CARE International Policy Brief

Financial inclusion in Uganda

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SINCE 2001 THE UGANDAN GOVERNMENT has taken steps to double the number of adults accessing formal financial services from 28% in 2009 to 54% in 2013. However, 2.6 million adults remain excluded (15% of the adult population) and usage of insurance products in particular remains low, with only 2% of the adult population reporting use of them.[1]

Broad and inclusive access to formal finance is essential for sustainable development in Uganda. Enabling a greater percentage of the population to access formal services (eg savings, credit and insurance products) can bring significant benefits:

- to individuals (increased security for their funds and the ability to access bigger loans)
- to businesses (reaching emerging markets, diversifying and expanding)
- to the government (supporting more inclusive growth and increased productivity through wider access to finance).

This briefing sets out how Uganda can capitalise upon existing good practice and innovation to become a leader in increasing access to formal finance in the East African region.

THE POTENTIAL

In Uganda 74% (up from 60% in 2009) of the rural poor rely on informal financial services, consisting mainly of community-led self-help groups and welfare funds where they save and loan money amongst themselves. Village Savings and Loan Associations (VSLAs) are particularly popular with the rural poor. Over the last 10 years CARE International in Uganda has helped to facilitate the establishment of 27,222 VSLA groups representing well over half a million people (each group has a membership of 25-30 people). They have saved 51 billion Ugandan shillings (roughly US$19 million). In addition 72% of these groups have taken out loans amongst each other, which includes paying the interest rates set by the groups.[2] Once established, however, many group members demand greater safety and security of their collective funds and increased access to larger loans. There is therefore a huge opportunity to link these informal savers with formal financial service providers, as has already been achieved by Barclays Bank Uganda.

1. CARE International in Uganda VSLA MIS (Management Information System) Data, 2014.

2. CARE International in Uganda VSLA MIS (Management Information System) Data, 2014.

THE EXISTING BARRIERS TO LINKING INFORMAL SAVERS TO FORMAL SERVICES

Based on its experience CARE International in Uganda has observed the following:

- **Lack of regulation leads to a lack of trust in financial services**

There is currently no sufficient regulatory framework for 'Tier 4' institutions which include Non-Deposit Financial Institutions (NDFI), mobile money/internet-based technologies and self-help groups like VSLAs.[3] This absence of licensing, guidelines and oversight results in high financial risks and a loss of confidence in financial services. Current legislation (the 2005 Microfinance Policy) fails to sufficiently recognise the benefits of informal VSLAs as a springboard for sustainable economic empowerment for poor people. Enhanced regulation could improve safety and soundness of the financial system; improve the quality of financial service provision including consumer protection and socio-economic development; and increase access to financial services by the financially excluded population.

- **Lack of regulations to encourage the private sector to bank the un-banked**

Existing laws do not provide incentives or regulations to support inclusive economic growth. This means that many formal financial institutions do not actively seek to reach previously unreached groups such as women and youth, nor are they required to develop new products or adapt their minimum deposit and/or collateral requirements. Instead many people are unable to meet the terms and conditions that come with formal financial services, including collateral and security on loans and expensive processing fees.

- **Limited examples of innovative business models fails to inspire others**

CARE, Plan and Barclays bank have proved that it is possible to link VSLA groups to banks because Barclays agreed to develop a new group savings account and overdraft. They also adapted their joining requirements.

3. The existing laws relevant to Tier 4 lack sufficient guidance on licensing and supervision. These include the Money Lender Act 1952; Companies Act 1961; Non-Governmental Organisations Registration Statute 1989; Cooperative Societies Statute 1991 and Cooperatives (Amended) Bill 1992; Bank of Uganda Statute 1993; Financial Institutions Statute 1993; the Micro-deposit-taking Institution Bill 2002.

More banks have now also started to link VSLA groups including Barclays Bank Uganda, Bank of Africa, Centenary Rural Development Bank, Post Bank Uganda Limited and Opportunity Bank, all using different, innovative delivery channels. The advent of mobile technology offers the potential to link larger numbers of people and reduce overheads for providers. 'Linkage' must also be pursued with caution to avoid poor people being manipulated by the formal financial services expected to protect them (eg very high interest rates). To safeguard the interests of the financially excluded population CARE has distilled its experiences into set principles for linkage, covering issues such as minimum requirements for group eligibility, the importance of financial literacy and avoiding using group savings as collateral. These principles have been distilled and adopted in the international Linking for Change Savings Charter signed by a growing number of banks, donors and NGOs.[4]

- **Low levels of financial education affect the numbers of those wanting to save with formal and informal providers**

Whilst large numbers of poor people are saving in Uganda, 5 million are not. Understanding and education about financial management is very low which reduces the potential number of savers that could become part of the formal system. Reasons for not saving or investing are inadequate information on saving (47%) and lack of money to invest (44%). Whilst demand exists, the use of formal insurance products is low (only 2%) compared to 43% using informal insurance products. Preference for informal insurance products/ services over formal is because individuals can easily join and it is affordable.[5]

RECOMMENDATIONS

CARE International in Uganda therefore strongly urges the government and formal financial institutions to **expedite the amendment and passage of the Microfinance Policy of 2005 taking into account the new developments in the microfinance sector, legibility criteria and the needs of the financially excluded population, mainly women and youth.**

Specific amendments should include:

- Define financial inclusion as 'a state in which all people who can use financial services have access to a full suite of quality services, provided at affordable prices, in a convenient manner, and with dignity for the client'.
- Recognise that VSLAs are one of the most effective mechanisms for financial inclusion that promote a savings culture among many Ugandans especially the poor, improve access to small loans for investment and build a social fund that strengthens resilience to external shocks.
- Develop incentives and regulation to encourage the private sector, including formal banks and appropriate technology providers, to develop pro-poor products, services and education that link informal savings groups to the formal sector, and ensure adoption of the international Linking for Change Savings Charter principles.
- Expediting the finalisation and passage of the Tier 4 microfinance regulatory framework, clearly providing for guidelines for licensing and supervision of all Tier 4 financial institutions with the purpose of improving their efficiency.

4. www.careinternational.org.uk/linking-for-change

5. Economic Policy and Research Center (2013) Uganda 2013 FinScope III report: Unlocking barriers to financial inclusion, see www.eprc.or.ug/data/mresearch/23/2/Research_Reports.html

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Useful references

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