More inclusive, more stable?

The financial inclusion - stability nexus in the global financial crisis

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The Second International Workshop P2P Financial Systems 2016

September 6, 2016

Overview

1. Introduction
2. Concepts
3. Regulation and supervision
4. Results

The relationship between financial inclusion and financial stability is complicated and complex

The paper gives an empirical contribution that serves as evidence to prove that financial inclusion is related to financial stability.

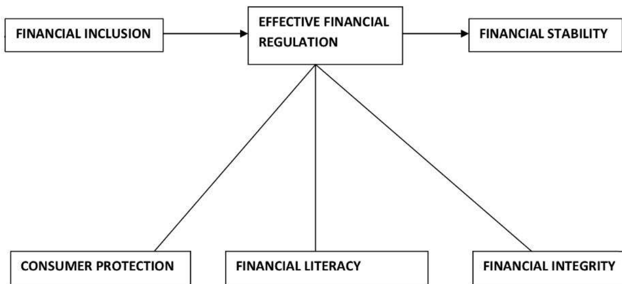
- A comprehensive approach to **financial inclusion** addresses at least three aspects: Access, usage and quality of financial services and products.
- In contrast to credit, increase access to other financial services (ATMs, branches, accounts) does not have a strong impact on banking sector stability and can be promoted extensively as long as their impact on growth is still positive.
- **Financial Stability**: It is not easy to define or measure. It has a multidimensional scope that depends on the interplay of key elements of the system: the existence of credit risk, i.e. that a borrower may not repay in full, is central to the analysis of money, financial intermediation and financial (in)stability, (Goodhart, Tsomocos, Zicchino and Aspachs, 2006).

Authors argue that financial instability is better captured by developments in bank lending (difference between real credit growth in the last pre-crisis year, 2007, and real credit growth during the crisis, in 2009) rather than deposit funding.

- High-quality regulation and supervision can make the difference between "good" and "bad" financial inclusion.
- It is costly and it is more complicated when financial inclusion is provided by a large number of institutions outside the regular banking system or the unregulated financial sector.
- Policies that require banks to expand credit to the underserved without adequate supervisory oversight can have a detrimental impact on bank stability.
- Gaps in the quality of banking supervision are larger in countries that have the lowest levels of access to financial services.

The failure of regulation is cited as the major cause of the recent world financial crisis.

Intermediary role of financial regulation



Source: Chiwira et al. (2013)

An effective financial regulatory framework plays an important role in ensuring that financial inclusion leads to financial stability.

Main result: A higher level of financial inclusion has a moderating effect on the credit crunch in the crisis

Sugestions:

- More emphasis on the transmission channels that lead from a higher level of financial inclusion to a more stable financial system.
- Beyond the increase in the number of borrowers, it is relevant to know how they are using the loans and what is their rate of repayment to learn about the implications on financial stability. An example: mortgage loans versus consumer loans.
- A theoretical framework, a model.
- Regulation: It is difficult to control by regulatory framework for each country.

References

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