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UNDERSTANDING
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NO 15

FINANCIAL INCLUSION IN NIGERIA

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Aims and Scope

Understanding Monetary Policy Series is designed to improve monetary policy communication and economic literacy. The series attempt to bring the technical aspects of monetary policy closer to the critical stakeholders who may not have had formal training in Monetary Management. The contents of the publication are therefore, intended for general information only. While necessary care was taken to ensure the inclusion of information in the publication to aid proper understanding of the monetary policy process and concepts, the Bank would not be liable for the interpretation or application of any piece of information contained herein.

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Central Bank of Nigeria

Mandate

▪Ensure Monetary and Price Stability

▪Issue Legal Tender Currency in Nigeria

▪Maintain External Reserves to safeguard the international value of the Legal Tender Currency

▪Promote a Sound Financial System in Nigeria

▪Act as Banker and Provide Economic and Financial Advice to the Federal Government

Vision

"To be a people-focused Central Bank promoting confidence in the economy and enabling an improved standard of living"

Mission Statement

"To **ENSURE** Monetary, Price and Financial System Stability as a Catalyst for Inclusive Growth and Sustainable Economic Development."

Core Values

Integrity

Partnership

Accountability

Courage

Tenacity

MONETARY POLICY DEPARTMENT

Mandate

To Facilitate the Conceptualization and Design of Monetary Policy of the Central Bank of Nigeria

Vision

To be Efficient and Effective in Promoting the Attainment and Sustenance of Monetary and Price Stability Objective of the Central Bank of Nigeria

Mission

To Provide a Dynamic Evidence-based Analytical Framework for the Formulation and Implementation of Monetary Policy for Optimal Economic Growth

FOREWORD

The Understanding Monetary Policy Series is designed to support the communication of monetary policy by the Central Bank of Nigeria (CBN). The series therefore, explain the basic concepts/operations, required to effectively understand the monetary policy framework of the Bank.

Monetary policy remains a very vague subject area to the vast majority of people in spite of the abundance of literature on the subject, most of which tend to adopt a formal and rigorous professional approach, typical of macroeconomic analysis.

In this series, public policy makers, policy analysts, businessmen, politicians, public sector administrators and other professionals, who are keen to learn the basic concepts of monetary policy and some technical aspects of central banking, would be treated to a menu of key monetary policy subject areas that will enrich their knowledge base of the key issues.

In order to achieve the primary objective of the series therefore, our target audience include people with little or no knowledge of macroeconomics and the science of central banking and yet are keen to follow the debate on monetary policy issues, and have a vision to extract beneficial information from the process. Others include those whose discussions of the central bank makes them crucial stakeholders. The series will therefore, be useful not only to policy makers, businessmen, academicians and investors, but to a wide range of people from all walks of life.

As a central bank, we hope that this series will help improve the level of literacy on monetary policy and demystify the general idea surrounding monetary policy formulation. We welcome insights from the public as we look forward to delivering contents that directly address the requirements of our readers and to ensure that the series are constantly updated, widely read and readily available to stakeholders.

Hassan Mahmud, Ph.D
Director, Monetary Policy Department
Central Bank of Nigeria

CONTENTS

UNDERSTANDING FINANCIAL INCLUSION IN NIGERIA[1]

Oyebanji J. Olaoye [2]

Abstract

The banking industry has witnessed considerable growth both in outreach and the number of products. The Structural Adjustment Programme (SAP) introduced various reform measures which helped increase the number and spread of financial institutions operating in the country. Despite the progress in the banking industry, the level of financial inclusion has remained low. Financial inclusion is the process of ensuring access to useful financial products and services at affordable prices to individuals and corporate entities, including vulnerable groups. Full financial inclusion is attained when all people who require the use of financial services and products have unrestricted access to them at affordable costs, in a convenient manner. This article discussed various conceptual issues, the rationale for financial inclusion, measurement and financial inclusion in Nigeria, challenges in achieving financial inclusion, and conclusion. Financial literacy is critical to the attainment of financial Inclusion, particularly when supported by appropriate consumer protection programmes. Despite the efforts that had been made, the level of financial literacy is still relatively low in Nigeria. The development could be attributed to scattered patterns of settlement of rural dwellers, low patronage of existing bank infrastructure, low income, inadequate physical access, low financial literacy level, and weak confidence in the banking system due to previous cases of bank failures. Development of the Financial Inclusion Strategy Plan for Nigeria in 2012 was a major milestone expected to reduce the proportion of Nigerians excluded from financial services from 46.3 per cent in 2010 to 20.0 per cent by 2020.

[1]This material is designed specifically as an educational material for enlightenment on the monetary policy of the Bank. Consequently, the Central Bank of Nigeria (CBN) does not take responsibility for the accuracy of the contents of this publication as it does not represent the official views or position of the Bank on the subject matter.

[2] This publication was originally authored by **Oyebanji J. Olaoye** in 2013 (Assistant Economist in the Monetary Policy Department, Central Bank of Nigeria) and revised/reviewed in 2021 by **Godfrey U. Uzonwanne** (Principal Manager, Monetary Policy Department, Central Bank of Nigeria)

SECTION ONE

1.0 Introduction

The evolution of the banking industry originated from the activities of goldsmiths in England in early the 17th century. Since then, the industry, which is a significant part of the financial sector, has witnessed considerable growth in processes, outreach, a number of products. In Nigeria, the financial sector has recorded robust growth over time. The Structural Adjustment Programme (SAP), which started in 1986, introduced many reform measures aimed at liberalizing the industry and creating an enabling environment for increased participation. The removal of entry barriers ushered in new entrants to the industry, thereby increasing the number and spread of financial institutions operating in the country. The number of licensed banks increased from 40 in 1985 to about 120 in 1991. In addition, non-bank financial institutions, including finance houses, and primary mortgage institutions were also established to complement the existing infrastructure in the sector. Competition among participants, resulting from the new reforms, led to innovation and development of new products. In general, the emergence of new institutions and products further deepened the financial sector.

This development accelerated the tempo of economic activities, due to the growth in savings and investments. However, a substantial proportion of the population remained out of reach or under-served by the financial system.

Financial inclusion is the process of ensuring access to useful financial products and services by individuals and corporate entities, including vulnerable groups, at affordable prices. Full financial inclusion is attained when everyone who requires the use of financial services and products have unrestricted access to them at affordable cost and in a convenient manner.

The concept of financial inclusion can be viewed from two broad perspectives which are demand and supply. The demand side deals with financial literacy and credit counseling and the Supply-side includes financial markets, banks, and services. Financial literacy is critical to the attainment of financial Inclusion, particularly when supported by appropriate consumer protection programmes. Although significant progress has been made in terms of the number of financial literacy initiatives that have been implemented, the level of financial literacy is still relatively low in Nigeria.

SECTION TWO

Conceptual Issues

2.1 Financial Inclusion

Financial inclusion refers to a state in which people easily have access to appropriate, desired financial products and services to facilitate financial and economic well-being. In promoting access to financial products and services, financial literacy and financial capabilities are essential. Financial capability refers to the knowledge of managing funds, as well as the understanding of financial products, while financial literacy enhances the transfer of knowledge. Financial services and products include the entire gamut of banking, insurance, stock brokerage, pensions, cooperatives, mortgages, and micro-finance services.

The financial system provides the platform for the redistribution of resources from surplus to deficit units in the economy. A sound financial system with a high degree of financial inclusion will reduce the level of poverty substantially. In contrast, financial exclusion is the opposite of financial inclusion, and connotes a situation where individuals and corporate organizations have zero or limited access to financial products and services.

2.2 Service Quality in Financial Inclusion

One of the critical elements of financial inclusion is the provision of quality services, particularly to the poor and majority of rural residents with extremely low levels of infrastructural development. Quality of service delivery in the financial sector involves having timely access to the right products at affordable prices and convenient locations. Therefore, the provision of quality financial services by service providers is required to enhance the achievement of a greater level of financial inclusion. To provide quality services, there is a need for effective and efficient infrastructure to be put in place.

2.3 Financial Services Outreach

The extent of geographical coverage and size of beneficiaries are the major determinants of the rate of financial inclusion. One of the key constraints in extending financial services to rural dwellers is the absence of basic infrastructure such as good road networks, power supply and information & communication technology (ICT) services. These are essential services needed for extending financial services to individuals that are financially excluded. Expansion of financial outreach will further increase the rate of financial inclusion as those people denied access due to non-availability of service in their vicinity will be captured. There is a direct relationship between financial service outreach and the rate of financial inclusion.

2.4 Non-Bank Institutions for Financial Inclusion

Non-bank financial institutions such as cooperative societies, specialized state financial institutions, and deposit-taking microfinance houses with less technical operational procedures are more suitable to deliver financial services to low-income groups. The structure of non-bank financial institutions placed them at an advantage to provide specialized services including financial advice to low-income earners. These institutions are critical to widening the coverage of financial inclusion due to their proximity to rural areas. Organized cooperative societies play intermediary roles by mobilizing funds from members and giving out loans without stringent collateral requirements. These institutions are not operating in silos as mobilized funds are also kept in banks and most of their transactions pass through banks' operations.

SECTION THREE

3.0 The Rationale for Financial Inclusion

3.1 Extension of Financial Services to Rural Areas

Traditionally, financial services are concentrated in urban centers, leaving rural dwellers to rely largely on informal arrangements including families or close relatives for their financial needs. The benefits accruable to a well-functioning financial sector, especially in the rural areas, cannot be over-emphasized. This justifies the need to increase financial penetration to all segments of the population.

Essentially, efforts have been made over the years by various agencies and institutions such as the World Bank, but such efforts have been focused on developing a formal financial sector to mobilize savings and convert them into investments. The major challenge to the realization of extending banking services to rural areas includes: (i) high cost of implementation; (ii) low level of demand and (iii) the ability and willingness of rural dwellers to pay for such services.

3.2 The Increasing Role of Information and Communication Technology (ICT)

Advances in ICT have led to the development of cost-effective ways of building new business models that can accelerate the expansion of financial services in rural areas. As a result, payment infrastructure and services have improved substantially, thereby providing huge opportunities for service providers to design customized financial services and products for both urban and rural dwellers. Technological products such as Global System for Mobile Communication (GSM), internet and mobile payments among others have improved the delivery of financial services significantly in most developing economies.

3.3 Financial Inclusion and Poverty Reduction

Financial inclusion is important for growth, reduction in poverty, and income inequality. Generally, there is a positive correlation between the incidence of poverty and financial exclusion in most regions of the world. Evidence has shown that the largest proportion of the unbanked population resides in developing countries (World Bank, 2009). The extension of modern financial infrastructure to both rural and urban dwellers offers a wide range of opportunities for expanding financial inclusion. The provision of financial services to the deprived and excluded segment of the society could enhance their level of participation in economic activities, thereby enabling them to take advantage of growth opportunities.

3.4 Financial Inclusion and Monetary Policy Effectiveness

One of the objectives of monetary policy is to control the cost and availability of credit and money in the economy. The effectiveness of monetary policy may be undermined if a larger proportion of the population lacks access to formal financial infrastructure. The larger the size of the formal sector the more effective monetary policy is likely to become. Central banks adjust the interest rate to affect aggregate demand. If a higher proportion of economic agents are not in the formal financial system, the effectiveness of such a policy change may be undermined, since higher or lower interest rates can only influence the banked population.

SECTION FOUR

4.0 Measuring Financial Inclusion in Nigeria

There are broadly two approaches to measuring financial Inclusion. These are supply-side measures and demand-side measures. Supply-side measures consider access factors that capture the ability to use formal financial services, while demand-side measures focus on factors that affect the regularity, frequency and length of time taken to utilize formal financial services. Table 1 below shows some of the approaches that have been adopted for measuring financial inclusion.

Table 1: Major Approaches to Measuring Financial Inclusion

Approaches to measuring Financial Inclusion		
Supply-side	**Demand-side**	**Others**
Availability of appropriate financial products. Access factors such as time, distance pricing, and terms. Number of financial access points per 1000 adults. Number of branches per 100 adults. ATMs per 1000 square km Number, type, return, features and monitoring of financial products. Number of loans and deposit accounts per capita.	Per cent of adults with formal accounts. Per cent of adults with formal savings accounts. Per cent of adults with formal credit accounts. Per cent of adults with formal insurance accounts.	Monitoring framework Progress of financial inclusion initiatives by measuring growth/changing patterns of customers and products, the volume of transactions, and returns on products.

From table 1, demand-side measures of financial inclusion take cognizance of factors related to account holder access to financial services. Some of the factors include frequency of use and mode of access, the purpose of the accounts, challenges to accessing the account, and availability of other options. The supply-side measures variables such as the number and appropriateness of financial products; accessibility in terms of time, distance pricing, and terms; number of financial access points including

ATMs and branches per 1000 adults and number of loans and deposit accounts per capita. Other specific measures of financial inclusion are discussed below:

4.1 Ratio of Currency-in-Circulation (CIC) to Money Supply and Gross Domestic Product (GDP)

CIC can be used as an indicator of cash utilization in two ways: first as a share of money supply and second, as a ratio of gross domestic product (GDP) of a country. An increase in the volume of CIC denotes a decrease in total deposits and available loans. This is a major indicator of financial inclusion.

4.2 Ratio of Currency Outside Banks to Money Supply

Currency outside banks represents a proportion of the CIC outside the banking system, held by the public for transactional purposes. It is an indicator of the level of sophistication of the payment infrastructure in an economy.

4.3 Currency Held by Banks and Volume of Deposits/Loans

Currency held by banks refers to the proportion of the CIC that is held in bank vaults. It is the summation of all naira currencies held by Deposit Money Banks, Merchant Banks, and Non-Interest Banks. This is a good indicator of the level of financial inclusion as it captures the volume of money that is available in the bank's vault. A high volume of currency held by banks (deposits) translates to an increased volume of loanable funds in the banking system.

SECTION FIVE

5.0 Financial Inclusion in Nigeria: Banking the Unbanked

Nigeria has made considerable progress in increasing access to financial services. One of the major players in this drive is the CBN. In the Nigerian context, "Financial Inclusion is achieved when all adult Nigerians have unlimited access to a broad range of formal financial services and products that meet their needs at affordable cost" (CBN 2012). Some of such services include payments, savings, loans, insurance, and pension products.

5.1 Key Stakeholders in the Nigeria Financial Inclusion Project

Key stakeholders in the Financial Inclusion project include banks, other financial institutions, insurance, regulators, technology/telecommunications firms, public institutions, and development partners/experts. The banking sector remains the main driver in accelerating financial inclusion given its role as the banker for other economic agents. Broadly, all the key stakeholders in the drive to achieve financial inclusion in Nigeria can be categorized into three:

i. **Providers:** These refer to providers of financial products and services, and their partners who provide the required infrastructure and technological support.
ii. **Enablers:** Enablers refer to regulators and public institutions responsible for setting standards for the achievement of financial inclusion.
iii. **Supporting Institutions:** These include other organizations that assist the regulatory institution in attaining the National Financial Inclusion objectives. Some of these supporting institutions include bilateral and multilateral development partners.

5.2 Nature and Status of Financial Inclusion in Nigeria

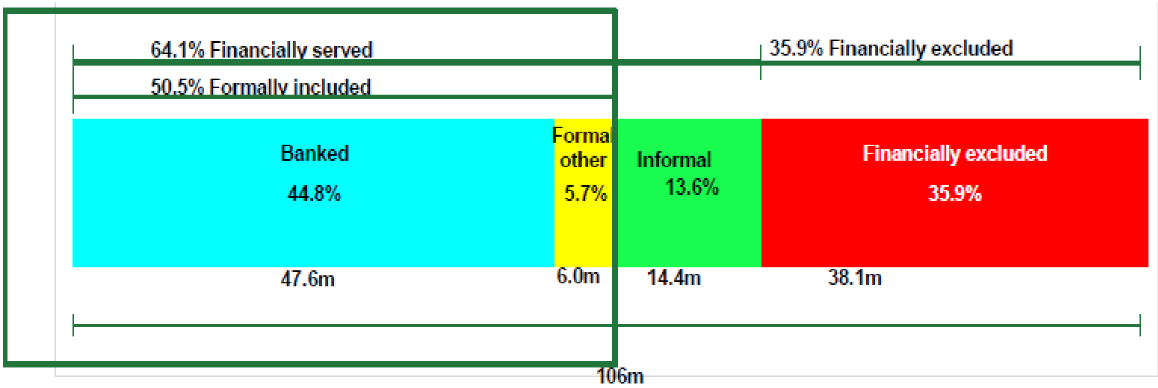
In the Nigerian context of financial inclusion, the following four key issues stand out:

I. Ease of access to financial products and services.
II. Availability of a broad range of financial products and services such as payments, savings, credit, insurance, and pensions products.
III. Designing of financial products according to need; and
IV. Realization of all these at an affordable cost especially for low-income groups.

Access to financial services in Nigeria has improved even though it is still low. As of 2020, about 51.0 per cent (about 51.0 million out of an adult population of 106.0 million) were served by banks and other formal (non-bank) financial services, compared with 91.0 per cent in South Africa and 83.0 per cent in Kenya. Over the same period, the number of adults served informally and excluded from formal financial services stood at about 50 per cent. In terms of gender breakdown, male accounted for about 57 per cent of adults served by banks and other formal channels, while females accounted for the balance.

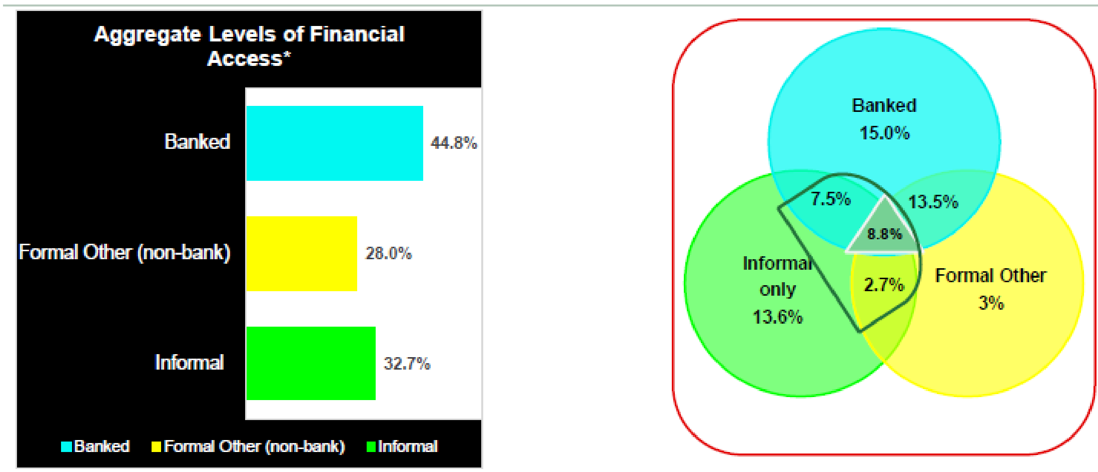
Figures 3 and 4 illustrate the status of financial inclusion in Nigeria as of 2020.

Figure 3: State of Financial Inclusion in Nigeria



Source: Nigeria Financial Inclusion Strategy document 2020

Figure 4: Usage of a Combination of Financial Services



Source: Nigeria Financial Inclusion Strategy document 2020

5.3 Nigeria's Financial Inclusion Strategy Plan

The Financial Inclusion Strategy Plan for Nigeria was developed in 2012 by the CBN with support from development partners and other organizations such as Alliance for Financial Inclusion (AFI), Bangkok; Enhancing Financial Innovation & Access (EFInA), Lagos; and Messrs Roland Berger Strategy Consultants, Germany. The overall objective of the plan is to reduce the proportion of Nigerians that are excluded from financial services from 46.3 per cent in 2010 to 20.0 per cent by 2020. In achieving this objective of the strategy plan, coordinated interventions will focus on the following areas:

I. Transformation of the existing Know-Your-Customer (KYC) regulation into a simplified Risk-based Tiered Framework that allows individuals without the required formal identification measure to enter the banking system.

II. Adoption of a Regulatory Framework for Agent Banking to enable financial institutions to bring banking services to the currently unbanked in all parts of the country.

III. Definition and implementation of a National Financial Literacy Framework to increase the awareness and understanding of the citizenry on financial products and services, with the goal of increasing sustainable usage.

IV. Implementation of a comprehensive Consumer Protection Framework to safeguard the interest of clients and sustain confidence in the financial sector.

V. Continued pursuance of Mobile-Payment System and other Cash-less Policy efforts to lessen the cost and enhance the ease of financial services and transactions.

VI. Implementation of Credit Enhancement Schemes/Programmes.

SECTION SIX

6.0 Challenges of Achieving Financial Inclusion in Nigeria

Five major barriers to Financial Inclusion have been identified to include: low and irregular income, lack of physical access, low level of financial literacy, the problem of affordability and eligibility. In addition, weak confidence in the banking system due to cases of bank failures in the past discourages people from embracing financial inclusion in Nigeria.

6.1 Scattered Settlement Pattern of Rural Dwellers

The scattered settlement pattern of rural dwellers in Nigeria remains a major impediment in the drive to achieve financial inclusion due to the difficulty and high cost of reaching customers. By their structure, non-bank institutions such as cooperatives, specialized financial institutions, and microfinance institutions are better placed to serve the rural population with customized financial services and products.

6.2 Underutilization of Banking Infrastructure

Low patronage of existing banking infrastructure is a major challenge to achieving financial inclusion in Nigeria. Available evidence has shown gross under-utilization of banking services and products. Despite the phenomenal growth in banking activities, evidenced by a large number of bank branches, ATMs, and POS terminals (5,797 bank branches, 9,958 ATMs, and 11,223 POS terminals in 2010), the average number of clients per branch is only 3,882 compared with 3,922 in Kenya and 8,595 in Tanzania. In this regard, the creation of awareness and increased confidence by clients in the banking system is critical towards deepening financial inclusion in Nigeria.

SECTION SEVEN

7.0 Conclusion

Financial Inclusion is an essential prerequisite for the attainment of sustainable growth and development in Nigeria. Although significant progress has been made in terms of the number of financial literacy initiatives that have been implemented, the level of financial literacy remains low. This is due to many factors including scattered settlement patterns of rural dwellers, low patronage of existing bank infrastructure, low income, inadequate physical access, low financial literacy level, and weak confidence in the banking system due to previous cases of bank failures. The development of the Financial Inclusion Strategy Plan for Nigeria in 2012 was a major milestone that is expected to reduce the proportion of Nigerians that are excluded from financial services from 46.3 per cent in 2010 to 20.0 per cent by 2020.

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