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Opinion - Economy

## How access to finance can reduce poverty

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FINANCE MATTERS.

*Financial products can address income fluctuations, protect savings from inflation, and provide support against economic shocks. However, regulatory issues need to be addressed, before these services are expanded to remote areas.*



Financial services, in all their diversity, can help transform the lives of the poor.

Poverty can be seen in many ways. One aspect that is of specific interest to us is the poverty of income, characterised by the inability of the family to afford the bare necessities of life, and a sense of complete loss of control over its future. A vast majority of our fellow citizens live such lives; they spend most of their time struggling to cope with the present, with little or no strength to dream and plan for a better future for themselves and their children.

If we look closely at the life of a hardworking family, we will find that despite every member putting in enormous effort, if somebody falls ill or the rain fails, all of this hard work is brought to naught. What if a breadwinner dies unexpectedly at the prime of his or her life — where will the money to keep the children in school come from?

Some families would have struggled with their meagre incomes and found a way to invest in gold, or in a patch of land, or in buying a home.

However, when the time comes to draw from these savings they find that inflation or lack of liquidity in the market has eroded most of the gains.

How would these families cope with financial stress? For the most part they don't; they eat less when there is no income, pull children out of school and live with their illness. As a family, they get involved in many different occupations so that if one fails they can fall back on another.

Through this effort, they do buy a measure of protection but at the cost of being unable to build deeper skills, or to focus in any one area that they may be good at. Their life pattern may ensure survival, but perpetuates the cycle of poverty.

TRANSFORMATIVE POTENTIAL

These are very real problems, and the question is: how can access to finance help?

At its core, finance is a service that is only about movement of resources that the family already has — from the present to the future; from the future to the present; from a state of the world in which there is rain to a state of the world in which there is no rain.

Unlike education or healthcare or NREGA, it is not a new input from the outside that can come to the family's assistance. One could, therefore, argue that access to finance is not a tool for poverty alleviation.

However, financial services, in all their diversity, could transform the lives of the poor in some of the following ways:

— A small credit line to manage the seasonality of incomes;

— Safe and accessible savings and investment products that provide inflation-protected returns and reduce a family's exposure to the vagaries of the local economy;

— Insurance products to tide over calamities such as the death of an earning member;

— Loans for an economic activity that enable the user to focus on work, knowing well that if things were to go wrong, savings remain protected along with insurance;

— Wealth management services to help the family understand what these products can do and how they interact with their existing reality.

At a more advanced level, access to finance means a put option on the price of the crop that ensures a farmer gets at least a minimum amount for his crop rather than having to sell it at whatever price prevails in the market.

REGULATORY CHALLENGES

Today, there are technology and business models to take these services to the remotest corners of the country in a viable manner. While a great deal of fundamental work on the regulatory front remains to be done, there are no fundamental barriers to making this approach a reality. However, at some point, regulatory change and service accountability will be called for.

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Today, for example, drugs cannot be sold without safety checks and no surgeon can operate on a patient without being conscious of the fact that should things go wrong he will be called to account; no such accountability exists for the provision of financial services.

In our view, finance, too, has the power not only to transform lives, but also to do enormous damage. Imagine the consequences, if a household that has volatile incomes were to take a loan that has fixed repayment schedules. During months when income is the lowest, meeting repayment dues can render the household more vulnerable than it was to begin with. The person providing the loan would at some point need to be held legally responsible for not having done a proper "diagnosis" before offering the fixed loan. While these are some of challenges in delivering financial services, the inherent power of finance is deeply transformative.

**(This fortnightly column will explore ways in which the power of finance can be unlocked for improving the wellbeing of millions of households.)**

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