

## Research Article

# Financial inclusion in Ethiopia: Using core set of financial inclusion indicators

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## Abstract

Financial inclusion is the key to inclusive development throughout the world. It is the access to get financial services such as saving, loan, insurance and others easily at an affordable cost, this study aims at evaluating the level of financial inclusion in Ethiopia in comparison with Sub Saharan Africa and low income countries. World Bank group 2017 data on financial inclusion is used. The result shows access to have a bank account and account at other financial institution has been realized improvement to the year, where as it is far below the Sub Saharan African average. The major reason for not having a bank account or account at financial institutions in Ethiopia are insufficient fund and financial institutions are too far away, while religious reasons and lack of trust on financial institutions are the least. No one pays utility bill digitally, the use of digital payment is very poor in Ethiopia; only three out of hundred individuals in Ethiopia used an account to receive government payments.

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*Key words; financial inclusion, loan, account, mobile money*

## Introduction

*Financial inclusion is the key to inclusive development throughout the world.* In earlier times it was micro credit and later micro finance, which holds the idea of providing financial services particularly small amount of loans to the poor. Now a day's financial inclusion is emerging as a new paradigm of economic growth that plays an essential role in alleviating poverty. Financial inclusion is access to formal financial service; access to saving and credit at an affordable cost (Eduardo, Diniz, Birochi and Pozzeben 2011), and a vast section of disadvantaged groups (Naha 2015). It is an equalizer that enables all citizens to contribute to economic growth (Aditi Kapoor 2013).

Financial inclusion is the one among special issues of federal democratic republic of Ethiopia as stated by the international monetary fund's country report form No15/326, 2016. According to the report there is a room for more financial inclusion in the country compared to other countries in the region. Despite strong effort undertaken by banks to offer financial products to attract clients and offer novel financial service, financial inclusion has a long way to go in Ethiopia FDIP (2016) because the country was listed the last second for financial inclusion from 26 politically, geographically and economically same countries.

In the existing state of affairs Ethiopia is at its stage of economic growth, the country is ranked first from the top ten fastest growing economies in Africa, (African Economic Outlook 2018). In spite of this an inclusive growth and upgrading living condition of low income and neglected people of the country is necessity. Reports of World bank and international monetary fund (IMF) point to an increased demand for inclusive growth and poverty reduction over the world could be achieved with appropriate financial inclusions, not only by developing countries but also developed countries. In line with this, existing empirical literatures in an academic arena explores different pillar to the improvement of financial participation such as; product availability, financial literacy, accessibility, risk management( Naha Garg 2015) absence of legal identity & gender biasness, level of income and bank charge, type of business, rigid term and condition( Iqbal, S. Sami 2017). Follow a line of investigation, researchers in different countries (Zins Weill 2016, Efobi, Beecroft & Osabuohien (2014) evaluate level of financial inclusion in different countries and identified causes and identified causes for exclusions

Hence this paper aims to fill the gap in Ethiopia by utilizing data from the World Bank's Global Findex database and contribute to the understanding of financial inclusion in Ethiopia by examining the level of financial inclusion in the country and compare the country with the other sub Saharan Africa and low income countries.

### **Statement of the problem**

Financial sector in Ethiopia consists of 2 public and 16 private banks, 17 licensed insurance companies in Ethiopia one of which is government owned, 35 microfinance institutions and more than 18,000 saving and credit cooperation making financial services available for both rural and urban areas.

Financial institutions are primary players on move toward financial inclusion. Financial inclusion is needed for uplifting the poor and disadvantaged people by providing diversified financial products and services which lead to achieve an inclusive growth. As compared to developed countries financial inclusion in African countries is very low, of which Ethiopia is listed almost the last, below sub Saharan Africa and low income countries as well Demirguc (2014). Different countries exercise various instrument to reduce financial exclusions such as mobile banking (best example Kenya), correspondence banking (India), using shops as financial service provision centers etc. While putting into practice all these instruments are at infant stage and some of them even don't exist in Ethiopia.

As Global development cannot be achieved letting Africa aside where only 34% adults owned account in sub Saharan Africa, according to global financial index data 2014 (Demirguc-Kunt et.al 2015) requirement of policy intervention is essential to ensure global inclusive development. A study by (Getnet, Alemu & Zewdu 2014) show only 10% of households have access to formal credit, of which only 1 percent of rural population has bank account. Accessibility and availability of financial service to reach the society is indispensable to achieve greater financial inclusion, currently commercial banks are singing a vital role in fulfilling this gap. Furthermore recent index of countries financial inclusion shows financial inclusion in Ethiopia is left untouched and it is an area demanding a quick remedy to maintain provision of financial service by adopting and expanding menses that will achieve full financial inclusion (Demirguc-Kunt et.al 2015). As a result of these, this study tries to make an effort to fill the gap on the understanding of financial inclusion in Ethiopia by utilizing data from the World Bank's Global Findex database and contribute to the understanding of financial inclusion by examining the level of financial inclusion towards ownership of a bank account, saving on financial inclusion, access to credit and make digital payment in the country in comparison with other sub Saharan Africa and low income countries.

### **Objective**

The general objective of this research is evaluating the level of financial inclusion in Ethiopia associated with Sub Saharan Africa and low income countries.

#### **Specific objective**

- ❖ To examine access to have a bank account and saving at formal financial institutions in Ethiopian.
- ❖ To find out the main barriers on access to have an account at formal financial institutions in Ethiopia.
- ❖ To examine level of getting credit at formal financial institutions in Ethiopia.
- ❖ To evaluate the use of mobile phone and digital payment to access financial services in Ethiopia compared with Sub Saharan Africa and low income countries.

### **Review of literature**

Financial inclusion is a state wherein there is effective access to a wide range of financial product and service: including medical insurance, education loan, general credit, weather based crop insurance, universal pension and personal loan to purchase house and durables (Akapour )

Access to basic finance includes; saving, payment, credit and investment that's why Exclusion brings financial distress, debt and poverty. Propensity to do a business relates to personal wealth or recent change therein (Evans & Javanovic 1989) individuals wealth and propensity for self employment observed only if

financial constraints exist. Unconstrained means the amount the entrepreneur needs to borrow is sufficient to cover capital market required to start a new business.

Mukhejee & Chakraborty (2012) banks in India are not achieving a desired goal so that so that it is suggested to report reserve bank about their contribution towards achievement of financial inclusion.

Financial inclusion refers to all initiatives that make formal financial services Available, Accessible and Affordable to all segments of the population. This requires particular attention to specific portions of the population that have been historically excluded from the formal financial sector either because of their income level and volatility, gender, location, type of activity, or level of financial literacy (Triki & Faye 2013). As a result of this a variety of key areas and strategies were identified for promoting financial inclusion. Triki & Faye (2013) These encompass the transformative role that technology could play in achieving greater financial inclusion, policy and regulation, financial education and customer protection, Advocacy program and data & measurement, lessons that Africa could learn from other developing regions, and the role of Development Finance Institutions (DFIs). Creating / raise awareness, build trust among various stockholders, identify the best modality for coordination, ensure relevance at national level be some of the tools help for its enhancement.

Financial inclusion can be measured by the three dimensions; the first is access to financial service, second usage of financial service and third quality of the product and service delivery. All of these measurements are comprehensive to provide a holistic assessment. G20 GFPI endorsed financial inclusion indicators 2013 and a new financial inclusion indicator has been proposed on 2016 to measure the use, availability and quality of digital financial services. The driving factor for revision and expansion the existing set of indicators is the expansion of new digital models, as well as availability of new data on demand and supply of digital financial services. Accordingly some of the indicators be; user indicators; adult with an account, adults with credit, adults using digital payment (new) payment using mobile phone (new), saving propensity. Quality indicators include dispute resolution, credit barrier and Access indicators; point of service and debit card ownership just to list some GFPI 2016.

### **Level of financial inclusion**

Financial sector in Ethiopia consists of 2 public and 16 private banks, 17 licensed insurance companies in Ethiopia one of which is government owned, 35 microfinance institutions and more than 18,000 saving and credit cooperation making financial services available for both rural and urban areas.

Financial inclusion is a particular concern in Africa. Beck and Cull (2015) observe that African banking systems are less inclusive than those outside Africa. 16.5 percent of households report having an account with a formal financial institution in the median African country. Mlachila et al. (2013a) point out that financial sector development has contributed to improve the process of growth although financial services are clustered around major urban areas. Where in Ethiopia only 10% of households have access to formal credit, of which only 1 percent of rural population (Getnet, Alemu & Zewdu 2014) has bank account. The emergence of mobile banking and the rising economic growth in many of African countries can foster or at least transform the situation of financial inclusion in Africa. As per the international statistics about financial inclusion with 2014 data from the Global Findex database, DeDemirgüç, -Kunt et al. (2015) Globally 62 percent of adults own an account at a formal financial institution, either at a bank or with a mobile money provider. In the developing world Account ownership has been substantially increasing and reached 54 percent of the population in 2014, particularly appreciation to innovative financial products like mobile banking. However, the share of the population with a formal account is still far lower than in high income economies (94 percent). 56 percent of adults in the world declared having saved money in the past 12 months in 2014 though the percentage of formal saving varies greatly between high-income economies and developing economies where it is only 13.3 percent in Sub Saharan Africa. Formal credit at a financial institution has only been used by 7.4 percent of adults in sub Saharan African countries while it has been used by 18 percent in high income economies on the other hand mobile banking in Africa is at the leading position (Demirgüç, -Kunt et al., 2015).

### **Data**

The data for this study was sourced from the World Bank's Global Findex database household survey on financial inclusion. It is the third round of data collection since the Global Findex database was launched in

2011, the dataset includes nationally representative data on access to and use of formal accounts, credit, digital payments and savings via adults aged 15 and above, though definition to adult is 18 years old or older in terms of Ethiopian’s definition to adult, in 144 economies during the year 2017. Additionally the 2014 World Bank financial inclusion survey is also used to make a figurative comparison. The Global Findex questionnaire provides detailed information on financial inclusion and encloses a large set of questions on the use and the motives for use of financial services and the reasons or factors responsible for ownership and the use of formal accounts.

**Result and discussion**

**1. Account**

Access to have a bank account is the one among financial inclusion indicators. 34.8 percent of Ethiopians (adult 15+) have an account at a formal financial institution. The result is almost equivalent to low income countries (34.9 percent) while it is below the sub Saharan Africa (42.9 percent). It has been scored a 13% increment within the three years from the year 2014 result. This step up is accredited to efforts made by commercial banks towards branch expansion, awareness creations and incentive mechanisms such PLS programs and prize linked remittances.

This indicates that access to have, and extent to use, formal accounts in Ethiopia has a long way to go. Provided the progress from its previous period average to reach its 2020 target stetted by national bank of Ethiopia by which 60% of adults will report personal ownership of transaction accounts in regulated financial inclusion.

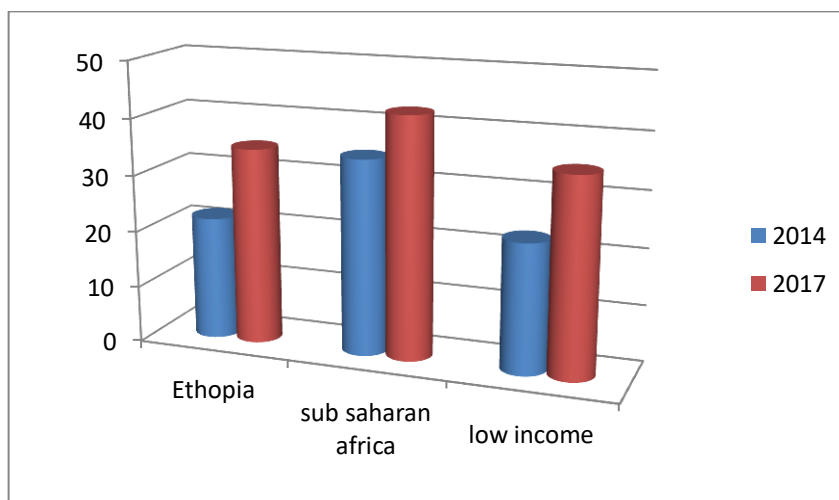
**Table 1 Account ownership**

**Account (% age 15+)**

	<u>Ethiopia</u>	<u>Sub Saharan Africa</u>	<u>low income</u>
All adult	34.8	42.6	34.93
All adult 2014	21.8	34.2	22.9
Women	29.1	36.9	29.9

Source: Global Findex database 2017

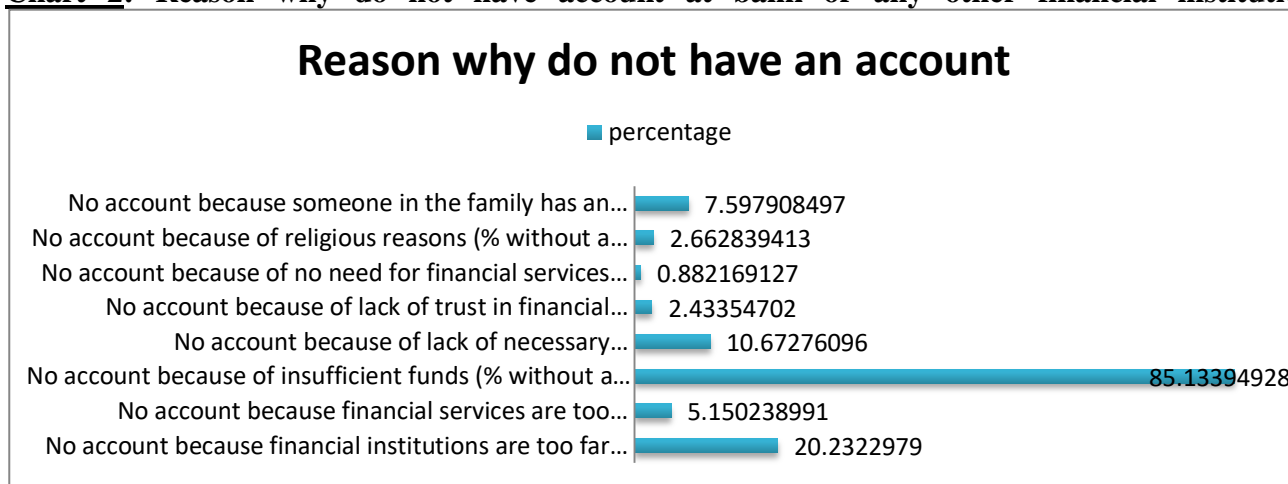
**Chart 1 Account ownership (15+)**



Source: Global Findex database 2014 &2017

In terms of individual characteristics account penetration to women is very low as compared to men, only 29.1 percent of women in Ethiopia have formal account at formal financial institutions, Mengistu (2018) Women account for a disproportionate share of the unbanked, and the gap is widening, in 2017 the gender gap to the year jumped to 12% from being virtually insignificant in 2014; women’s account ownership has been increased only by eight percentage points from 2014 while it is nearly doubled for men in the three years. The survey further asked those without account on the subject of reasons why they do not have a bank account or account at formal financial institutions.

**Chart 2: Reason why do not have account at bank or any other financial institutions**



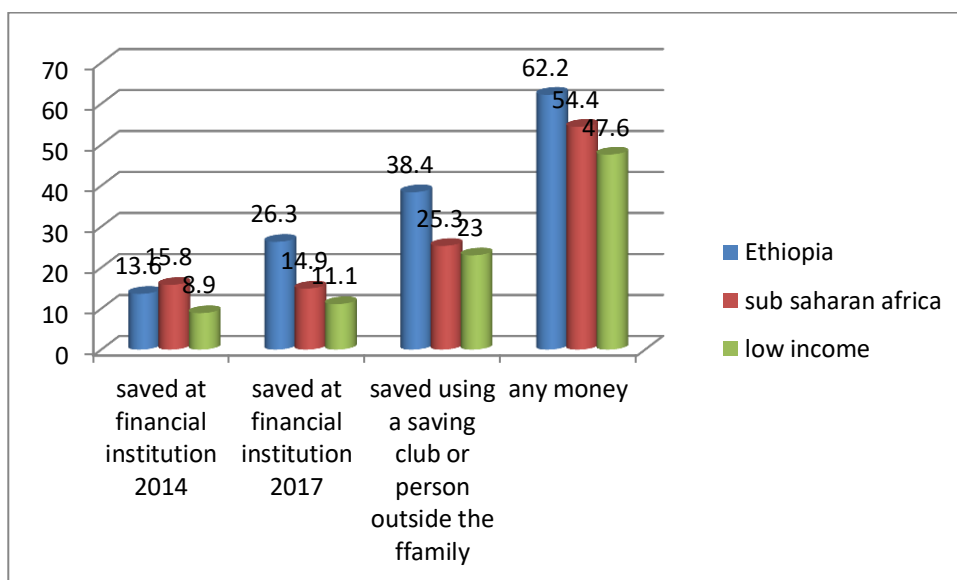
Source: Global Findex database 2017

As it is observed on chart 2 above, the major reason why they do not have account at bank or any other financial institutions for more than 85 percent adults (15+) in Ethiopia is insufficient fund and the other reason that hinder the access to bank account is financial institutions are too far away from them quoted by 13.2 percent. Religious reasons and lack of trust on financial institutions are the least ones which replied only by 1.7 percent and 2.4 percent respondents without financial institution accounts.

## 2. Formal saving

Another measure of financial inclusion is whether or not an individual save any money at formal financial institutions. In terms of this, the survey results show that 26.3 percent of Ethiopian individuals who been saved at financial institutions in the past 12 months. This is to a large extent higher than what low income countries do where its corresponding average is 11.1 percent and it is also higher than sub Saharan African countries which accounts to 14.9 percent. Moreover percentage of individuals who has been saved at formal financial institutions during the year 2014 becomes almost doubled in the year 2017. Provided the improvement in saving habit of the people, reliance on informal institutions is still high.

**Chart 3: Formal saving**



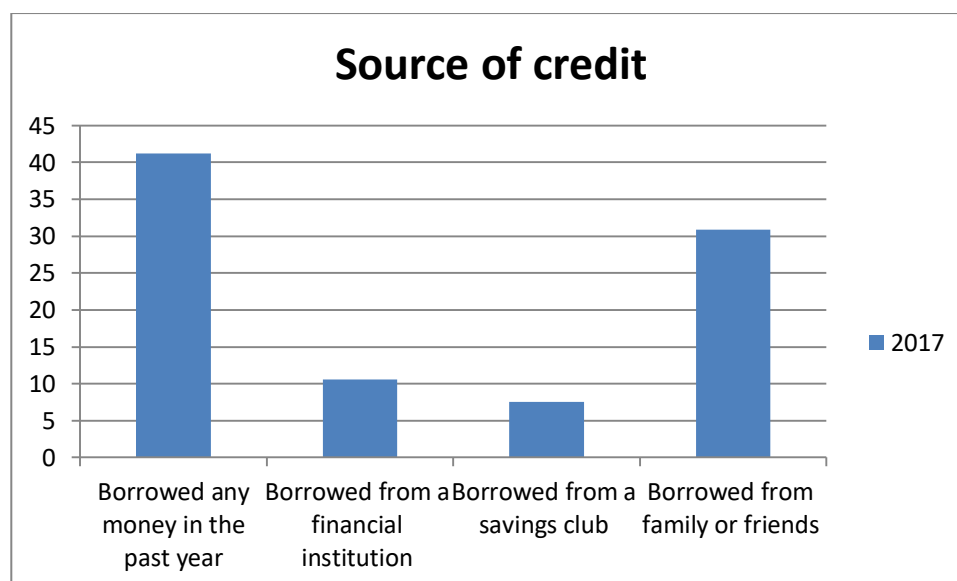
Source: Global Findex database 2017

As shown in the chart above, out of the 62 % Ethiopians (adults 15+) who has been saved any money in the past 12 months, only 26.3 percent has been saved at recognised financial institutions while others save at informal institutions such as saving club or person outside the family. This reliance of saving at informal financial institution in Ethiopia is attributable to use of the traditional and historic saving method in the country called ‘iqube’, it is rotating saving and credit association where each member agrees to regularly pay a small sum of money (daily, weekly or monthly) in to a common pool so that each member, in rotation, can receive one large sum (Mengistu 2018) and Iddir, a non-formal insurance group intended to mitigate emergency situations like the death of a household member.

### 3. Formal credit

The third measure of financial inclusion is access to get credit from formal financial institutions. Individuals borrowed money in the past year accounts to 41.2 percent; nonetheless situation is very different as look upon the levels of formal credit, out of who borrowed only 10.5 percent o Ethiopian adults obtained credit from financial institutions in the past year of course it is relatively higher than sub Saharan Africa and low income countries average (8.4 percent and 7.9 percent respectively).

**Chart 3 source of credit**





Majority of individuals borrowed money during the last 12 months borrow from family and friends as seen on the chart above it is about 30.9 percent while 10 percent is sourced from formal financial institutions. This can be explained by the fact that credit is highly rigorous in those afford the formal institutions minimum requirement

**4. Mobile account & Digital payments**

	<b>Sub</b>		
	<u><b>Ethiopia</b></u>	<u><b>Saharan Africa</b></u>	<u><b>Low income</b></u>
<b>Mobile account &amp; Digital payments in the past year (% age 15+)</b>			
Mobile money account all adult	0.3	20.9	17.6
Made or received digital payments	11.9	34.4	25.6
Used an account to pay utility bills	0.0	7.7	4.4
Used an account to receive private sector wages	0.7	5.7	3.3
Used an account to receive government payments	3.0	7.3	4.3
Used a mobile phone or the internet to access an account	0.4	20.8	17.1

Source: Global Findex database 2 017

No one pays her utility bill digitally, the use of digital payment is too low in Ethiopia; only three out of hundred individuals in Ethiopia used an account to receive government payments and out of hundred individuals almost 12 Ethiopian individuals Made or received digital payments, it is significantly lower than the low income countries (25.6 percent) and sub Saharan African countries (34.4 percent).

Moreover only 0.3 percent of Ethiopian individuals have mobile money account. it is to the contrary that the African continent is at a leading position concerning mobile money banking, especially in East Africa where for example more than 73 percent of Kenyans are mobile money customers (Demombynes &Thegeya, 2012) and it is also contrary to that African individuals resort more to mobile account than people on a global scale (20.9% versus 4.4%). Mobile phone adoption alone isn't sufficient to drive mobile financial services Mengistu (2018) about 13 million people with a mobile phone are unbanked hence penetration of mobile phone is not being the root cause for low penetration of mobile financial services. In spite of this the country is approaching to a surprising steps forward in digital financial inclusion (Shelly 2018); the banking sector is championing agent banking with mobile technology and offered agent banking products such as HelloCash and M-BIRR user interfaces in multiple languages, offline capabilities, and multilingual customer service centers. Moreover, Commercial Bank of Ethiopia (CBE), the largest state-owned bank, launched CBE Birr in December 2017 with no-fee transactions and short codes to enable payments. Kifiya, a locally-owned technology company, acquired an MFI to offer integrated digital services, including G2P/P2G payments and data-driven agricultural index insurance.

**Conclusion**

In Ethiopia access to have a bank account and account at other financial institution has been realized improvement to the year, where as it is far below the Sub Saharan African average. Provided the progress from its previous period(2014), that access to have formal accounts in Ethiopia has a long way to go to reach National Bank's 2020 target by which 60% of adults will report personal ownership of transaction accounts in regulated financial inclusion. On the subject of reasons for not having a bank account or account at formal financial institutions, the major reason almost for more than 85 percent adults (15+) in Ethiopia is insufficient fund. The other reason that frequently replied is financial institutions are too far

away, whereas religious reasons and lack of trust on financial institutions are not as such a problem in Ethiopia.

Saving at formal institution is higher than what other low income countries and sub Saharan African countries do. It has also shown an interesting improvement year after year however the reliance on other saving informal institutions such as iqub and Iddir is still high. Only 10.5 percent of Ethiopian adults obtained credit from financial institutions in the past year, even though it is relatively better as compared with sub Saharan Africa and low income countries average (8.4 percent and 7.9 percent respectively) it is lower than what provided by informal sources such as family friends and saving clubs.

No one pays utility bill digitally, the use of digital payment is very poor in Ethiopia; only three out of hundred individuals in Ethiopia used an account to receive government payments

Contrary to that African continent is at a leading position concerning mobile money banking, and contrary to that African individual's resort more too mobile account than people on a global scale, only 0.3 percent of Ethiopian individuals have mobile money account.

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