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Access to Credit under the Microscope: Financial Inclusion from Microfinance to Fintech
International Economics Series

Presbitero begins by outlining the importance of access to finance, which could improve household welfare, consumption smoothing and employment outcomes, translating into inclusive economic growth. Notwithstanding the importance of financial inclusion, 1.7 billion people worldwide are unbanked, not only in developing countries. For instance, in the US more than 5% of households are unbanked and 23% do not use credit, with large differences across income levels, as well as race and ethnicity. Hence, programs and policies that can expand the ability of individuals to access credit are extremely important. Both traditional "brick-and-mortar" bank branching expansion programs and Fintech (digital credit) can promote financial inclusion. The lecture focuses on the effects that small community-focused banks have on access to credit—studying a large-scale microcredit expansion program in Rwanda—and then touches upon the opportunities and risks of digital credit, looking at the East Africa's experience.

The analysis of a microcredit expansion program in Rwanda looks at access to credit, focusing on the transition of borrowers from community-focused savings and credit cooperatives (Umurenge SACCOs) to commercial banks. Exploiting detailed and high-quality loan-level data from the credit register, the analysis shows that small community-focused banks can generate positive spillovers to the local economy by reducing information frictions in credit markers and enabling the transition of previously unbanked borrowers to commercial banks. This result could be generalized and applied also to the context of advanced economies.

The government-sponsored microcredit expansion program set up Umurenge SACCO program in each municipality in Rwanda with the goal of providing financial services at low-transaction costs. Analyzing data from the credit register over 9 years around the program, Presbitero and his co-authors show a significant rise in access to credit for previously unbanked individuals. The program also generated positive spillovers to the commercial banking sector. As the newly-created institutions faced lending constraints, a sizable share of first-time borrowers obtained subsequent loans—that were larger, cheaper, and longer-term—from commercial banks, which expanded their branch network in under-served low-risk areas. The individuals switching from Umurenge SACCOs to banks were less risky than non-switchers and not riskier than existing bank borrowers, suggesting that commercial banks "cream-skim"' low-risk borrowers from the pool of newly-banked individuals.

Microfinance institutions play an important screening role for the unbanked population and can serve as a pathway for first-time borrowers to commercial banks. However, in light of less risky borrowers transitioning to commercial banks, microlenders may be left with a pool of riskier borrowers, which may pose risks for financial stability.

Presbitero then proceeds to discuss the rise of Fintech and digital credit in recent years. He outlines the potentiality of digital credit: transaction costs are low; non-traditional data (e.g., digital footprint) can complement standard information and overcome the lack of credit history; loans are approved and disbursed immediately; and about two third of unbanked adults have a mobile phone where they can access digital credit. Yet, digital credit can pose significant threats to borrowers. The digital credit industry is unregulated and loans are expensive, which can lead to spikes in personal debt. Consistent with these concerns, recent survey data show that a large number of individuals who take out a digital credit loan in Tanzania and Kenya are unable to repay their loan on time or default. As this information stays for a few years in the credit bureau, a default on a digital loan will reduce the future ability of these individuals to borrow.