transition. Financial inclusion has an indirect but notable and more greatly acknowledged role in strengthening low-income people in the climate change transition and ensuring their access to clean water and energy. Connection points include, for example, financing of water connections, bill payments for both water and energy, and climate transition-relevant inclusive insurance products allowing the creation of job opportunities for target groups.

SDC Best Practice: Microinsurance Rollout by the Lead Foundation in Egypt

The Lead Foundation is a not-for-profit microfinance institution whose mission is to provide poor and low-income entrepreneurs, especially women, with sustainable access to quality microfinance services that address their needs and build their capacity.

With funding support from the Swiss Capacity Building Facility (SCBF) and a concurrent grant from Visa Inc. and Women's World Banking, the Lead Foundation was able to (i) enhance its IT systems, (ii) build its programme management capacity, and (iii) assess the profitability of a hospital and life insurance product to develop a three-year roadmap for its continued success. As a result, Lead enabled more clients to have health support which enhances their ability to cope with medical emergencies while mitigating the associated financial burden and any negative impacts on household well-being. By the end of the pilot project supported by SCBF, Lead had 191,794 active clients, 88 percent of whom were women.

8 DECENT WORK AND ECONOMIC GROWTH



Access to financial institutions and products and services gives people the opportunity to gain higher returns on capital. This effect can lead to increases in their income, and consequently affects economic growth and reduces income equality. Sustainable inclusion in the financial system strengthens the foundation of low-income people to shared economic growth. Effective financial systems can mobilise savings to finance investments in productive business activities and facilitate innovation.

9 INDUSTRY, INNOVATION AND INFRASTRUCTURE



Access to financial services is likely to facilitate the establishment of more businesses and enterprises. In particular, credit products and services allow existing ventures to expand their income-generating activities by enabling greater investment in production and management resources. Inclusive finance supports the increase of growth-oriented MSEs, allowing the creation of job opportunities for target groups.

10 REDUCED INEQUALITIES



Financial inclusion, particularly the drivers of digital transformation, can be a powerful equalizing force. Financial inclusion can give low-income households new tools to access quality health, education, and utility services – areas that can constrain economic opportunity. Households unequally participating in economic activities and growth, especially women, can hence increase their incomes, improve financial resilience, and access new economic and social opportunities.

11 SUSTAINABLE CITIES AND COMMUNITIES



The rapidly growing global urban population relies heavily on the existence of affordable public services such as housing and transportation, and access to financial services that allow access to and use of these services. Financial inclusion and the use of digital technology has the potential to increase quality and efficiency of services, for instance through digital payment systems or micro-mortgages, and promote new, inclusive housing and mobility solutions toward increasing urban life quality.

13 CLIMATE ACTION



Financial inclusion can help individuals, communities, businesses, and governments to combat and prepare for the damaging effects of climate change, particularly by building resilience and driving sustainable investments. Risk mitigation through access to (digital) savings, credit, and insurance services can help mitigate climate-related risks, while environmentally friendly investments can help reduce carbon emissions.

16 PEACE, JUSTICE AND STRONG INSTITUTIONS



Financial inclusion helps promote peace. The likelihood of social turmoil is lowered by providing a foundation for equitable growth and improving the lives of the poor. Through the improved provision of demand-oriented, quality finance products by responsible financial intermediaries to MSEs, as well as smallholder farmers and women-led businesses, the financial system supports objectives to promote employment and create jobs. Positive income and employment effects contribute to reduced inequality and promote peace in societies.



FSD GUIDANCE

**SDC'S OBJECTIVES
AND PRINCIPLES
IN SUPPORTING
FINANCIAL SECTOR
DEVELOPMENT**

4

4.1 SDC's general objectives and transversal topics

SDC's objectives and intervention principles are derived from a combinational analysis of overall sector developments and SDC's institutional, organisational, and technical comparative advantages. The core of the analysis is an institution-wide, cross-sectoral thinking process, which, supported through external expertise, aimed at identifying SDC's strengths and intervention logic. As a result of this process, and in line with the four main market systems functions previously described in Section 2.2, SDC's general objectives in FSD can be defined as:

- ▶ **Targeting the demand side.** Supporting those who demand financial services and products to become financial capable through improving their [financial literacy](#) and bankability (e.g., financial and business management skills) to sustainably include informed people in the financial system. SDC is focusing on low-income households (notably low-income women), smallholder farmers, and small businesses – and all those excluded from financial systems, based on the LNOB pledge. Targeting these groups is essential in order to reduce risks of remaining or falling back into poverty, to achieve a more effective cushion against economic and market fluctuations, and to save for larger investments such as children's education or setting up a business.
- ▶ **Targeting the supply side.** Supporting informal, semiformal, and formal financial institutions to become responsible, viable, and client-oriented service institutions maximising their own potential (and at the same time fulfilling their responsibility) concerning the financial inclusion of SDC's target groups. This is to be achieved through the provision of tailor-made, responsible, and safe savings and insurance products and services, and increased outreach and/or accessibility (through innovative solutions like agent banking or DFS). SDC can play a guiding and supportive role, particularly in the transition process of formalising informal financial services providers and the prospect of enabling them to fulfil their role and exploit their potential toward financial inclusion. SDC places special emphasis on savings and inclusive insurance products and services. Access to and use of savings promotes financial inclusion and the autonomy of target groups, financial institutions, and the national economy. Tailor-made inclusive insurance solutions, in particular but not limited to agricultural and disaster insurance, provide SDC's target groups with the means to protect themselves against the effects of risks. It also extends social protection through security, contributing to poverty alleviation and the inclusion of excluded and

underserved groups (women in particular), in line with the LNOB pledge. A key priority is given to agricultural finance and associated risks that negatively affect target groups, such as risks caused by climatic factors, natural disasters, and unpredictable price changes. SDC's interventions cover the development and implementation of new innovative insurance solutions (e.g., data-driven index insurance) created in collaboration with public and private partners in target countries.

- ▶ **Targeting support services.** Assisting support infrastructure actors in improving the quality and accessibility of products and services for financial institutions and final beneficiaries, and by improving the skills and capacity of their management and staff members.
- ▶ **Targeting the regulatory and supervisory framework.** Facilitating and supporting regulatory/supervisory actors in creating an enabling regulatory framework for the financial sector, always with a clear focus on promoting financial inclusiveness for SDC's target beneficiaries, namely rural households, MSEs, and smallholder farmers. This includes, for instance, supporting the transformation of informal and semiformal financial institutions into formal ones, and improving the skills and capacity of their management and staff members. SDC engages where it can provide adequate support to regulators and supervisors, based on relevant experience on a micro and meso level in SDC priority countries. SDC and SECO proactively ensure effective coordination and keep each other informed of relevant interventions.

SDC cooperation programs define the levels of cooperation and the roles, specific instruments, and areas of expertise SDC intends to employ in coordination with local partners and other donors, based on an analysis of complementarity and value added.

Financial Inclusion of Migrants

According to the United Nations Department of Economic and Social Affairs, the number of international migrants globally reached 280 million in 2020, an increase of 120 million (63 percent) since 2000. This number is likely to further increase, reflecting global economic downfalls from the COVID-19 pandemic. Global, regional, and domestic financial sectors need to find answers to this scenario. Financial inclusion of migrants, especially migrant women, is important not only from an economic but from a social point of view, to cover their family's basic needs. Despite their wide-ranging needs for financial and related non-financial services, migrants and refugees face many obstacles to accessing these services, including lack of identification, lack of income, and lack of [financial education](#). Due to the many parallels between financial inclusion of the poor and financial inclusion of migrants, the international discourse agrees that the following interventions initiated by various market actors can yield sustainable results to improve inclusion:

- ▶ Digitalisation of cash-based interventions and financial education, financial literacy, digital literacy
- ▶ Tailor-made financial and non-financial products and services (e.g., savings and loan products, [micro-] insurances, welfare services, social security, pension funds)
- ▶ Remittance transfer and [mobile money](#) services
- ▶ Universally recognised digital IDs, [KYC](#) processes “light”

Transversal topics in financial systems development

SDC's FSD interventions are geared toward achieving maximum pro-poor impact through the promotion of financial inclusion and capacity development throughout the financial sector. In light of the challenges that lie ahead and in line with the underlying LNOB principle, addressing transversal key topics relevant to the majority of interventions – and as underlying prerequisites toward sustainability and impact – is crucial to making a difference. In addition to other pertinent transversal topics, four topics are considered key and are proactively addressed throughout FSD interventions to seek synergies and leverage complementarities (where applicable):

- ▶ **Strengthening resilience against climate change and promoting inclusive measures to cope with climate transition.** The climate change crisis could force 100 million people into poverty and is reorienting a significant share of development funding toward climate change solutions. The financial sector can play a key role in supporting low-income people to prepare for and participate in the climate transition. Key pillars will be the protection of basic standards of living through increased resilience (e.g., through savings and insurance), improved access to essential services (e.g., pay-as-you-go for electricity and water usage), and the promotion of income generation (e.g., through adequate loan products).

- ▶ **Fostering women empowerment and gender-equal economic and social participation.** Despite overall progress in financial inclusion, the gender gap remains evident. To advance inclusive finance for women, there needs to be a deeper understanding of use cases about how financial services can be leveraged by women, particularly in the field of DFS, and how stakeholders can engage and support the transition process (e.g., through women's peer networking platforms, awareness creation, etc.).
- ▶ **Facilitating consumer protection principles in the financial sector through the Universal Standards for Social Performance Management (USSPM).** To motivate use of accessible formal financial services, FSD interventions have to strengthen trust in the financial sector and promote frameworks and rules to protect consumers and financial institution clients. This particularly holds true for the emerging DFS sector. SDC emphasizes the promotion of good practices in social performance management (SPM) and consumer/client protection through its strong, early-stage support of the Social Performance Task Force (SPTF). ([see box on next page](#)).
- ▶ **Invigorating good governance of financial institutions.** For measures to unfold their potential toward inclusive finance, it is crucial to support the design of good governance practices (e.g., with regard to rule of law, informational transparency, public participation) to enable financial services to empower different target groups.

Social Performance Task Force (SPTF)

A particular focus of SDC is the promotion of client/consumer protection. SDC is one of the core funders of the SPTF, a not-for-profit membership organisation with more than 3,000 members. The SPTF is mandated to develop and promote standards and good practices for SPM in an effort to make financial services safer and more beneficial to clients. The Universal Standards for SPM have been developed since 2005 and include the Client Protection Standards from the Smart Campaign. After the closure of the Smart Campaign in July 2020, SPTF and CERISE have taken the lead on client protection and developed the [Client Protection Pathway](#), a roadmap for improved client protection practice. SPTF and CERISE are providing guidance, tools and resources along the key steps of the Pathway to deliver transparent, respectful, and prudent financial services to all clients, and ensure that the client protection standards are progressively implemented.

4.2 SDC's general operational principles

SDC's general operational principles for FSD are outlined according to intervention levels and key actors. The operational principles build on **SDC's main comparative advantages** in FSD:

- ▶ **A high level of expertise in rural finance**, capitalising on synergies with complementary rural development activities;
- ▶ **Close proximity to partner institutions** and target groups as defined by the LNOB pledge, particularly women, and a high level of understanding of local cultural and socioeconomic contexts in priority and partner regions and countries to promote inclusion;
- ▶ **Strong ability and experience to work in multi-partner arrangements** on final beneficiary, institutional, market infrastructural, and policy levels;
- ▶ **Support of technical and/or methodical innovations** for partners on all levels;
- ▶ **Support in FSD-related research** and analytical work;
- ▶ **Development cooperation with a long-term perspective**, as SDC puts emphasis on long-term partnerships using approaches and instruments for long-term sustainability of effects concerning economic growth, well-being, and poverty reduction, particularly the LNOB pledge;
- ▶ A diverse set of flexible financial and technical assistance instruments adaptable to local needs and conditions; and
- ▶ A high level of expertise and commitment to sustainable capacity development at all intervention levels.

Based on these comparative advantages, and in close cooperation with other international organisations, SDC builds on **seven general operational principles and priorities** in financial sector development:

1. **In line with the MSD approach and based on sector-wide analyses, SDC cooperation programmes are designed** to take into consideration underlying causes constraining MSD, financial inclusion, local priorities, and partnerships, as well as SDC's comparative advantages.
2. **SDC focuses its interventions on geographical areas and activities in which its expertise can complement accessible local and regional expertise along the principle of subsidiarity.** This approach forms the basis for SDC to harmonise and align its contributions to the development of local financial markets, promoting inclusive finance and the support of national policies targeting the long-term reduction of poverty.
3. **It is SDC's priority to foster partner financial institutions' own contributions** (financial commitment and in-kind) to ensure ownership and sustainability. SDC places importance on understanding and enhancing a financial institution's motivation and commitment toward the systemic changes needed to allow financial services to contribute to achieving the SDGs.
4. SDC aims at **leveraging synergies and building upon complementarities with other development disciplines and their programmes and projects.** The topical proximity to areas like private-sector development, agricultural and rural development, and private-sector engagement offers vast opportunities to do so. For instance, synergies can be leveraged in the promotion of local

companies and the development of integrated value chains through business linking and collaboration with agricultural extension services, as well as through other market infrastructural services like education, transportation, etc. However, such collaborations shall not compromise the need to institutionally separate financial and non-financial services (NFS).

5. **Capacity development is essential at all levels for strengthening financial sectors.** SDC's capacity-development support is highly adapted to a partner's human and financial resources and encompasses broad-scale approaches, as well as selective specific interventions with limited durations. Considering a partner financial institution's or support organisation's perspective and a participatory planning and implementation process enhances ownership, management buy-in, and sustainable integration of measurements in organisational strategies and resource plans.
6. **SDC is particularly committed to supporting the development, testing, and dissemination of innovative banking technologies** adapted to local conditions (e.g., digitised agricultural lending applications, GPS-based plot, environmental and social exclusion criteria assessment) that support informal and formal financial institutions to realise efficiency gains through appropriate risk assessment with positive effects for final beneficiaries.
7. **Importance is given to the capitalisation, exchange, and dissemination of practical experiences and good practices.** SDC therefore supports national, regional, and international networks and conferences, and actively participates in international committees, global initiatives, and think tanks (e.g., CGAP, SPTF). Attention is given to supporting and facilitating the application of sector knowledge and good practices within SDC and its partnerships.

4.3 SDC's strategic orientation, operational principles, and instruments

Over decades, SDC focused its FSD programmes and projects on rural areas and capacity building activities. However, the actively conducted discourse within the development world has progressed from a traditional "access to finance" to a holistic "financial inclusion" way of thinking. SDC's proactive participation in this dialogue influenced SDC's long-lasting priority areas. SDC supports its partner countries with measures targeting demand- and supply-side financial sector supporting functions and the regulatory and policy framework. SDC sees great potential in the ongoing digital transformation in partner country financial sectors and individual financial institutions. Interventions can support the digital transformation process within dedicated financial institutions with the objective of increasing outreach to new customer segments (e.g., rural agricultural customers, women, youth).

4.3.1 The demand side

SDC does not intervene directly on behalf of its target groups, but through relevant support organisations (e.g., member-based associations, cooperatives, producer groups, self-help groups) that assist the final beneficiaries in their transition to sustainable inclusive finance. However, the delivery of non-financial services, like the strengthening of member-based organisations or financial education, must be decoupled from concrete financial services to equip target groups with the necessary capacity to access financial services. It also leaves them the choice of whether or not to access financial service(s), and, if so, which one(s). Bilateral development cooperation commits itself to creating economic, social, and environmental opportunities in a select number of priority countries. This is approached by:

- **Strengthening financial health and [financial capability](#)**¹⁵ through financial education of low-income households and individuals (notably women), smallholder farmers, and MSEs to facilitate livelihood improvement. In other words, SDC's priority target groups can sustainably benefit from interventions that make financial and non-financial services available for the continued improvement of individual livelihoods and eventually for the greater welfare of a partner country.

¹⁵ Financial capability is the combination of attitude, knowledge, skills, and self-efficacy needed to make and exercise money management decisions that best fit the circumstances of one's life, within an enabling environment that includes, but is not limited to, access to appropriate financial services.

- ▶ In terms of financial products, SDC concretely supports the demand side through capacity building and active support in awareness creation and information collection, which are required to tailor financial services to demand-side needs. A priority, first-intervention focus by SDC is on **promoting savings mobilisation for low-income people** due to its importance as the first step in financial inclusion, and domestic retail and institutional deposits (short- or long-term) that induce a healthy liability structure and financial stability. Depending on context, SDC has specific experience and expertise with informal savings mechanisms. A second emphasis in terms of financial products is on the **development of inclusive insurance markets, particularly agricultural and disaster insurance, but also health insurance as the last frontier of financial inclusion**. Well-designed inclusive insurance products (e.g., against crop and property losses caused by natural hazards) are crucial in reducing the risks incurred by small (holder) farmers and micro and small business owners. These products serve to increase productivity, thus setting the ground for strengthening food security.

Operational principles and instruments for targeting the demand side:

- ▶ Strengthening members of target groups in areas like skills, education, and training, as well as health and social abilities through professional and dedicated local or national support organisations, groups, and associations. Emphasis is placed on the importance of financial education and financial capability as key to the sustainable inclusive finance of identified target groups. The same counts for basic business and financial management skills, as well as for vocational training.
- ▶ **SDC understands client/consumer protection from the demand-side perspective as a matter of (financial) literacy and education.** The better target groups are informed about basic functions of financial market actors (e.g., financial institutions), terms and conditions, and the risks and obligations of financial products and services, the more trust and confidence they accumulate in accessing and using them on a regular basis. SDC's support measures can take the form of enabling support organisations, service providers, or self-help groups in the development and implementation of financial education/financial literacy training. In addition, SDC can support educational campaigns and awareness creation for designated target groups.

4.3.2 The supply side

Potential (semi)formal partner financial institutions are identified in terms of their capacities and motivations to contribute to the systemic changes SDC aims to contribute to. In this regard they represent both actors to be strengthened and instrumental institutions that strive to achieve development objectives like improved financial inclusion. A due diligence process is important when selecting partner financial institutions. **Only financial intermediaries with the potential to increase their efforts and expand their services on a cost-covering basis to facilitate the financial inclusion of SDC target groups are eligible for cooperation.** SDC's principles do not foresee unilateral intervention, but rather cooperation and partnerships with local actors when working to improve the regulatory and legal framework. Therefore, selected FIs must be able to deliver on their financial inclusion agenda under the existing legal and regulatory framework. As a second prerequisite, any potential partner financial institution must share a development vision with SDC and commit itself to implementing it within a specific timeframe. The vision must be based on a client-centric approach and have the potential to improve existing or develop new responsible, customer-oriented, innovative financial services and products that appropriately address the needs of SDC target groups. Emphasis is placed on accessible and safe savings products (e.g., saving accounts, saving plans, term deposit accounts [TDAs], etc.); insurance products; innovative and easily accessible digital financial services such as mobile money, mobile wallets, and mobile payment services; and gender-specific financial products.

When identifying and supporting formal partner financial institutions, SDC takes into account the following considerations:

- ▶ **A professional management approach** to maintain or aim toward solid institutional and financial sustainability. Senior management must be committed and open to institutional change and development.
- ▶ **Commitment and implementation readiness for the establishment of general risk management frameworks** or best practice risk management systems, internal control and internal audit systems and functions, transparent performance evaluation, and a dedicated reporting function¹⁶.
- ▶ **Establishment and compliance with a good institutional (corporate) governance system** with laid-down rules, practices, and processes that sustainably direct and control the financial institution.

¹⁶ FI compliance with international industry standards are an asset in FI selection.

- ▶ **Commitment and implementation readiness for the improvement or establishment of best practice human resources and leadership policies** that cover staff training, capacity building, personnel retention, and career path elements, as well as leadership development.

Operational principles and instruments for targeting the supply side:

- ▶ **Testing/piloting innovative approaches to increase financial inclusion.** SDC provides technical assistance to develop and scale innovative client-centric financial products, channels, and services (FPCSs) to reach its target groups. This entails capacity building, feasibility studies, research work, and pilots to introduce new FPCSs, plus support innovation and upscaling by financial institutions and non-bank financial institutions (NBFIs) like insurance companies, fintechs, and “[insurtechs](#)”. Targeted institutions can include early-stage ventures whose business model has yet to be proven as compared to traditional financial institutions. Since the development of inclusive insurance markets is a great priority for SDC, supporting local or international insurance companies that already offer inclusive agricultural or other types of insurance or are committed to doing so in the near future can sustainably benefit target groups.
- ▶ **Downscaling.** Downscaling is a well-known and proven business and development approach that traditionally describes the structured expansion of corporate or large commercial banks into the upper SME sector (potentially even the low-income individual sector) but is also applicable to fintechs and MNOs. Downscaling requires genuine commitment, solid business strategies, and perseverance by management and staff members of commercial banks when it is intended to sustainably penetrate the above-mentioned economic segments and/or agricultural or rural markets. SDC’s operational principles entail support to fully operational commercial banks, with a clear development agenda and strategic vision to deepen outreach through technical assistance and capacity building.
- ▶ **Transformation.** Semiformal and formal financial institutions with a clear vision and the institutional and financial potential of economic viability and large-scale outreach are strengthened to expand their economic activities into upper market segments. Upscaling equally leads to more formality and the potential transformation into regulated (deposit-taking) financial institutions like microfinance institutions, savings and loan companies, finance houses, etc. SDC’s operational principles entail classic technical assistance, organisational development, and capacity building activities.

In addition, SDC facilitates an institution’s access to domestic capital markets or, if more feasible, regional and international microfinance funds or social and impact investors. Access most often improves institutional governance, strategic depth, and financial leverage.

- ▶ **Restructuring of public (private) development banks.** SDC may assist in the restructuring of development and agricultural banks and [apex institutions](#)¹⁷. A precondition for SDC support is the financial institution’s willingness to assume strategic roles vis-à-vis retail/commercial financial institutions in serving SDC target groups.

SDC’s various financial instruments are carefully chosen by taking into account the partner financial institution’s developmental stage, as well as by matching its financial requirements:

- ▶ **Grants (and possibly other instruments) to co-finance investment into pro-poor innovations** and, in exceptional, well-justified cases, to temporarily cover part of its operational expenses at gradually decreasing levels.
- ▶ **Return-based instruments**, meaning repayments are envisioned (or at least possible), including:
 - ▶ **Loans (and in exceptional cases, equity) for refinancing purposes**, as long as access to funding and/or equity on the domestic, regional, and international capital markets is not possible or feasible.
 - ▶ **Risk-sharing instruments** to share SDC partner financial institutions’ risks when, for example, entering new market segments or developing and testing new products and services (e.g., DFS) or innovations (e.g., agent or [branchless banking](#) models), with the potential to reduce transaction costs and deepen outreach toward low-income clients and rural areas.
 - ▶ **Structured funds, such as blended finance pooling mechanisms**, where various categories of investors (e.g., private commercial investors, DFIs, donors) with different risk-return profiles jointly invest (different types of loans or loans and grants) in a financial vehicle. The objective is to mobilise large volumes of investment capital – and/or in medium-/long term loans (which are, for example, essential to MSE development). In the context of financial inclusion, where private (impact) investors (and impact investment vehicles) are financing (e.g., MFIs), the emphasis is increasingly on financing fintech companies, among others, or encouraging financial inclusion of excluded groups, such as migrants. They are considered too risky by private, commercial investors, so they depend on patient capital from the global development and impact investing communities.

¹⁷ An apex institution is a second-tier or wholesale organisation that channels funding (grants, loans, guarantees) to financial institutions in a country or region.

- ▶ **Impact bonds** where (impact) investors advance funds for an investment in a development or humanitarian project, and an outcome payer pays the investor a return if the project achieves predefined development outcomes.
- ▶ **Social impact incentives (SIINC) and other outcome and results-based payments**, where payments are made directly to an organisation (e.g., financial institution, social enterprise, etc.) provided that predefined development outcomes or agreed-upon results have been achieved – and, if applicable, additional investment is mobilised.

Blended Finance

Blended finance is the use of development finance to attract private capital toward projects that contribute to sustainable development while providing financial returns to investors. According to CGAP, blended finance is a key mechanism to attract private investors to close the estimated \$2.5–3.7 trillion annual gap to finance the SDGs. In financial inclusion, blended finance is an important enabler of the SDGs. The concept is not new; blended finance has a strong track record in attracting private investment from international and local sources. Within the framework of the SDGs, donors and development finance institutions are encouraged to use their funding to “crowd in” private capital. They can find guidance in the OECD Blended Finance Principles, which provide direction toward anchoring, designing, tailoring, monitoring, and partnering for blended finance.

4.3.3 The financial system’s infrastructure and supporting functions

SDC supports financial institution networks, associations, and alliances; training institutes and BDS providers; rating agencies; credit bureaus; auditor associations; payment systems associations and providers; fintechs and mobile network operators (MNOs); IT and TA providers; etc., through a broad range of technical assistance, capacity building, and organisational development and innovation support.

Operational principles and instruments for targeting the financial system’s infrastructure and supporting function:

SDC makes use of a **wide variety of operational instruments** to strengthen the (financial market) infrastructure of partner countries, such as:

- ▶ Technical assistance, for example, to improve quality and flow of information between financial institutions, their clients, investors, and the general public.
- ▶ Establishment, facilitation, or co-financing of national and international partnerships with chambers, industry associations, or sector-specific educational institutions.
- ▶ Supporting organisational development, for example, by organising exchange visits, study tours, national and international seminars, and conferences.
- ▶ Fostering innovation, for example, by commissioning quality research and analytical work.

The financial sector’s regulatory and policy framework:

In the context of supporting the financial sector’s regulatory and policy framework toward financial inclusiveness for SDC target groups in line with the LNOB pledge, SDC focuses on the following activities in its priority countries:

- ▶ Based on country programme-specific strategies, **SDC can contribute to the development of more favourable and enabling framework conditions toward financial inclusion**, particularly by fostering the transformation from informal to formal financial services provider.
- ▶ Interventions targeting a partner country’s policy, regulatory, and supervisory framework are usually implemented in **coordination and collaboration with other international organisations** like the World Bank and/or other bilateral and multilateral donors, including SECO.

Operational principles and instruments for targeting the financial sector's regulatory and policy framework:

More competitive and inclusive financial markets require an enabling environment for all market participants created through conducive and efficient laws and by effective, non-bureaucratic supervisory authorities and mechanisms. SDC aims to support these processes to enable inclusivity of financial systems for its target groups through micro- and meso-level interventions in line with the LNOB pledge.

- ▶ **SDC may engage in a policy dialogue to support micro- and meso-level innovation and reform processes** of the regulatory and supervisory framework to enable financial inclusion of its target groups. These interventions are informed by SDC's programmes and projects, and always implemented in close coordination and cooperation with other bilateral and multilateral donors and/or international organisations, SECO in particular, and directly target micro- and meso-level processes. Conducive and enabling regulatory and supervisory frameworks must be established in areas like digital financial services, payment systems, savings mobilisation, and consumer protection – all areas with tremendous implications for the financial inclusion of SDC target groups. Further, it must enable informal and semiformal FIs to engage in transformation toward formal FIs – a process which SDC can support.
- ▶ Depending on the fiscal and legal situation of a partner country, SDC may also support the improvement of the legal framework for financial transactions (e.g., payment systems, settlement systems, legal context for DFS, etc.), as general contract and property laws and collateral laws directly influence the operations of financial institutions and their clients, particularly SDC target groups. Interventions targeting the legal framework of a financial system in most cases require a multidisciplinary approach that seeks synergies from interventions by disciplines such as agricultural and rural development, private-sector development, and governance.

SDC's instruments to **support regulation and supervision for financial inclusion include the provision of quality research and analytical work**; the organisation and (co)-financing of exchange visits and study tours; the organisation of conferences, summits, round tables, and seminars; and bilateral technical assistance with micro- and meso-level focus, capacity building, and organisational development of institutions.



FSD GUIDANCE

OUTLOOK AND PRIORITIES

It is already foreseeable that the international community and SDC will face several challenges in implementing strategies and/or policies that promote the establishment of responsible inclusive financial systems which are able to sustainably facilitate economic growth and equality of low-income households, small farms, and MSEs. At the same time, emerging innovations and technologies represent the unseen potential for enabling financial services to contribute to achieving the SDGs. Overall, future FSD will have to react to and find answers to global developments, such as:

- ▶ **Increasing pressure on vulnerable households, small-holder farmers, and MSEs related to climate change**, including more frequent adverse climate effects, food insecurity, and economic development obstacles;
- ▶ **The increasing importance of creating equal economic opportunities and economic inclusion for women** and young people in the global south;
- ▶ **Continuous or increasingly high migration activity**, and its implications on economic development in origin and receiving countries;
- ▶ **Exponentially progressing diversification and expansion of the digital financial services ecosystem** as a key driver for financial inclusion; and
- ▶ **The emergence of technological innovation in economic sectors** like agriculture, forestry, and MSE businesses, including integrated value chain development.

In response to these and other future challenges, SDC and other economic development funders/donors must prioritize interventions. Particularly important for SDC in this regard will be to:

- ▶ **Further acknowledge and promote the crucial role of financial inclusion as an enabler to reach the SDGs.** Although neither all SDGs nor all future challenges have explicit or direct links to FSD, financial inclusion will be a key instrument in paving the way toward coping with emerging obstacles and reaching the SDGs.
- ▶ **Focus overall FSD and financial inclusion efforts and interventions on least-developed countries, particularly in fragile contexts.** This will result in a continuous need to innovate and develop or adapt tailored solutions, particularly those that address increased resilience and economic safety nets. It also includes an emphasis on insurance and savings products.

- ▶ **Emphasize the role of excluded and underserved groups, specifically women and migrants.** In line with the LNOB pledge, these are target groups of FSD and financial inclusion interventions, which acknowledges the different types of barriers to financial inclusion and diverse needs that exist.
- ▶ **Boost engagement in driving forward digitalisation for financial inclusion**, given its immense potential to reach and effectively cater to these target groups through cost-efficient and scalable product and service solutions. To leverage this potential, it also will be key to understand and mitigate the risks and possible new exclusion factors that digitalisation may bring about.

The financial volume of SDC's engagement in FSD is modest compared to that of other international financing institutions or major bilateral donors. SDC must focus on interventions and areas that add value; longer-term perspectives, quality, innovation, and strategic (local) partners; and the capitalisation of its experiences and synergies with likeminded partners. To this extent, SDC and other economic development funders/donors have to bundle and align efforts based on each organisation's strength, with a focus on:

- ▶ **Further strengthening and efficiently coordinating FSD initiatives**, measures, interventions, and activities to ensure that funders focus on filling longstanding gaps in the sector without duplicating efforts. This entails the development of coherent funder strategies; the establishment and steering of coordinated exchange platforms; and the creation and/or strengthening of linkages on various levels to improve networking and information transparency, among other initiatives.
- ▶ **Continuously developing and defining institutional roles and activity profiles within the international cooperation landscape** and among DFIs, IFIs, donors, Microfinance Investment Vehicles, and social and impact investors. SDC faces the continuing challenge of identifying its optimal role vis-à-vis private actors and multi-donor programmes to achieve harmony with other actors and alignment with donor interventions.



FSD GUIDANCE

ANNEXES

Annex I. G20 High-Level Principles for Digital Financial Inclusion

The **G20 High-Level Principles for Digital Financial Inclusion** were developed in 2016 through G20 and international standard-setting body standards and guidance. They build on the success of the **2010 G20 Principles for Innovative Financial Inclusion**, providing a basis for country action plans which reflect country context and national circumstances to leverage the huge potential that digital technologies offer.

Principle 1: Promote a Digital Approach to Financial Inclusion

Promote digital financial services as a priority to drive the development of inclusive financial systems, including through coordinated, monitored, and evaluated national strategies and action plans.

Principle 2: Balance Innovation and Risk to Achieve Digital Financial Inclusion

Balance promoting innovation to achieve digital financial inclusion with identifying, assessing, monitoring, and managing new risk.

Principle 3: Provide an Enabling and Proportionate Legal and Regulatory Framework for Digital Financial Inclusion

Provide an enabling and proportionate legal and regulatory framework for digital financial inclusion, taking into account relevant G20 and international standard-setting body standards and guidance.

Principle 4: Expand the Digital Financial Services Infrastructure Ecosystem

Expand the DFS ecosystem – including financial and information and communications technology infrastructure – for the safe, reliable, and low-cost provision of DFS to all relevant geographical areas, especially underserved rural areas.

Principle 5: Establish Responsible Digital Financial Practices to Protect Consumers

Establish a comprehensive approach to consumer and data protection that focuses on issues of specific relevance to digital financial services.

Principle 6: Strengthen Digital and Financial Literacy and Awareness

Support and evaluate programmes that enhance digital and financial literacy in light of the unique characteristics, advantages, and risks of digital financial services and channels.

Principle 7: Facilitate Customer Identification for Digital Financial Services

Facilitate access to DFS by developing or encouraging the development of customer identity systems, products, and services that are accessible, affordable, and verifiable, and that accommodate multiple needs and risk levels for a risk-based approach to customer due diligence.

Principle 8: Track Digital Financial Inclusion Progress

Track progress on digital financial inclusion through a comprehensive and robust data measurement and evaluation system. This system should leverage new sources of digital data and enable stakeholders to analyse and monitor the supply of – and demand for – digital financial services, as well as assess the impact of key programmes and reforms.

Annex II. Key Platforms and Initiatives

- ▶ Alliance for Financial Inclusion (AFI) www.afi-global.org
- ▶ Better Than Cash Alliance www.betterthancash.org
- ▶ Center for Financial Inclusion (CFI) www.centerforfinancialinclusion.org
- ▶ CERISE www.cerise-spm.org
- ▶ Consultative Group to Assist the Poor (CGAP) www.cgap.org
- ▶ European Microfinance Platform www.e-mfp.eu
- ▶ Financial Alliance for Women www.financialallianceforwomen.org
- ▶ Global Partnership for Financial Inclusion (GPFI) www.gpfi.org
- ▶ Making Finance Work for Africa (MFW4A) www.mfw4a.org
- ▶ Microinsurance Network www.microinsurancenetwerk.org
- ▶ MIX www.themix.org
- ▶ SME Finance Forum www.smefinanceforum.org
- ▶ Social Performance Task Force (SPTF) www.sptf.info
- ▶ UN Capital Development Fund www.uncdf.org
- ▶ Women Entrepreneurs Finance Initiative (We-Fi) www.we-fi.org

Annex III. Glossary of Terms

Access

The availability of affordable and appropriate financial services to a given person. Access is often seen as the goal of financial inclusion; however, access is difficult to measure. Usage is often used as a proxy for access, although usage can underestimate the number of households that have access because it fails to capture those who currently have access to a financial service but are not using it.

Affordability

A characteristic of quality financial services. Describes products for which the price is in line with a client's ability to pay for them. Affordability is considered one of the greatest barriers to access.

Agent

Any third party acting on behalf of a bank, a financial institution, or a non-bank institution (including an e-money issuer or other payment services provider) to deal directly with customers under contractual agreement. The term "agent" is commonly used even if a principal agent relationship does not exist under the regulatory framework in place. Agents can be both banking (small banks) and non-banking correspondents (post offices, gas stations, and mom-and-pop shops).

Agent Banking

Also known as correspondent banking, agent banking is a model for delivering financial services whereby a bank partners with a retail agent (correspondent) to extend financial services in locations where bank branches would be uneconomical. Agent banking is a delivery channel that holds high potential for closing the location gap.

AML/CFT

An acronym for "anti-money laundering/countering the financing of terrorism": policies to detect and reduce money laundering and the financing of terrorism. The term usually refers to the international AML/CFT standards set up by the Financial Action Task Force – an inter-governmental body. While each country can choose how to adapt these international standards, in most countries financial institutions are required to apply certain know your customer (KYC) regulations to all customers, strengthen internal controls, and watch for suspicious transactions. While important, these regulations sometimes create barriers to financial inclusion.

Apex

An apex institution is a second-tier or wholesale organisation that channels funding (grants, loans, guarantees) to financial institutions in a country or region.

Branchless Banking

Banking models and delivery channels that deliver financial services to clients through outlets other than full-service bank branches. Branchless banking refers to mobile banking, correspondent and agent banking, electronic banking, and the use of ATMs. The appeal of branchless banking in the context of financial inclusion is its ability to close the location gap and increase affordability through automation.

Client Protection or Consumer Protection

The effort to ensure fair, responsible, and transparent services for clients. Consumer protection/client protection includes avoiding over-indebtedness, providing transparent and responsible pricing, having appropriate collection practices, exhibiting ethical staff behaviour, having mechanisms for redress of grievances, and keeping client data private.

The Client Protection Pathway

A global effort to embed a set of Client Protection Standards firmly into the practices of the financial service industry, based on the work done for 10 years by the Smart Campaign. SPTF and CERISE manage the CP Pathway as a new initiative to support client protection implementation in the financial service industry. The CP pathway is organized into three steps (1. Commitment to implement, 2. Assessment and implementation, 3. Certification to demonstrate achievement) and SPTF and CERISE are providing guidance, tools and resources for each step to help Financial Service Providers deliver transparent, respectful, and prudent financial services to all clients and ensure that the Client Protection Standards are progressively implemented.

Consumption Smoothing

Reduction in the variability of consumption by households, often through the use of financial services. Consumption smoothing is often cited as a benefit of access to financial services. The majority of the financially excluded are households in which income and consumption are characterised by volatility. Financial services can help poor households who, despite living on less than "\$2 a day," do not actually receive \$2 every day. Savings and loans allow people to tap into past income (through savings) or future income (through loans), helping them smooth consumption. Consumption smoothing can refer to short, medium, or lifecycle time horizons.

Continually Excluded

Individuals who are financially excluded despite progress to date toward financial inclusion. The continually excluded represent groups of people that are most difficult to reach with financial services, such as people with disabilities, rural and remote populations, and extremely poor populations. As financial inclusion pushes out the viability frontier, the continually excluded segment will shrink but it will continue to represent populations that require the most innovation in order to be served financial services.

Core Function

The exchange between demand and supply in a market system. For example, in financial services markets, core function describes the demand for a financial service (e.g., credit, savings, insurance, money transfers) and its supply by the different providers present in the market.

Credit Union

A provider of financial services that is owned by its members under a cooperative form of governance. Credit unions usually provide savings services and loans to their members. They play an important role in financial inclusion because they often have greater presence in rural areas where traditional banks might not be present and because they often offer services at more affordable rates than other financial institutions. Credit unions are known by many names around the world, including cooperatives, cajas (in many Latin American countries), and savings and credit cooperatives (SACCOs) (throughout Africa).

Customer Due Diligence

Often used synonymously with KYC measures, customer due diligence generally refers more broadly to the policies and procedures used by a digital financial services provider to obtain customer information and assess the risks of money laundering and the financing of terrorism posed by a customer, including detecting, monitoring, and reporting suspicious activities.

Delivery Channel

A method of providing products or services. Examples of delivery channels include traditional banking outlets such as bank branches and ATMs, or branchless banking channels such as mobile banking and agent banking.

Digital Financial Inclusion

The use and promotion of digital financial services (DFS) to advance financial inclusion. The essential components of digital financial inclusion are a digital transactional platform, a device used by the customer to electronically connect to the platform and perform financial transactions, the use of retail agents for the customer to transact from, and provision of a wide range of financial products and services.

Digital Financial Services

The broad range of financial services accessed and delivered through digital channels, including payments, credit, savings, remittances, and insurance. The digital financial services (DFS) concept includes mobile financial services. In this context, the term “digital channels” refers to the internet, mobile phones (both smartphones and digital feature phones), ATMs, POS terminals, Near Field Communication-enabled devices, chips, electronically enabled cards, biometric devices, tablets, phablets, and any other digital system. DFS models usually employ agents and the networks of other third-party intermediaries to improve accessibility and lower the overall service delivery cost.

Drivers of Change

A catalyst or agent of (systemic) change or reform. Drivers of change may be individuals or institutional champions of reform, or the product of the interaction among structural features, formal and informal institutions, and individuals that give rise to a process of reform.

Electronic Money (e-money)

A type of monetary value electronically stored and generally understood to have the following four attributes: (i) issued upon receipt of funds in an amount no lesser in value than the value of the e-money issued and in the same currency; (ii) stored on an electronic device, whether SIM-enabled or not (e.g., a chip, pre-paid card, mobile phone, tablet, phablet, or any other computer system); (iii) accepted as a means of payment by parties other than the issuer; and (iv) convertible into cash.

Electronic Wallet (e-wallet)

A place to store electronic money to allow rapid and secure electronic transactions. An electronic wallet can take the form of a smart card or a mobile phone. E-wallets allow individuals to store money in a secure place even if they do not have a bank account. In addition, e-wallet users can pay for certain products and services without carrying cash, making e-wallets an alternative and safe way to transport money.

Financial Capability

The combination of knowledge, understanding, skills, attitudes, and especially behaviours that people need to make the sound personal finance decisions most suited to their social and financial circumstances.

Financial Deepening

The process of increasing financial intermediation or engagement within the financial system. For example, an increase in the amount and number of deposits in the financial system would indicate financial deepening. Financial deepening is sometimes used as a synonym for financial inclusion, however, it is important to note that the two concepts are not the same. Deepening can happen without financial inclusion if volumes of financial flows increase while only a fraction of the population participates.

Financial Education

The provision of education on the use of financial services. Financial education is important in the context of financial inclusion because as previously excluded populations gain access to formal financial services, they need to be able to use these services in a productive and responsible manner that will not cause them harm. Financial education may be provided by schools, financial institutions, and other members of the financial sector's infrastructure – through channels ranging from classrooms and mass media to social media, technology, and direct contact with financial institution staff.

Financial Identity

Identification pertinent to a specific individual's financial activity that is linked to the individual's financial records and accounts. Account numbers, PIN numbers, passwords, and information on account balances and past transactions are all part of an individual's financial identity. Since a lack of financial identity may be a barrier to access to financial services, the provision of financial identity may provide an entry for those previously excluded.

Financial Inclusion

A state where both individuals and businesses have opportunities to access and the ability to use a range of appropriate financial services that are responsibly and sustainably provided by formal financial institutions.

Financial Literacy

The ability to understand how to use financial products and services and how to manage personal, household, or micro-enterprise finances over time. Improvements in financial literacy levels can be achieved through financial education.

Financial Safety Nets

It is a comprehensive portfolio of measures that helps in reducing risk. A financial safety net is meant to protect households, at least in part, from losing financial security or derailing financial goals. This is especially true in the case of some unexpected event, such as an illness or personal tragedy. An emergency fund is a common part of a financial safety net. This means having enough savings to meet ends. Having insurance policies in place can also be an important factor.

Fintech

FinTech is an abbreviation combining the terms 'financial' and 'technology' or 'financial technologies'. The field of FinTech in the broad sense brings together all the companies implementing innovative solutions aimed at improving and automating the delivery and use of financial services.

Formal Financial Services Provider

An institution that provides formal financial services, is formally recognised by the government, and is often (but not necessarily) regulated. Formal financial services providers include commercial banks, state banks, rural/agricultural banks, savings banks, and non-bank finance institutions. Other financial institutions, such as microfinance NGOs and credit unions, can be considered formal financial services providers despite not always being regulated.

Full Suite of Basic Financial Services

A group of core financial services that includes basic credit, savings, insurance, and payment services. These four services serve the different needs that households encounter, and ensuring access to this product range is an important goal of financial inclusion. Credit allows households to use future income to manage current vulnerabilities or to capitalize on investment opportunities. Savings provide a safe and value-retaining place where households can store funds, allowing them to tap into "past income" as needed. Insurance protects against vulnerability to shocks (e.g., death, illness, disability in the family). Payment services allow people to carry out financial transactions without having to be face-to-face.

Greenfielding

The 'Greenfield approach' describes the foundation of a financial institution with the specific purpose of offering regulated formal financial services to the poor from the very start. As the name suggests, the bank is founded on the green field without any pre-existing infrastructure, staff or clients. The foundation is often processed by international holding companies in which the sponsor or primary shareholder provides the technical expertise while other like-minded investors, including development finance institutions and bilateral donor institutions, provide various forms of funding (Ledgerwood 2013).

Informal Economy

A segment of economic activity that is not controlled, supervised, or taxed by the government. The informal economy is where the majority of excluded populations conduct their personal and work-related transactions.

Informal Financial Services Provider

An unregulated provider of financial services, generally not legally registered with the government. Informal financial services providers may include moneylenders, pawnbrokers, rotating savings and credit associations (ROSCAs), and accumulating savings and credit associations (ASCAs). Informal financial services providers usually are characterised by their community-based nature and informality. Their services can be convenient but may be costly and unreliable. (ROSCAs and ASCAs are sometimes categorized as informal services providers although the debate on how to categorize them continues.)

Insurtech

Insurtech is a combination of the words 'insurance' and 'technology'. In the insurance sector, Insurtechs are the equivalent of FinTechs. It brings together all the companies implementing innovative solutions aimed at improving or rethinking the insurance sector.

Know Your Customer

Regulation that requires all financial institutions to ensure that they validate the identity of all clients. Know your customer (KYC) regulation is part of the AML/CFT standards, and, while important, can sometimes create barriers to financial inclusion. For example, new KYC regulations require that providers review new client identity documents (e.g., a passport, identification card, employment documentation), which many financially excluded clients lack.

Location Gap

When the distance between a potential user of a financial service and the nearest location where he or she can access the service creates a barrier to access. The location gap is an important challenge in the context of financial inclusion. In many countries, most of the financially excluded are in rural areas that are too far from the nearest banking outlet. Alternative delivery channels can help to close the location gap.

Market Actor

Any organisation or individual that performs a function in a market system. Market actors can be private- or public-sector organisations. The main types of market actors in financial services markets include clients, FSPs, technical service providers, policy makers, regulators, and supervisors.

Market Functions

A market system has three key market functions: (i) the core function, (ii) supporting functions, and (iii) rules and norms. When designing an intervention, funders should consider which function(s) the intervention will affect, who currently performs that function, who currently pays for it, and how these parameters will change through the intervention.

Market System

The interaction of multiple market actors performing multiple market functions, including the core function (e.g., the demand and supply of financial services), supporting functions, and rules and norms. The term "market system" is broadly used to describe the complex and dynamic interactions between all market actors, including private- and public-sector actors.

Market Systems Approach

A combination of frameworks, principles, and practices that can be used to frame development interventions that lead toward systemic change rather than fill a void in the market. Historically used in other sectors (e.g., agriculture value chains), the market systems approach has increasingly gained the interest of funders and practitioners in financial inclusion.

Microcredit

The provision of small loans to the poor. Microcredit generally refers to small working capital loans but can also mean any small credit given to a low-income individual/entrepreneur. Microcredit, in its modern form, began in the 1970s in several places around the world under different lending methodologies, including group lending and village banking. The microcredit movement made the important contribution of proving that the poor can use credit and repay, despite their small and volatile income and lack of traditional collateral. The microcredit sector soon gave way to the microfinance industry, which strives to provide not only credit but savings, microinsurance, and other financial services to the poor. Today the microfinance industry is one of the main advocates pushing for full financial inclusion.

Microfinance

The provision of financial products and services focused on serving low-income clients who often lack access to other forms of formal financial services. Although sometimes used as a synonym for microcredit, microfinance refers to the provision of services beyond credit, including savings, insurance, and payments. Microfinance as an industry evolved from the first microcredit pilots a few decades ago which proved that the poor need and can use financial services. The industry is rooted in and advocates the use of financial services in a way that enhances and does not harm the lives of its low-income clients. Despite its rapid growth, over 2 billion people still lack access to financial services, and this has inspired the more recent push for financial inclusion.

Microfinance as a Platform

The use of microfinance as a channel for increasing access to non-financial products and services that improve lives, such as business development, health, energy, or education. Financial institutions can play this role in at least three ways, including: (i) by providing specialized loans and insurance (e.g., an education loan, health insurance, or a loan to purchase a solar lamp); (ii) by facilitating marketing and distribution of products to the institution's clients; and (iii) by micro-franchising to provide clients with the training and resources necessary to become a retailer of non-financial products.

Microfinance Plus

The combination of microfinance with the provision of supplementary non-financial services or products that can enhance a client's livelihood or quality of life. An example of microfinance plus includes the provision of health education during a meeting between a loan officer and a borrower group.

Microinsurance

Insurance products specifically designed for the needs of low-income households and often characterised by very low premiums, small payouts, and very simple claims mechanisms.

Mobile Banking

The provision of financial services via mobile phone. Mobile banking is an alternative delivery channel that supports payment transactions, including money transfers and, in some cases, loan repayments. Because in many developing countries mobile penetration is growing faster than the penetration of financial services, many point to mobile banking as a possible way to decrease the location gap and increase financial inclusion.

Mobile Money

A type of electronic money (e-money) that is transferred electronically using mobile networks and SIM-enabled devices, primarily mobile phones. The issuer of mobile money may be an MNO, a financial institution, or another licensed third-party provider, depending on local laws and the business model.

Non-Bank Financial Institution

Different from a bank, a non-bank financial institution (NBFI) is a financial institution that is allowed to provide certain financial services by virtue of the regulatory framework in place. NBFIs usually operate under a license (following a registration procedure) or based on "letters of no objection" from the regulator. One common example of an NBFI is an MNO or an entity established by an MNO to provide a limited range of financial services. NBFIs are usually subject to lighter prudential regulation than banks.

Over-indebtedness

A state in which a borrower's debt service obligations are so high that they require the borrower to make sacrifices in basic quality of life. Over-indebtedness can arise from excessive borrowing (especially from multiple institutions) or from unpredictable events or vulnerability. Over-indebtedness can be temporary or chronic.

Privacy of Client Data

A Client Protection Principle which states that the privacy of individual client data will be respected in accordance with the laws and regulations of individual jurisdictions, and that such data cannot be used for other purposes without the express permission of the client. This principle recognises that providers of financial services can play an important role in helping clients achieve the benefits of establishing a credit history.

Product Bundling

A condition in which two or more products are sold together in one package. For example, some microfinance institutions bundle a loan with a savings account; to be approved for a loan, the client must open a savings account. Loans are often bundled with credit life insurance. Product bundling can also be voluntary. Product bundling can generate cost savings for a provider and increase product affordability but can discourage customers who desire greater freedom to choose which products they use.

Quality

One of the four dimensions of the Center for Financial Inclusion's vision of financial inclusion, describing how financial services are provided. Quality financial inclusion includes the following traits: affordability, convenience, product fit, safety, dignity of treatment, and client protection. Quality refers to product design and delivery traits that enhance the value of services to clients.

Redress of Grievance

A Client Protection Principle which states that providers will have in place timely and responsive mechanisms for resolving complaints and problems of individual clients.

Remittances

Funds, generally a portion of a salary, that are transferred from one individual to another. International remittances are funds transferred by a foreign worker to his/her home country, while domestic remittances are funds within one nation – generally from a worker in an urban area to a household in a rural area.

Rules and Norms

Rules and norms shape incentives for market actors and determine who can participate in financial services markets and under what conditions. Formal rules include laws and regulations issued by the legislator and public authorities (e.g., banking regulation, licensing criteria for MFIs, KYC procedures). They also include rules issued by industry bodies (e.g., industry standards, codes of conduct). Informal rules are the product of local culture and generally accepted practices.

Supporting Functions

A range of functions that falls outside of the core exchange of a market system but significantly affects the strength or weakness of that market. These functions support, shape, inform, and enable transactions between demand and supply. Important supporting functions in financial services markets include information, coordination, skills and capacity, payment systems, and funding. Supporting functions are necessary for markets to work efficiently, ensuring that demand and supply for financial services match and transactions can take place in a secure manner and at the lowest possible transaction costs. In weak market systems, supporting functions tend to be absent, dysfunctional, or discriminate against the poor. Supporting functions can be provided by a variety of actors from the private, public, or associative sector.

Systemic Change

A change in the underlying dynamics and structures of how a market system works that is significant in scale, sustainable, and resilient. Systemic change occurs if market actors beyond those directly involved in a funder's intervention adopt a new behaviour that improves the poor's participation in financial services markets. Also referred to as system-level change or market systems change.

Annex IV. Selected Readings and Links

The following annotated bibliography contains a small selection of published and unpublished literature relating to the financial sector, which focuses on lessons learned from experience and good practices. The list is not exhaustive.

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