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A STUDY ON THE IMPACT OF

DIGITAL FINANCE ON FINANCIAL INCLUSION

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Abstract:

Ironically, a third or more of the population of developing nations is still not eligible for financial services even in the twenty-first century. Numerous studies that have been done in this direction suggest that including those who are financially excluded in banking results in both individual and social welfare. In order to assist alleviate poverty in developing and emerging economies, the G-20 nations and the World Bank have been driving the push for greater financial inclusion in developing countries since 2010 (GPFI, 2010). Policy makers and academics are paying more attention to the value of digital finance and financial inclusion for reducing poverty and boosting the economy today, largely due to the numerous problems that still exist in Digital currency and mobile technology can cater the needs of small transaction at an affordable cost. Additionally, it can facilitate quicker, more accurate, and accurate bulk transactions. Financial service users, digital finance providers, governments, and the economy all benefit from digital finance and financial inclusion, including increased access to finance for the underprivileged, decreased cost of financial intermediation for banks and Fintech providers, and increased overall government spending. Digital financial inclusion, financial data inclusion, and digital finance are some areas where the discrepancy is highly extensive and is garnering more attention. There hasn't been much focus in the past on the connection between these and the problems they pose for financial inclusion. Therefore, this study looks at how digital finance affects both financial inclusion and the stability of the financial system. This research article investigates the effects of digital finance on financial inclusion and financial system stability, a problem that has not been covered in other studies. It also includes a full overview of digital finance.

Key words: Digital Finance, Financial Inclusion, Financial literacy, Financial Stability.

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Introduction:

Digital financial inclusion aims to provide formal financial services to underserved and financially excluded populations. It involves digital access to and usage of financial services by these populations, typically delivered through mobile phones and similar devices. The goal is to persuade individuals to shift from cash-based transactions to digital financial services.

To achieve digital financial inclusion, it is assumed that the underserved population already has some form of formal bank account and requires digital access for conducting basic financial activities remotely. An effective program should be tailored to meet the needs of these populations, delivered at a sustainable cost for providers and affordable for customers. It is important to ensure that the benefits of digital financial inclusion are understood and embraced by the underserved population.

Digital transactional platforms play a crucial role in enabling digital financial inclusion. These platforms allow customers to make or receive payments, transfers, and store value electronically. They can interact with digital devices, such as point-of-sale terminals, using either digital or analog devices (e.g., mobile phones or payment cards). Retail agents equipped with digital devices can facilitate the conversion of cash into electronically stored value and vice versa.

In addition to basic transactions, digital financial inclusion also extends to the provision of credit, savings, insurance, and securities by banks and non-banks. These services often rely on digital data for targeting consumers and managing risks.

Despite the progress made, there are still significant numbers of unbanked individuals worldwide. According to the Global Findex Database, 1.7 billion adults globally do not have a bank account, limiting their access to mobile banking and mobile money services. Countries like China, India, Pakistan, and Indonesia have large populations without access to bank accounts. However, efforts are being made to increase financial inclusion in these and other nations.

Overall, digital financial inclusion presents an opportunity to bridge the gap and provide essential financial services to underserved populations, potentially leading to economic growth, stability, and improved welfare for individuals and societies.

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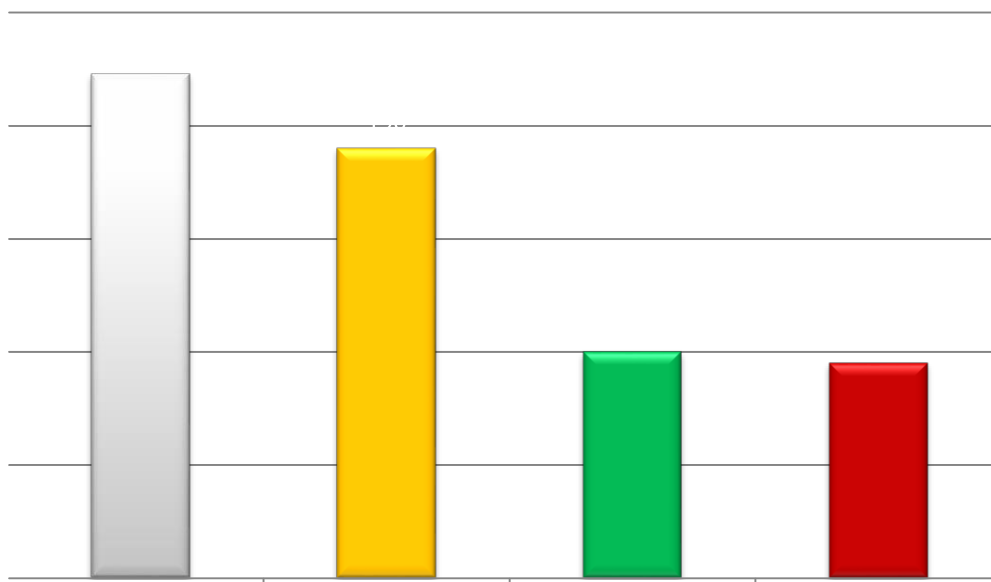

Source: Global Findex Database, 2017

Advantages of Promoting Digital Finance:

Indeed, digital financial inclusion offers numerous benefits that can positively impact individuals, businesses, and economies. Here are some key advantages:

Lower transaction costs: Digital financial inclusion reduces the need for physical infrastructure and paperwork, leading to lower banking transaction costs. This can result in cost savings for both financial institutions and customers.

Enhanced competition and quality services: With the ability to easily switch banks, digital financial inclusion promotes competition among financial service providers. This incentivizes banks to improve the quality of their services to retain customers.

Access for the underserved: Digital finance enables affordable, convenient, and secure banking services for individuals in underserved populations, particularly in developing countries. It allows them to transition from cash-based transactions to digital financial transactions on secure platforms.

Economic growth and stability: Digital finance provides convenient access to a wide range of financial products and services for individuals and businesses, fostering economic growth and stability. It can boost aggregate expenditure, improve GDP levels, and increase financial intermediation.

Reduced physical cash circulation: By promoting digital transactions, financial inclusion helps reduce the reliance on physical cash, which can lead to a reduction in inflation rates, particularly in developing and poor countries.

Expansion of financial services: Digital financial inclusion extends financial services beyond traditional sectors, reaching non-financial sectors such as agriculture, healthcare, and education. This expansion enhances access to basic services for individuals and promotes overall development.

Welfare improvement: Access to reliable digital platforms enables individuals and businesses to carry out financial

transactions and access funds directly from their bank accounts, leading to improved welfare and financial security.

Affordability of digital platforms: To fully realize the benefits of digital financial inclusion, it is crucial to ensure that the cost of obtaining digital transactional platforms such as mobile phones and computers is low or negligible for individuals, especially those in low-income communities.

Government benefits: Digital finance platforms contribute to increased aggregate expenditure, generating higher tax revenue for governments. Additionally, they help reduce the circulation of counterfeit currencies, bolstering the overall economy.

Rural and remote access: Digital financial services can bridge the gap between formal financial institutions and customers in rural and remote areas, improving financial access for individuals who have limited access to physical banks.

Overall, digital financial inclusion has the potential to empower individuals, promote economic growth, reduce costs, and enhance financial services for underserved populations, contributing to a more inclusive and prosperous society.

Disadvantages of Digital Financial Inclusion:

While digital financial inclusion brings numerous benefits, it is important to acknowledge the challenges and risks associated with its implementation. Some of these concerns include:

Novelty risks: Customers may face risks due to their unfamiliarity with digital financial products, services, and suppliers. This can make them vulnerable to misuse and exploitation.

Agent-related risks: Service providers in digital finance are often not subject to the same consumer protection regulations as traditional financial institutions, which can expose customers to potential risks.

Technological hazards: System-wide technological risks can lead to service interruptions, loss of data (including payment instructions), and the potential for privacy or security breaches during the transmission and storage of digital data.

Exclusion of those without digital devices: Individuals who do not have access to mobile phones or other digital devices may be excluded from digital financial services.

Dependency on internet access: Digital finance heavily relies on internet connectivity, which means those without access to the internet may be unable to benefit from these services.

Readiness of the population: The introduction of digital finance in a country should consider the readiness of the population. If people are not prepared or equipped to use digital financial services, it may lead to voluntary financial exclusion.

Transaction costs and exclusion of low-income individuals: Fee-based digital finance platforms may disproportionately benefit high- and medium-income individuals, while poor and low-income individuals may struggle to afford the associated transaction costs, leading to exclusion.

Policy and regulatory challenges: Many policy and regulatory environments may not yet be fully supportive or conducive to facilitating comprehensive digital finance transactions.

Addressing these challenges requires careful consideration of consumer protection measures, technological

resilience, efforts to bridge the digital divide, and creating an enabling policy and regulatory environment that safeguards the interests of all users while promoting financial inclusion.

Review of literature:

Finau et al. (2016): Explored rural dwellers' perceptions of digital financial services (DFS) and identified factors that hindered DFS adoption, such as agents' lack of liquidity and implicit costs imposed on consumers. Additionally, consumers tended to spend funds received through mobile money rather than using their mobile phones for saving purposes.

Ghaffar & Sharif (2016): Examined the level of financial literacy in Pakistan and found that individuals with more financial knowledge tend to save money. The study also revealed that middle-aged and older people were more cautious with their spending, and male respondents exhibited better saving habits. Those earning higher salaries agreed that financial literacy contributes to a financially secure life.

Aggarwal & Gupta (2016): Investigated the relationship between the gender gap in stock market participation and financial literacy, while considering education level and wealth as external factors. The study found that female teachers participate less in the stock market compared to males by 16.7%. This non-participation was attributed to deficiencies in advanced financial literacy and risk aversion.

Totenhagen et al. (2015): Identified key considerations and promising delivery methods to promote positive changes in financial literacy and behavior among youth. The study conducted a comprehensive review of current literature on youth financial literacy education and identified characteristics of financial education programs that influence positive changes.

Hospido et al. (2015): Measured the impact of financial literacy training in compulsory education in Spain. The study used a matched sample of students and teachers in Madrid and employed different estimation strategies. It found that students in private schools did not significantly increase their financial knowledge, possibly due to less intensive program implementation. The study also analyzed the bias arising from non-random selection of schools participating in financial literacy programs.

Arif (2015): Examined the relationship between financial literacy and factors influencing investment decisions.

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The study collected data from 154 respondents using a modified questionnaire and concluded that investors had a below-average level of financial literacy. The study also found significant differences in financial literacy based on age, gender, work activity, and marital status.

Morris & Koffi (2015): Investigated the relationship between the financial literacy level of Canadian university students and their prior education on financial topics. The study revealed that education on financial topics improved financial literacy, but the improvement was insignificant for secondary-level courses. Socio-demographic variables also influenced financial literacy.

Potrich et al. (2015): Explored individual financial literacy levels through socio-economic variables. The study collected data from 1400 participants and used descriptive statistics and multivariate analysis techniques. The results indicated that men without dependent family members and with higher educational and income levels were more likely to belong to the group with high financial literacy levels.

M & M (2015): Examined the financial literacy and its determinants among Gen Y employees in Coimbatore city. The study found that gender, education, income, and age influenced the level of financial literacy. It concluded that financial literacy among Gen Y employees in Coimbatore city was low.

Shih & Ke (2014): Discussed consumer money attitudes, financial literacy regarding financial decisions, and financial behavior. The study suggested that consumers with retention planning and achievement-esteem attitudes toward money made high-risk financial decisions. Anxiety toward money was more prevalent among low-risk investors. Financial literacy influenced consumer financial behavior, and demographic variables played segmentation roles.

Park (2011): Examined the impact of three dimensions of digital literacy on privacy-related online behaviors. The study found that user knowledge

The research methodology described in your statement indicates a descriptive study that aims to assess the degree of digital financial inclusion and literacy. The researcher utilized a structured questionnaire to collect data, drawing from various published questionnaires to develop their questionnaire. The questionnaire primarily focused on aspects related to financial inclusion and literacy, with each region having a digital component.

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The survey consisted of two sections: one for digital financial inclusion and another for digital financial literacy. Each section contained seven sets of questions, and a 5-point scale was used for all items. The responses were scored, allowing the researcher to determine the level of digital financial literacy and inclusion for each individual in the sample.

To ensure the reliability and validity of the questionnaire, the researcher employed Smart PLS version 3 for analysis. A sample size of 200 participants was utilized to measure digital financial literacy and inclusion.

Findings of the study:

- Digital financial inclusion refers to the use of affordable digital methods to provide a range of formal financial services that cater to the needs of underserved and financially excluded communities. It is beneficial for individuals to have a good understanding of the various financial products and services available in the market, as it can help them maximize their own financial well-being. Awareness of digital products and services is crucial as it promotes their usage, leading to economic growth.

- Extending the reach of the banking industry to the financially excluded population has positive effects on both social and individual welfare. The G-20 nations and the World Bank have been driving efforts for greater financial inclusion in developing countries since 2010, aiming to reduce poverty in these economies. Mobile technology and digital currency can effectively address the needs of small transactions at a lower cost. They also enable faster and more accurate bulk transactions. Digital finance and financial inclusion benefit financial service users, digital finance providers, governments, and the economy as a whole. They increase access to finance for underprivileged individuals while reducing the cost of financial intermediation for banks and fintech providers.

- Additionally, fintech providers have the potential to stimulate economic growth by increasing the volume of financial transactions in the financial system, although the effectiveness of this impact is still not fully understood.

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Conclusion:

The provision of financial services through mobile phones and related devices has the potential to enhance access to finance for the population that is currently excluded. This is particularly significant because a significant portion of the excluded population owns mobile phones. By leveraging digital finance, there is an opportunity to promote financial inclusion, provided that individuals have access to mobile phones and reasonable internet connectivity.

The expansion of digital finance can have positive impacts on financial inclusion, especially for low-income and poor individuals. It can improve their access to essential services, thereby enhancing financial inclusion in rural areas. In a country like India, where a substantial portion of the population remains unbanked, there is significant potential for providing digital financial inclusion and banking services.

By leveraging mobile technology and digital platforms, financial services can be made more accessible, convenient, and cost-effective. This can enable individuals who were previously excluded from the formal financial system to participate and benefit from various financial services, such as payments, savings, credit, and insurance. It has the potential to bridge the gap between the unbanked population and formal financial services, thereby promoting financial inclusion and contributing to socioeconomic development.

However, it is important to ensure that efforts are made to address barriers such as limited access to mobile phones, internet connectivity, digital literacy, and trust in digital financial services. Effective regulations and consumer protection measures should also be in place to safeguard the interests of users and maintain the integrity of the financial system.

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