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POLICYINSIGHTS

INSTITUTE OF POLICY STUDIES OF SRI LANKA

PROMOTING FINANCIAL INCLUSION IN THE 4IR: OPPORTUNITIES AND CHALLENGES FOR SRI LANKA

From the IPS flagship publication 'Sri Lanka: State of the Economy 2019'

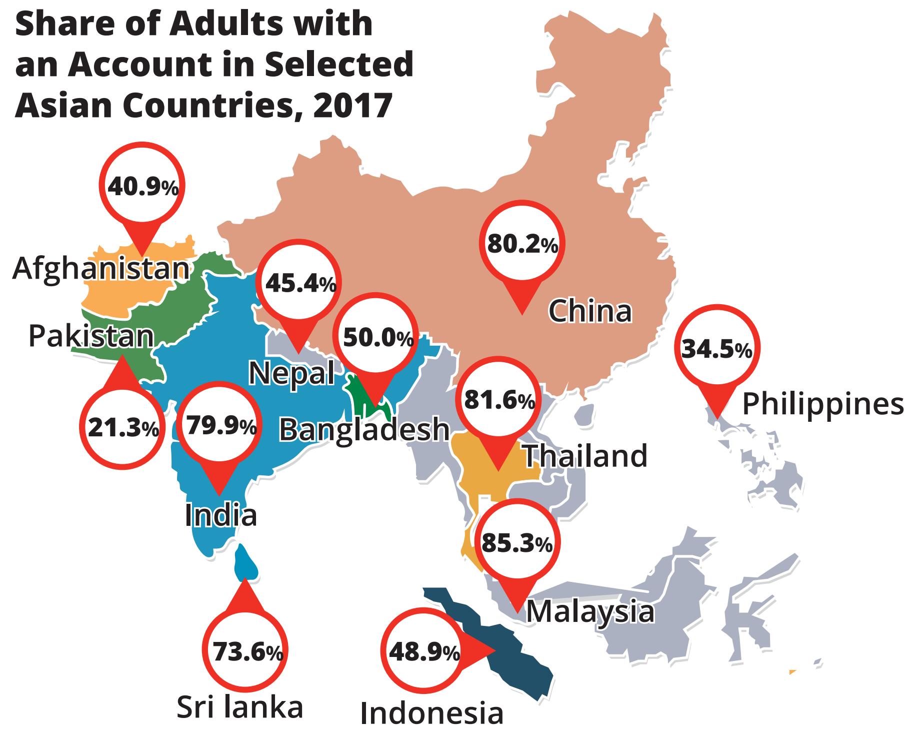
Financial inclusion has been looked upon as an important instrument for reducing poverty and vulnerability and achieving the sustainable development goals (SDGs). Sri Lanka's financial sector comprises a wide range of institutions – both formal and semi-formal – providing a variety of financial services like loans, savings, payment services, money transfer and insurance. In addition to financial institutions like banks, leasing and finance companies and co-operatives, non-financial institutions such as mobile network operators have emerged in recent years as important providers of financial services, particularly digital financial services.

Financial Inclusion in Sri Lanka: Current Status and Issues

Despite Sri Lanka's high level of access to financial institutions compared to many South Asian counterparts and the availability of a widespread network of financial service providers, there are several issues and challenges that need to be addressed to achieve greater financial inclusion in the country.

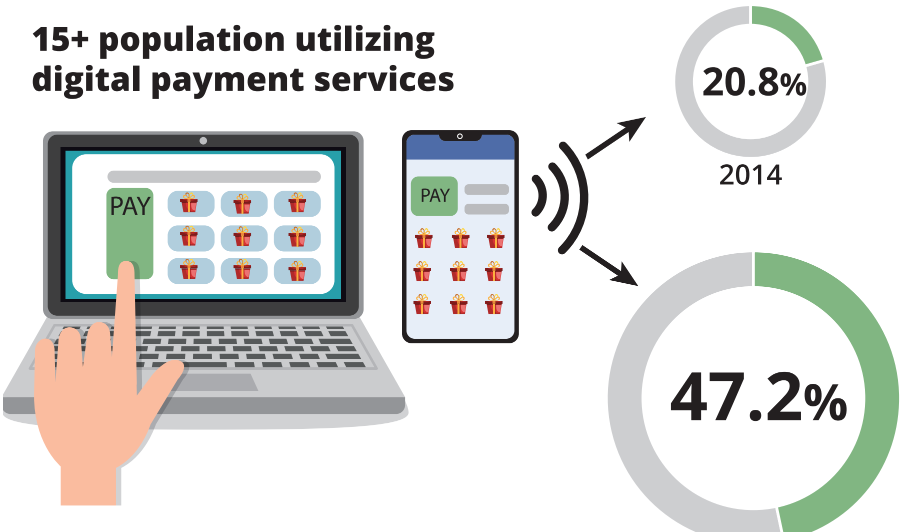
High transactions costs, documentation requirements, cumbersome procedures and time lags related to transactions are often highlighted as inefficiencies associated with financial services like savings, loans, money transfers and insurance. With regard to savings, although a large share of adults have bank accounts, there are several 'dormant' accounts with only a minimum balance, or irregular savings, primarily due to distance to bank branches and high transaction costs.

Further, opening a bank account often requires several documents, which either discourage or prevent clients from opening an account with the bank. Moreover, high transaction cost is one of the key reasons why a substantial share of international remittances is sent through informal channels. Using formal channels such as banks is often considered costly by migrant workers. Distance to bank branches and lack of awareness on available products is other contributory factors for the low utilization of formal channels for remittances. Furthermore, utilization of insurance through formal sources has remained low due to many reasons like high cost of insurance, difficulty in paying premium at regular intervals, lack of trust/confidence and lack of awareness of benefits of insurance among low income groups Nevertheless, in recent years, various technology-based solutions including mobile money banking, mobile insurance and use of biometrics have emerged in the financial sector in Sri Lanka, which could help addressing some of these inefficiencies, thus improving financial inclusion in the country.



Source: *World Bank. (2018). The little data book on financial inclusion 2018. Washington D.C.: World Bank.*

15+ population utilizing digital payment services



Source: *World Bank. (2018). The little data book on financial inclusion 2018. Washington D.C.: World Bank.*

Promoting Financial Inclusion through the 4IR in Sri Lanka

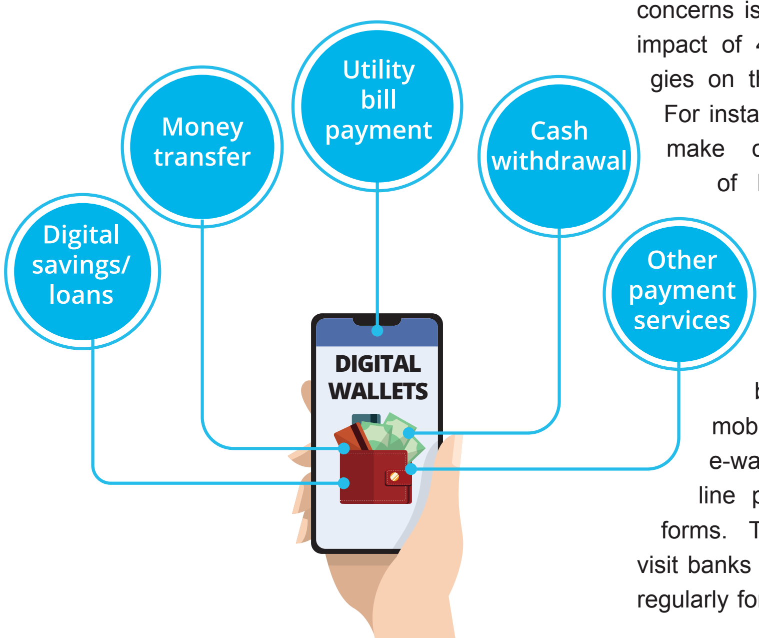
Growth in the use of mobile phones and internet in recent years has contributed to a number of innovations in the financial sector, providing customers with access to a broad range of financial services/ products that can be accessed easily and more conveniently through their mobile phones. E-wallets, mobile wallets and payment apps as well as insurtech innovations like mobile micro- insurance are among such key innovations in the financial sector in recent years.

A number of banks as well as the main mobile network operators have launched their own e-wallets/mobile wallets and payment apps in recent years allowing their clients to access a whole range of services at anytime from anywhere through their mobile devices. These services often go beyond just banking services like money transfer to utility bill payments and payment at various retail outlets /services. Mobile microinsurance is another innovation which could help address a number of challenges related to microinsurance sector such as high transaction costs, poor infrastructure, and lack of awareness and demand for insurance from clients, particularly those from low-income segments. These innovations play an important role in enhancing financial inclusion in the country, particularly by providing access to a range of financial services in a convenient, secure and timely manner with lower transaction costs and extending access to these services to those who have previously had no access to traditional banking services. They can also play a key role in taking the country closer towards a 'cashless society'

In addition, there are many benefits of technologies like AI and biometrics, particularly in improving efficiency and enhancing security of financial services. Yet, only a handful of financial institutions so far have moved in to deploy these technologies. Blockchain technology too remains at an early stage of adopting in Sri Lanka's financial sector, with feasibility, particularly in areas like KYC, currently being studied by a Blockchain working committee.

Challenges and Way Forward

Despite several potential benefits of 4IR technologies to the financial sector, there are some challenges and concerns too that need to be addressed. One of the key concerns is the potential impact of 4IR technologies on the workforce. For instance, 4IR may make certain tasks of banking staff obsolete as these services can be easily accessible through mobile banking, e-wallets and online payment platforms. The need to visit banks by customers regularly for services like money transfers, receipt of money will be minimised. Moreover, the 4IR also creates concerns over employees being replaced by AI-enabled machines like robots or chatbots. However, the 4IR can create demand for IT-enabled high skilled employees for the financial sector who are capable of dealing with advanced technological innovations. This further stresses the need for skills upgrade and training for employees of financial institutions.



Another concern is that the 4IR may exacerbate the 'digital divide' in the country by improving access to diverse services and products to those who are more tech savvy and have smart phones, while excluding the already marginalised groups like the poorest groups who may not have access to smart phones and the internet. Moreover, 4IR technologies are likely to be embraced easily by the youth or millennials, but less likely to be used by older generation, thus widening the gap between different demographic groups.

This Policy Insight is based on the comprehensive chapter on "Promoting Financial Inclusion in the 4IR:Opportunities and Challenges for Sri Lanka" in the 'Sri Lanka: State of the Economy 2019 Report' - the flagship publication of the institute of Policy Studies of Sri Lanka (IPS). The complete report can be purchased form the publications section of the IPS.

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