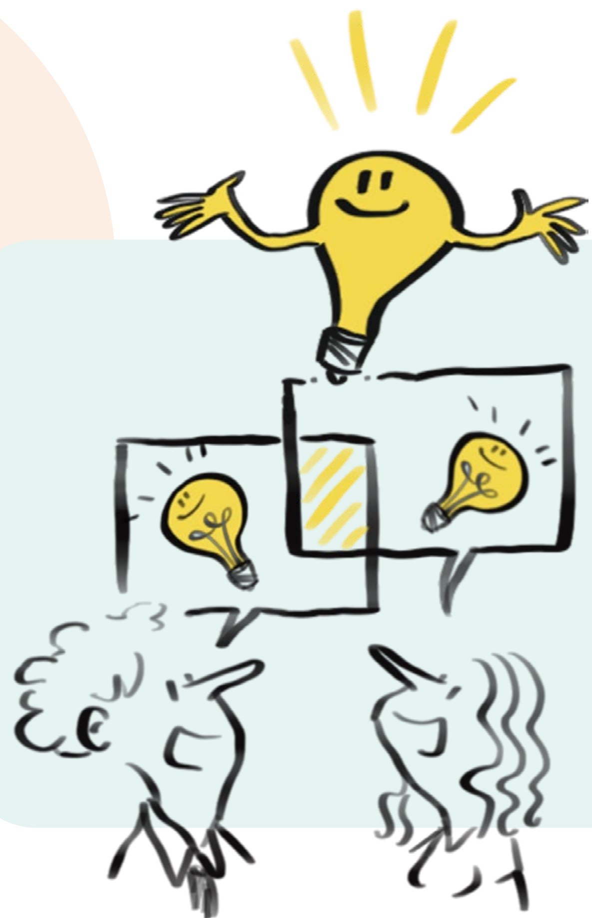
Building the future of inclusive finance



***Insights** from the roundtable*

organised by ADA, the ADA Chair and InFiNe on 16 October 2024

InFiNe Inclusive Finance Network Luxembourg

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ada

Building the future of inclusive finance

On the occasion of their joint anniversaries which add up to 50 years of experience in inclusive finance, ADA, InFiNe and the ADA Chair at the University of Luxembourg organised a roundtable discussion on 16 October 2024. The roundtable brought together more than 70 representatives of Luxembourg's sustainable finance ecosystem to discuss the future of inclusive finance.

The roundtable consisted of:

- ***an introduction speech***
  by Professor Dirk Zetzsche, holder of the ADA Chair
- ***two roundtable discussions***
  moderated by Philippe Guichandut, General secretary of Grameen Credit Agricole Foundation and Vice-Chairman of InFiNe, and Paola D'Angelo, Managing director of SPTF Europe as of 1 January 2025
- ***a conclusion***
  by Laura Foschi, Executive Director of ADA.

The following speakers representing various segments of the inclusive finance sector participated in the **two roundtable discussions:**

- Kingsley Adofo-Addo, Head, SME Banking / Team Lead Green Climate Fund Desk, **Ecobank,** Ghana, and Edgardo Perez Preciado, CEO, Fundación Genesis Empresarial, Guatemala, represented **local financial institutions in emerging markets**
- David Grimaud, CEO, **Bamboo Capital Partners,** and Milena Bertram, Head of Impact & Sustainability, **Finance in Motion,** represented **private asset impact fund managers**
- Lucie Bernatkova, Vice President, Portfolio Manager, Impact Investments, **AllianzGI,** and François Passant, Executive Director at **Nordea Asset Management,** represented **the broader financial sector**
- Robert Jarvis, Advisor for Sustainable Finance at the **Ministry of Finance,** and Shaneera Rasqué, ESG Coordinator - Investment Funds, **CSSF (Commission de Surveillance du Secteur Financier),** represented **the public sector.**

The discussions were showcased live by the graphic artist Geoffroy Lefort. In addition, to gain a better understanding of the audience, an online questionnaire was sent to invitees in advance which was filled in by 37 people.

This document includes the graphic designer's drawings and summarises the answers to the questionnaire, the speeches and the roundtable discussions with the audience which led to two calls to action to make inclusive finance a powerful development tool.

ADA, InFiNe and the University of Luxembourg wish to thank all the respondents to the questionnaire, the speakers and the roundtable participants for their invaluable contributions to the debate.

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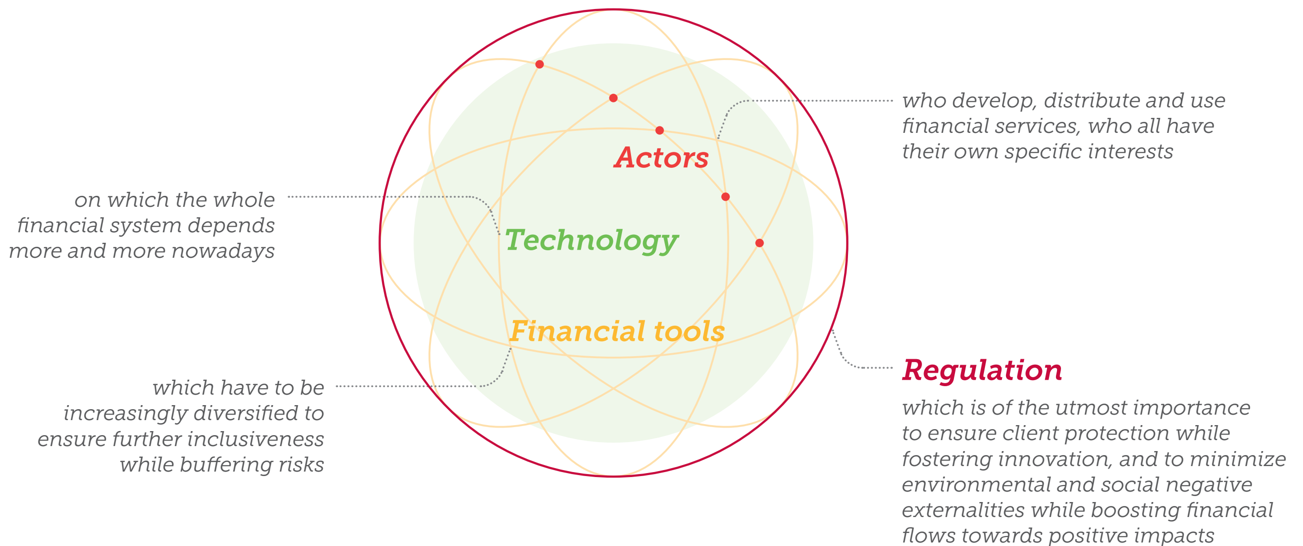
Introduction

Financial inclusion can be defined as a broad range of financial services paired with the means to not only ***access*** but also properly ***use*** them. Financial inclusion results from a complex interplay between:



While the optimal equilibrium between these elements remains challenging to achieve in local evolving contexts, **financial inclusion is also expected to be key to achieving the Sustainable Development Goals, especially in emerging markets.**

To this end, **it is essential to scale up inclusive finance,** which raises ***three questions*** that will determine its future:

1. ***How to build truly inclusive financial systems*** *and avoid making inclusive finance a remote niche of the financial sector?*
2. ***How to measure financial inclusion*** *to know where we stand, since we are still facing a lack of harmonisation of data and practices?*
3. ***How does financial inclusion impact the financial system, the economy and society at large,*** *and therefore what is its effective contribution to the Sustainable Development Goals?*[1]

These initial reflections opened the debate which focused on ***two fundamental facets of inclusive finance:***

Inclusive finance as a market: *a triple bottom line investment opportunity rather than as a risky segment*

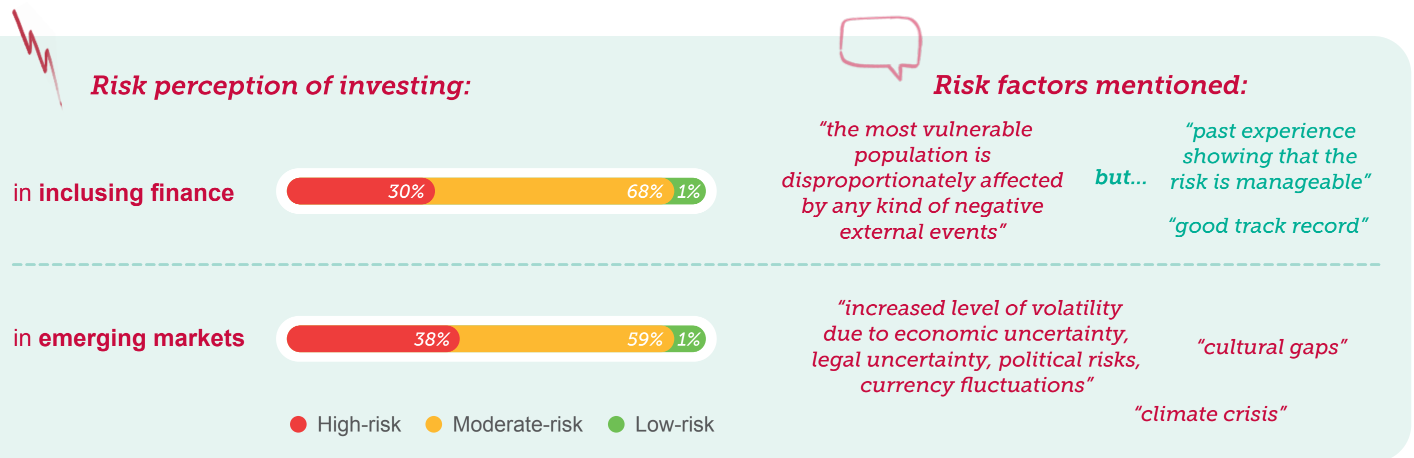
Inclusive finance as a sustainable development tool: *a channel to generate impact on various development issues beyond financial inclusion*

1 Zetzsche, D. (2024). The Future of Financial Inclusion. http://dx.doi.org/10.2139/ssrn.4988417

Inclusive finance as a market: *from risks to opportunities*

One of the barriers to scale inclusive finance lies in the risk perception of investing in emerging markets, and therefore in inclusive finance.

If investing in inclusive finance and emerging markets is mainly considered as moderately risky in both cases, emerging markets tend to be considered as slightly more risky than inclusive finance as a sector.



The risk perception of investing in emerging markets is a real challenge that private asset managers committed to generating impact have to overcome. What is even more problematic is the ***disconnection between the risk perception of private investors and the actual level of risk in emerging markets,*** with the perception often exceeding the actual level of risk.

Therefore, narrowing this gap to consider actual risk levels by ***relying on existing, correct risk data is a must.*** These data sometimes do exist, such as in the credit risk database for emerging markets called GEMs (Global Emerging Markets Risk Database) that was established by the European Investment Bank (EIB) and IFC to show real risk based on track records of investments in these countries. **Unfortunately, these data are not always public or sufficiently publicised and are therefore not used by private investors.**

That said, **even if the actual risks are often lower than the perceived ones, they still exist**. ***However, real risks are in most cases manageable with the proper instruments.***

In this regard, the example of Ecobank, a pan-African banking group, is enlightening. Ecobank serves micro, small and medium enterprises with a set of financial services, including inclusive finance for the underserved. Even though inclusive finance does present some risks according to Ecobank, a robust risk management framework enables them to ensure that potential benefits outweigh these risks. Indeed, Ecobank considers inclusive finance as an ***opportunity*** to expand their customer base and capitalize on new and growing markets by bringing the unbanked into the formal financial system and supporting their development. By enabling individuals and businesses to save, invest and manage risks more effectively, ***financial inclusion is not only a social good but a powerful economic driver that contributes to economic stability.***

"When there is a will there is a win."
Ecobank

Such an approach could be inspiring for **private asset fund managers further away from the field,** who nevertheless face additional challenges, such as the high cost of operations, liquidity requirements, currency risk, hedging costs, or the lack of data at investee level.

Therefore, specific financial de-risking instruments appear necessary.

Private asset managers need committed donors to provide concessional and patient capital for blended finance structures to help them overcome the risk perception that is usually much higher than the actual risk level (in terms of geography, sectors, investee profiles, etc.). This would contribute to ***building a track record*** to convince the private sector that investments in underserved segments can be profitable, even in emerging markets.

Unlocking institutional private capital for emerging markets requires investment structures that:

- have the right scale for mobilising institutional capital,
- offer wide diversification (geographies, counterparts, asset classes, sectors) to manage risks and target multiple projects,
- use appropriate de-risking instruments such as junior equity, first-loss concessional debt, guarantees, etc.

However, blended finance currently faces several constraints:

- in the current global economic context, ***private investors are even more risk-averse,*** which affects fundraising. This makes the role of catalytic capital even more critical.
- There is a ***lack of standardisation*** of the requirements from institutional and concessional capital providers, who should harmonize their strategies, investment criteria and financial products.
- ***Well-designed regulatory frameworks are needed*** in OECD markets to facilitate the setting up of such structures.

"When we want to go fast, we go alone. When we want to go further, we go together. ***There is high risk perception because we go alone."***

Ecobank

As a consequence, partnerships, **including between public entities from various countries,** are essential to push back the barriers and mobilise capital more efficiently.

While gathering all parties - private capital providers, catalytic capital providers, regulators, potential investees - around the table is necessary, this takes time: a ***long-term perspective and patience*** are needed.

All this is nothing new and has been discussed for 30 years. It may therefore be tempting to propose a completely different approach. If international private capital is not easily accessible, why not rely on local financial institutions such as Ecobank or other local capital providers? As a matter of fact, money is maybe more easily accessible locally.

However, relying solely on one source would repeat the same mistakes. If local financial institutions mobilise local capital through deposits, this only enables them to provide short-term finance. ***What is still missing is long-term external funding that could be blended with short-term local capital to eventually generate real leverage.***

Inclusive finance as a development tool to contribute to the SDGs

Another way to scale up inclusive finance is by highlighting the impact it can generate beyond financial inclusion.

There seems to be no debate about the role that inclusive finance can play in achieving the SDGs:

Impact expected from investing in inclusive finance:

"Improved gender inclusion, strengthened resilience and entrepreneurship, enhanced sustainability practices, more and better job creation"

"access to basic needs"

"just transition"

"more equality"

Fundacion Genesis Empresarial, the largest microfinance institution in Guatemala, is a perfect example of a financial institution that has embedded its impact strategy into its business model. **Offering much more than financial inclusion,** the impact that Genesis aims to generate for its clients goes from **reducing their vulnerability to the economic and social development of their whole household.** To achieve this, Genesis provides financial and non-financial support to its customers along a defined development pathway and closely monitors the progress of customers and their families. Genesis will soon fully revise this development pathway to integrate resilience to climate change among the expected outcomes of its services, reflecting its **holistic impact approach.**

While some private asset impact fund managers keep managing separate inclusive finance funds on the one hand and funds for other sectors or impact objectives on the other hand (such as agriculture, climate, energy, etc.), others have been **investing in inclusive finance institutions with the aim to contribute to various SDGs** for a while. For instance, some impact funds target climate-smart agriculture through local financial institutions, including inclusive finance institutions, and therefore expect to contribute to a variety of development objectives related to food security, environmental conservation or job maintenance and creation through inclusive finance.

"Financial inclusion can lead to financial exclusion if not done with excellence."

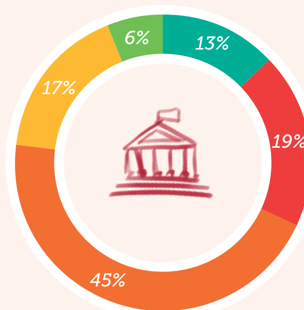
Genesis

If impact intentions and expectations from the actors already investing in inclusive finance are clear, ***making a real difference requires upscaling.*** To do so, mobilising much more capital from **more mainstream financial markets** is essential.

This is where the first challenge lies: the demand for impact or even ESG-oriented finance has tangibly slowed down against a backdrop of war affecting Europe. Investors' priorities have changed. Even though this may be a cyclical phenomenon, a second factor tends to reinforce this trend: the era of low interest rates is over, and ***financial returns are more than ever at the forefront of the investors' expectations.*** Therefore, the question is: can impact investing deliver at least market-like returns?

The ***low level of return of impact investments is indeed cited among the top challenges*** related to impact for investors, coming in third place for all respondents to the questionnaire, but in second place for asset managers.

The main challenges related to impact for investors:



- Identifying the type of impact which is possible to achive
- Identifying potential investees which really have impact
- Mesuring impact
- Low returns of impact investments
- Other

Nevertheless, ***impact measurement was unanimously identified as the main challenge,*** due to:

- the **well-known lack of accessible and good quality data**
- the **absence of a harmonised impact measurement framework.**

While the feasibility of such a common framework has been questioned given the diversity of impact themes, fund structures or local contexts, the message is nonetheless that it must be tried, especially to avoid green and social impact washing, to provide solid evidence and to build investor trust that is essential to keep mobilising more impact-oriented capital.

The harmonisation of such a framework echoes the **harmonisation of rules in general, which is the responsibility of the regulator and is considered as key to tackling current challenges such as climate change.**

However, the current European regulation related to sustainable finance (Sustainable Finance Disclosure Regulation - SFDR) has been criticised for being particularly burdensome and complex, **with the risk of even disincentivising asset managers from impact investing,** given the high operating costs implied by the new rules.

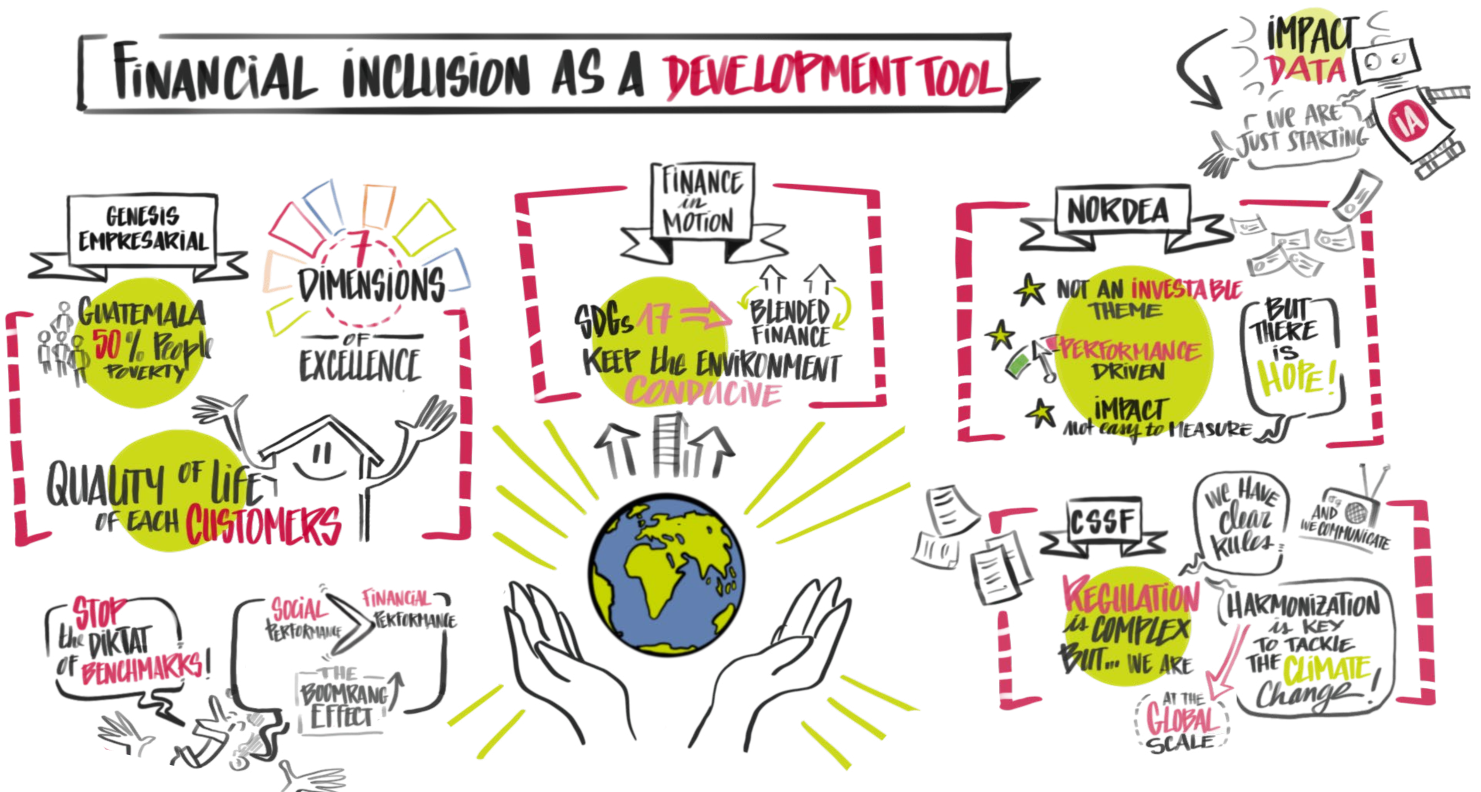
In consequence, **an evolution of the current regulation seems necessary to keep the regulatory environment conducive and enable it to keep playing its role as a facilitator.** So is international cooperation between regulators to ensure interoperability and avoid market fragmentation.

"the tyranny of short-term benchmarks"

In addition, ***it seems inconsistent to expect impact data to be available quickly when patient and long-term capital is required in the first place.***

The temptation to quickly establish impact benchmarks against which to compare oneself has been identified as dangerous, all the more so as **one is often afraid to be too far away from benchmarks, which does not encourage innovation or risk-taking.**

- Nevertheless, it should be stressed that the broader financial sector is still in its infancy when it comes to impact issues. ***Modern technology could accelerate progress in terms of accessibility and harmonisation of impact data,*** thereby boosting what has been achieved with financial data over decades.



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Conclusion

The inclusive finance sector has evolved considerably over the last 30 years. Nevertheless, it still only represents a niche and absolutely must be scaled up to generate impact that makes a difference.

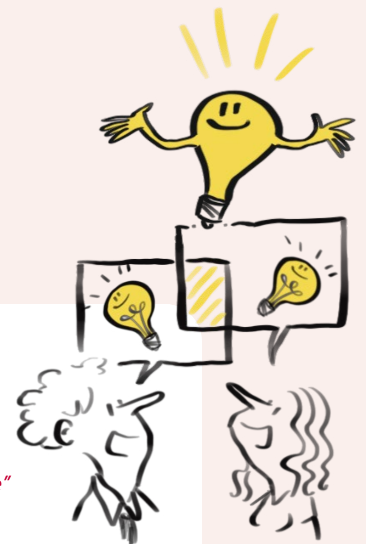
However, certain challenges have persisted throughout all these years – this may give rise to frustrations, but perseverance remains the key.

First,

while risk management mechanisms have evolved, the perception of risk has not. ***We now need to change the mindset.*** And to go further, **we need to go together.**

Therefore, the Luxembourgish financial sector is ***called to action:*** let's sit down at the same table to ***collectively design de-risking solutions.*** Existing platforms in Luxembourg, such as InFiNe, could ideally co-host such an initiative...

LUXEMBOURGISH ACTORS, LET'S COME UP with DERISKING SOLUTIONS



...and initial requests to this end have already been made:

A variety of financial instruments:

"guarantees" *"currency hedging at low cost"* *"flexible and long-term finance"* *"first-loss"* *"more market or investment-oriented technical assistance funds"*

To be provided to:

"a large group of investors" with *"more pooling"* a *"common facility"* *"co-investment with local financial intermediaries"* *"private-public collaboration"* *"cross-border collaboration"*

Along with:

"education of investors and information on investment opportunities in emerging markets" *"data mining"* *"making data public or using already available data"*

Second,

expectations in terms of impact remain very high, regulation is evolving and harmonisation is underway. The Sustainable Development Goals are a widely used analytical framework and technological progress should make data collection and analysis easier. As a result, we need to capitalise on this momentum to make an extra joint effort and collect impact evidence for attracting ever more impact-oriented capital

LET'S MEASURE the CONTRIBUTION OF INCLUSIVE FINANCE TO THE SDGs

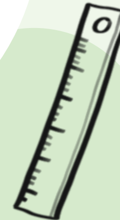
This is a second ***call to action*** to the Luxembourg ecosystem to ***better assess the contribution of inclusive finance to the Sustainable Development Goals by 2030.***

This should be made possible by relying on existing initiatives to **map Luxembourg's contribution to inclusive finance** on the one hand, and on **academic research** led by the University of Luxembourg on the **impact of financial inclusion** on the other hand.

Taking part in these initiatives should help build the inclusive finance of tomorrow.

All actors interested in joining, whether based in Luxembourg or not, **can express their interest to ADA,** which will act as facilitator.

LUXEMBOURGISH ACTORS, LET'S COME UP with DERISKING SOLUTIONS



LET'S MEASURE the CONTRIBUTION OF INCLUSIVE FINANCE TO THE SDGs

Edited by

Expert in inclusive finance, driver of partnerships and innovation

ADA (Appui au Développement Autonome) is a Luxembourgish non-governmental organisation that strengthens the autonomy of vulnerable people by leveraging inclusive finance to improve their living conditions.

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