

"Closing the Divide through Women's Access to Finance "

Introduction

Financial inclusion is the access individuals and businesses have to useful and affordable financial products and services that meet their needs, such as for transactions, payments, savings, credit and insurance. They also must be delivered in a responsible and sustainable way¹ promoting engagement in the formal financial sector.² Access to affordable finance aims to enhance living standards³, increase income, stimulate business investment, reduce unemployment⁴, and foster economic growth⁵ by expanding financial networks⁶ and reducing barriers to entry.

Thus, enhancing women's financial inclusion is crucial because women are disproportionately affected by poverty due to unequal work division and limited control over economic resources.⁷

One of the main ways to increase access to financial services is through digitalization. Digital financial inclusion is “the deployment of cost-saving digital means to reach financially excluded and underserved populations with a range of formal financial services suited to their needs that are responsibly delivered at a cost affordable to customers and sustainable for providers”.⁸

In this brief we cover three main enablers of financial inclusion:

¹ “Financial Inclusion,” World Bank, March 29, 2022, <https://www.worldbank.org/en/topic/financialinclusion/overview>.

² “National Financial Inclusion Strategy of Sri Lanka: ‘Better Quality Inclusion for Better Lives.’” Central Bank of Sri Lanka, 2021. https://www.cbsl.gov.lk/sites/default/files/cbslweb_documents/publications/annual_report/2021/en/1_Preliminary.pdf

³ Ibid

⁴ Loan Thi-Hong Van, Anh The Vo, Nhan Thien Nguyen & Duc Hong Vo (2021) Financial Inclusion and Economic GROWTH: An International Evidence, *Emerging Markets Finance and Trade*, 57:1, 239-263, DOI: 10.1080/1540496X.2019.1697672

⁵ Mehrotra, Aaron N. and Yetman, James, Financial Inclusion - Issues for Central Banks (March 2015). *BIS Quarterly Review* March 2015, Available at SSRN: <https://ssrn.com/abstract=2580310>

⁶ Loan Thi-Hong Van, Anh The Vo, Nhan Thien Nguyen & Duc Hong Vo (2021) Financial Inclusion and Economic GROWTH: An International Evidence, *Emerging Markets Finance and Trade*, 57:1, 239-263, DOI: 10.1080/1540496X.2019.1697672

⁷ Holloway, Kyle, Zahra Niazi, and Rebecca Rouse. Rep. Women's Economic Empowerment Through Financial Inclusion A Review of Existing Evidence and Remaining Knowledge Gaps. *Innovations for Poverty Action*, March 2017. <https://poverty-action.org/sites/default/files/publications/Womens-Economic-Empowerment-Through-Financial-Inclusion-Web.pdf>

⁸ “Digital Financial Inclusion”, World Bank, March 14th 2024, <https://www.worldbank.org/en/topic/financialinclusion/publication/digital-financial-inclusion>

1. Financial and Digital Literacy

Financial literacy encompasses knowledge, attitudes, and behaviour crucial for informed financial decisions and well-being. Despite having a high literacy rate of 93.3%⁹, the level of financial literacy is only 57.9%¹⁰. The lack of financial education¹¹ leads to poor financial decisions and cycles of debt and poverty.¹²

Digital literacy as defined by UNESCO is the ability to access, manage, understand, integrate, communicate, evaluate and create information safely and appropriately through digital technologies for employment, decent jobs and entrepreneurship. It includes competencies that are variously referred to as computer literacy, ICT literacy, information literacy and media literacy.¹³ Despite a 57.2% digital literacy rate in Sri Lanka, only 44.5% use digital devices to search the internet and 17.8% to send emails¹⁴ due to the technology adoption hurdle and lack of technical knowhow. This is only one example of the lack of overall digital literacy in Sri Lanka. It shows that even with access to a digital device, many people lack the skills to use those devices.

The lack of financial literacy leads to over reliance on informal financial services. For women entrepreneurs at the micro level, low financial literacy leads to challenges in preparing documentation and business proposals required to access financing from formal financial institutions.

2. Digital Infrastructure

Despite having digital payment systems such as ‘Just Pay’ and ‘Lanka QR’ in Sri Lanka, the services are not promoted and the uptake is low as consumers are more comfortable with cash payments.¹⁵ The limited adoption of digital payment methods such as credit

⁹ Labour Force Survey 2021

¹⁰ Financial Literacy Survey Sri Lanka 2021

¹¹ “Sri Lankans Now Have Access to Free Financial Education to Take Control of Their Financial Future.” Asia Securities, March 15, 2022. . Available at <https://www.asiasecurities.lk/news-room-article/sri-lankans-now-have-access-to-free-financial-education-to-take-control-of-their-financial-future>.

¹² Ibid.

¹³ (2018) *A global framework of reference on Digital Literacy Skills For ...* - UNESCO. Available at: <https://uis.unesco.org/sites/default/files/documents/ip51-global-framework-reference-digital-literacy-skills-2018-en.pdf>.

¹⁴ *Sri Lanka Labour Force Survey Annual Report - 2021* (2021) Department of Census and Statistics. Available at: <http://www.statistics.gov.lk/LabourForce/StaticallInformation/AnnualReports/2021>.

¹⁵ Hewawasam, P.C., Khatibi, A. and Azam, S.M.F. (2023) *Sri Lankan Consumers' recommendations of QR code -enabled payment ...* Available at:

cards, debit cards, online bank transfers, and FinTech solutions can be attributed to citizens' lack of trust and awareness. This impedes the growth and sustainability of digital entrepreneurship in the country.

An important factor in the development of the digital payment landscape is the introduction of digital identification systems (Digital ID). This facilitates the opening of bank accounts by reducing the time and cost of onboarding customers, thereby boosting financial inclusion and lowering the cost of financial services.

The development of an interoperable payments interface is vital for the expansion of digital financial services. According to the National Payments Corporation of India (NPCI), the Unified Payments Interface (UPI) in India powers multiple bank accounts into a single mobile application (of any participating bank), merging several banking features, seamless fund routing and merchant payments into one hood” (NCPI 2024).¹⁶

A few years ago, India also unveiled the Account Aggregator (AA) network: “a financial data-sharing system that could revolutionize investing and credit, giving millions of consumers greater access and control over their financial records and expanding the potential pool of customers for lenders and fintech companies”.¹⁷

3. Enabling Environment

As of March 2020, Sri Lanka had 16.6 bank branches per 100,000 adults, almost double the South Asian regional average of 9.4.¹⁸ Although there is wide network of financial institutions there is insufficient access to banking and financial services¹⁹ which prompts a significant portion of the population to engage in high-risk informal transactions.²⁰ The NFI

https://www.researchgate.net/publication/367768300_Sri_Lankan_Consumers'_Recommendations_Of_Qr_Code_Enabled_Payment_Solutions_To_Create_A_Cashless_Society_Do_Moderating_Variables_Collaborate.

¹⁶ UPI: Unified Payments Interface - instant mobile payments: NPCI (no date) National Payments Corporation of India (NPCI). Available at: <https://www.npci.org.in/what-we-do/upi/product-overview> (Accessed: 18 March 2024).

¹⁷ 'Know all about Account Aggregator Network- a financial data-sharing system' (2021) Government of India Press Information Bureau [Preprint]. Available at: <https://pib.gov.in/PressReleaseIframePage.aspx?PRID=1753713> (Accessed: 14 March 2024).

¹⁸ *National Financial Inclusion Strategy for Sri Lanka (2021-2024)*. Central Bank of Sri Lanka (CBSL), technical and financial assistance from the International Financial Corporation in partnership with the Government of Australia, 2021. https://www.rdd.cbsl.lk/images/pdf/NFISofSriLanka_English.pdf.

¹⁹ Kumari, D.A.T. Financial Inclusion and Its Impact on Inclusive Growth: The Macroeconomic Perspective in Sri Lanka, 2021. <https://storage.googleapis.com/jnl-sljo-j-aeb-files/journals/1/articles/29/submission/proof/29-1-55-1-10-20211119.pdf>.

²⁰ Ibid.

Survey indicates that 62% of women rely on the informal sector for borrowing.²¹

According to the Ministry of Finance, there are around 11,000 microfinance institutions in Sri Lanka of which only four are registered with the Central Bank.²² Unregulated microfinance in Sri Lanka often involve illegal deposit mobilization²³, exploits vulnerable customers, especially women, through excessive interest rates and unethical practices.²⁴ Poor corporate governance leads to financial distress, high interest rates (up to 70%), and severe debt²⁵, causing reduced savings, stress, and asset pawning.²⁶ This exploitation, including harassment and humiliation (90% of victims being women), and even suicides,²⁷ eroding confidence in the financial sector, perpetuating poverty cycles and impacting the country's financial stability, contrary to the Central Bank of Sri Lanka's objectives.

Currently, the microfinance sector of Sri Lanka is regulated through the Microfinance Act No. 6 of 2016. The Act provides for the licensing, regulation and supervision of companies carrying on microfinance business, which are called licensed microfinance companies (LMFCs). (Central Bank of Sri Lanka).²⁸ To address gaps in the existing Act, a new Microfinance and Credit Regulatory Authority Bill was gazetted in January 2024.²⁹ The bill has been criticised for not adequately addressing the “extortive and predatory practices of microfinance lenders” and for excluding some entities from the

²¹WOMEN MATTER! FINDINGS FROM SRI LANKA'S NATIONAL FINANCIAL INCLUSION SURVEY 2018/19, 2019. <https://documents1.worldbank.org/curated/en/484581587110814426/pdf/Women-Matter-Findings-from-Sri-Lanka-s-National-Financial-Inclusion-Survey-2018-19.pdf>.

²²Sirimanna, B. (2024) Sri Lanka's microfinance bill under fire from community groups, The Sunday Times. Available at: <https://www.sundaytimes.lk/240218/business-times/sri-lankas-microfinance-bill-under-fire-from-community-groups-548896.html#:~:text=Sri%20Lanka%27s%20microfinance%20and%20credit,practices%20at%20the%20grassroots%20level>. (Accessed: 14 March 2024).

²³Illegal deposit mobilization is the unauthorized and illicit gathering of funds from the public, with the promise of returns or interest. It entails individuals or entities collecting deposits without securing the required approvals or licenses from regulatory authorities.

²⁴Siriwardana, Thusitha. “Microfinance: Addressing a Social Disaster.” Groundviews, December 26, 2022. <https://groundviews.org/2022/12/26/microfinance-addressing-a-social-disaster-in-sri-lanka/>.

²⁵PERAMPALAM, SUTHAHARAN, and MITHULA GUGANESHAN. “What's Ailing Sri Lanka's Microfinance Industry – And Could Fintech Provide a Solution?” NextBillion, 2018. <https://nextbillion.net/whats-ailing-sri-lankas-microcredit-industry-and-could-fintech-provide-a-solution/>.

²⁶ Ibid.

²⁷ Ibid.

²⁸Microfinance sector: Central Bank of Sri Lanka (no date) Microfinance Sector | Central Bank of Sri Lanka. Available at: [https://www.cbsl.gov.lk/en/financial-system/financial-system-stability/microfinance-sector#:~:text=The%20Microfinance%20Act%20No%206%20of%202016&text=The%20Act%20provides%20for%20the,Lanka%20\(the%20Monetary%20Board\)](https://www.cbsl.gov.lk/en/financial-system/financial-system-stability/microfinance-sector#:~:text=The%20Microfinance%20Act%20No%206%20of%202016&text=The%20Act%20provides%20for%20the,Lanka%20(the%20Monetary%20Board)). (Accessed: 19 March 2024).

²⁹Rajawasam, N. (2024) Sri Lanka's new microfinance bill to be presented to Parliament Next Week, EconomyNext. Available at: <https://economynext.com/sri-lankas-new-microfinance-bill-to-be-presented-to-parliament-next-week-146159/> (Accessed: 14 March 2024).

purview of this Act.³⁰

A survey conducted by UNDP states that 44% of the total population are deprived in terms of the debt status indicator. Additionally, the debt status (18%) is the highest contributor to overall multidimensional vulnerability In Sri Lanka.³¹

Strong financial consumer protection is also essential for financial inclusion. Ongoing technological progress, rising complexity in financial services, and increased competition among market players have led financial regulators to prioritize consumer awareness and the effectiveness of consumer protection frameworks.³² However, customers lack awareness of proper complaint procedures against financial entities, and there's a deficiency in a transparent and comprehensive complaint redress framework for financial consumers.³³ These issues result in delayed complaint resolutions, negatively affecting the reputation of both individual financial entities and regulators.³⁴ Insufficient comprehension of risks linked to digital products exposes consumers to unfair and faulty practices.³⁵

The Central Bank of Sri Lanka (CBSL) issued the Financial Consumer Protection Regulations No. 01 of 2023 under Section 10(c) of the Monetary Law Act, No. 58 of 1949. The regulations aim to ensure that individuals and businesses dealing with financial products and services of regulated financial institutions are treated in a fair and transparent manner with improved service level enabling them to take well informed decisions on their finance activities with more confidence (Central Bank of Sri Lanka). Speedy implementation of these regulations is vital.

5. Policy Recommendations

Financial and Digital Literacy

³⁰ (No date) *TISL challenges anti-corruption bill in Supreme Court – the island*. Available at: <https://island.lk/tisl-challenges-anti-corruption-bill-in-supreme-court/> (Accessed: 19 March 2024).

³¹ *Understanding multidimensional vulnerabilities: Impact on people of Sri Lanka* (no date) UNDP. Available at: <https://www.undp.org/srilanka/mvi> (Accessed: 18 March 2024).

³² *Financial Consumer Protection Framework: A Way Forward* (no date) Central Bank of Sri Lanka. Available at: https://www.cbsl.gov.lk/sites/default/files/cbslweb_documents/publications/annual_report/2022/en/13_Box_11.pdf (Accessed: 14 March 2024).

³³ Thennakoon, Nishadi, Financial Consumer Protection is not a Destination, it's a Journey (June 17, 2020). Daily FT Sri Lanka, 2020, Available at SSRN: <https://ssrn.com/abstract=3629024>

³⁴ Ibid

³⁵ Ibid

- Financial literacy courses should be integrated into school curricula, covering global and local financial innovations.
- Restructuring the school IT syllabus could promote digital literacy by equipping them with essential skills such as accessing digital financial services and the knowledge to effectively use digital devices.
- Implement programmes like “Suhuruliya”, which promotes ICT capacity development for women entrepreneurs and key stakeholders including government officials, private sector, civil society groups and media.

Digital Infrastructure

Develop a unique digital identity to be used to access government services, financial transactions, and other services.

- Develop a standardised universal payment interface that can be used across financial institutions which is easily accessible through mobile apps, websites, and physical payment terminals.

Enabling Environment

- Lack of a comprehensive national policy on microfinance is a challenge.³⁶ Regulation should cover all entities in the microfinance sector to ensure legal recognition and protection for customers.³⁷
- A strong consumer protection framework, along with extensive financial inclusion and education initiatives, is crucial. Providing customers with relevant and updated information empowers them to make informed choices about financial products and services, protecting them from deceptive practices. Delays in responses to complaints must also be minimized.³⁸
- Developing the skills of financial institution employees will enhance consumer protection frameworks.

³⁶Siriwardana, Thusitha. “Microfinance: Addressing a Social Disaster.” Groundviews, December 26, 2022. <https://groundviews.org/2022/12/26/microfinance-addressing-a-social-disaster-in-sri-lanka/>.

³⁷“Cabinet Approves Proposed Microfinance & Credit Regulatory Authority Act.” Lanka Microfinance Practitioners Association, June 21, 2021. <https://www.microfinance.lk/cabinet-approves-proposed-microfinance-credit-regulatory-authority-act/>.

³⁸Thennakoon, Nishadi, Financial Consumer Protection is not a Destination, it's a Journey (June 17, 2020). Daily FT Sri Lanka, 2020, Available at SSRN: <https://ssrn.com/abstract=3629024>

6. Conclusion

This report examines the landscape of financial inclusion in Sri Lanka, with a specific focus on aspects such as the role of digitalization in improving access to finance, the importance of digital and financial literacy, the regulation of the microfinance industry and financial consumer protection. Some of the key findings are that despite having extensive networks of physical bank branches, most Sri Lankans rely on informal sources, particularly unregistered microfinance institutions that often involve illegal deposit mobilization, excessive interest rates, and unethical recovery methods, leading to severe debt, reduced savings, and adverse social consequences, especially impacting women. Additionally, despite a high literacy rate, financial literacy is low in Sri Lanka, impacting financial decisions and contributing to cycles of debt and poverty. This report advocates for a holistic approach to address the multifaceted challenges hindering financial inclusion, especially for women. Promoting financial inclusion through digitalization requires a multi stakeholder approach. The government has a responsibility to drive financial and digital literacy programs, establish a strong financial consumer protection framework, establish comprehensive regulations for the microfinance sector, create a unique Digital ID, establish a platform for data sharing, and promote the interoperable payments interface. The corporate sector has a role in fostering partnerships among financial institutions, technology companies, and startups, collaborating with other institutions to avoid redundancy in financial literacy and entrepreneurship training programs, and driving innovation and investment in technology. Social responsibility lies in advocacy, spreading awareness and providing feedback to the government and corporate sector.