Terms of Reference

MODEL ON THE INFLUENCE AND EFFECT OF FINANCIAL INCLUSION ON POVERTY IN MOZAMBIQUE

20 June 2022

Research purpose:

Generate a descriptive model that will enable FSDMoç to identify, measure and analyse the variables that influence the way its financial inclusion initiatives could affect the poverty of households and small businesses in Mozambique.

Context and statements of the issue to be researched:

There are several important knowledge-related challenges involved in improving the structure, legal architecture and functioning of the financial sector in Mozambique so that it reduces poverty and provides the stimuli need for growth and entrepreneurial risk-taking.

Some interesting research on the livelihoods and lives of Mozambicans have produced well-documented normative descriptions that include financial contexts and sectors, but little in the way of descriptions and correlation, let alone causality linkages, between the variables related to financial activity and changes in the variables that define poverty or lifestyle. For example, FinScope's Surveys for Mozambique in 2012 and again in 2019[1] pinpoint some of these variables by noting that there is (a) about 75% of the adult population (16 years and older) do not use any financial products/services neither formal nor informal (i.e. by definition they are financially excluded),a factor that

[1] https://finmark.org.za/system/documents/files/000/000/154/original/Mozambique_Pocketguide_English-2020-07-21.pdf?1597303342#:~:text=The%20objectives%20of%20FinScope%20Consumer%20Survey%20Mozambique%202019%20were%20to%3A&text=To%20describe%20the%20levels%20of,%E2%80%93%20both%20formal%20and%20informal).&text=To%20describe%20the%20landscape%20of,used%20by%20financially%20included%20individuals).

is particularly high in rural areas; (b) about 75% of MSME owners are financially excluded, i.e. they do not use any financial products/services (neither formal nor informal) to manage their business finances, and only 11% are served by formal institutions (banks and formal non-banks); and (c) about half of MSME owners save (mainly at home), but only 5% borrow money (mainly from family and friends), and mostly for cash flow management and not capital investment for growth or productivity. The Finscope analyses describe the statistics relating to individual and household-level financial access and use, but generally use proxy measures on the supply side to do that. FinScope and other sources publish statistics that clearly show that efforts to promote Financial Inclusion have had a significant effect at the meso or macro level (ex., the percentage of people who have access to banking services through digital financial applications has significantly improved), but those statistics don't make the link between FI services and poverty per se (i.e. the benefits to users in terms of poverty mitigation).

The World Bank's (WB) Mozambique Financial Sector Assessment (2009) indicated that the outreach of foreign-owned banks and financial firms that operate in Mozambique (including microfinance) was limited; financial intermediation was also highly segmented focusing on large corporates and salaried employees who had relatively good access to credit already, while for many segments of the population, access to credit and financial services was severely constrained. These conclusions have shaped the country strategy of global financial inclusion for all international financial institutions ever since.

Evidence of the positive relationship between a better functioning financial sector, sustainable economic growth and reduced inequality and poverty is often said to be strong in country-level strategic documents but the fact is that this conclusion is largely based on assumptions concerning correlation and not on evidence-supported research[2]. Moreover, the definition of what constitutes "reduced inequality and

[2] For example, improvements in the percentage of people that have access to bank accounts is assumed to be evidence of reduction in poverty, whereas the experience of places such as India clearly identifies the opposite.

poverty" is not provided to the reader in a way that links any "reduction" to efforts of financial inclusion; For example, if FSDMoç were to invest in an application or a service to improve the access and use of savings groups, how would that ease poverty of those who now had access and use? This knowledge gap has led FSDMoç specifically, and donors generally, to ask how they should prioritize the myriad of investment opportunities they are asked to consider if they cannot relate the expected effects of said investments to manifestations of poverty. What variables of poverty or SMSE growth and sustainability are changed as a result of FI initiatives, and are households and SMSE[3] perceiving that their poverty manifestations are being changed for the better? And FSDMoç believes that these are only a few relevant questions that need to be answered.

A 2013 meta-analysis commissioned by Sida entitled "What works for market development: A review of the evidence"[4] found support for the widely-held proposition that the financial system is crucial for economic development through, for example, its critical role in mobilizing savings, allocating resources, facilitating trading of services and goods, and hedging of risks for economic actors. Economists insist, however, that the correlation is not necessarily causal but contributory. The report also noted that a well-functioning financial system is instrumental for inclusive economic growth as it mobilizes finance for investments and working capital to MSMEs stimulating innovation, growth and job creation. Access to financial services (including credit, savings, insurance, remittances) was found to enable <u>the poor</u> to more effectively deal with shocks and cashflow variations, smoothingtheir consumption, build up human capital and leverage opportunities to expand material assets for economic activities and increase incomes. The study, as are many like it, is essentially at macro and meso levels; it does not deal with direct and observable effects at the micro level. It also focusses

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Further, there is no analysis that empirically makes a link between the services and their effects in terms of well-being related to poverty abatement. For example, just because one has access does not indicate how that affects their well-being (no matter how defined by them), if it does at all.

[3] This ToR has knowingly not included "individuals" as a beneficiary cluster.

[4] https://www.oecd.org/derec/sweden/What-works-for-market-development-a-review-of-the-evidence.pdf

on economic growth rather than poverty abatement; these two concepts are admittedly quite interlinked but they are not synonymous.

In fact, over time, economists have differed in their views on whether the development of the financial system was a cause of economic growth, or a result of it. Over the last decade, researchers have been able to test for the direction of influence and effect and establish that the deepening of the financial system in a country or region leads to growth and not the other way round. There is now a small, but very persuasive set of studies, using cross-country data sets, which show a robust relationship (but not necessarily a definitive causality one) between FSD and growth[5]. Moreover, studies tend to show that financial deepening correlates to poverty reduction.

These findings have spurred the development community to: a) assess what contexts, market conditions and policies are needed for FI to generate poverty reduction, b) define the outcomes that are needed to maximize the effects of financial system changes on growth and poverty reduction, and c) define specifically how the poverty of individuals, households and small enterprises is affected by changes in the financial systems.

Drawing on the joint World Bank and IMF Financial Sector Assessment Program (FSAP) assessment, and the findings of other studies, the World Bank's "Making Finance Work for Africa" recommended that financial systems changes needed to be built on the following three strands: **stability**, especially macro stability; **certainty**, focusing on predictability through, among other things, contract enforcement; and **transparency** of policies and commercial practices. Some macro-level indicators are available to monitor these three strands, but they do not inform on how the strands have physically affected the poor.

[5] For example, see Md Abdullah Omar and Kazuo Inaba, "Does financial inclusion reduce poverty and income inequality in developing countrie?. A panel data analysis", Journal of Economic Structures, 2020, 9:37. This study included 116 development countries. The focus was on an income-based definition of poverty.

In their 2004 text entitled: "Finance, Inequality and Poverty", Beck, Demirguc-Kunt, and Levine[6] found that financial development "causes" faster economic growth and reduces income inequality by disproportionately boosting the incomes of the poor. The authors note in their paper that these results are robust after controlling for other country characteristics and potential reverse causality They also show that almost 30 per cent of the variation across countries in rates of poverty reduction are attributable to cross-country variation in financial development. The study was a landmark in its time, and the concepts and associations between variables are still assumed to be relevant, but the analyses are again at a macro level, focusing on changes in income levels for the poor with correlations being made with improvements in the financial systems in place. None of these studies has concluded on what might be a broad definition of "causality"; moreover, the world has moved on from income-based analysis of poverty to the concept of multi-dimensional poverty. Whereas the former allows for conclusions to be drawn based on a single variable, the latter requires a greater knowledge on effects across a broad spectrum of variables. That is what this ToR wants to adopt as a basis.

A literature search indicates that there is a host of interesting studies that have analyzed the direct impact of FSD, including FI specifically, on poverty, especially in regards to the correlation between:

- Access to finance and child labor. There is indication that in many countries where there is an absence of developed financial markets, households can resort to child labor to cope with income variability[7]
- Access to finance and hunger. Research indicates that financial sector development significantly reduces undernourishment and improves food

[6] https://www.nber.org/papers/w10979

[7] For one of the most scientifically rigorous studies, refer to: https://www.nber.org/papers/w9018. Other authors have confirmed the conclusions of this study but have not developed models to identify effects of changes in the independent variables.

insecurity[8]

- Access to finance and unforeseen shocks, including climate and environmental – In the specific context of SDC cooperation, there is evidence that financial deepening reduces the poor's vulnerability to shocks[9]

These effects have been confirmed by meta studies published in many journals and websites. Multiple studies have documented a robust negative relationship at the country level between indicators of financial depth and the level of income inequality as measured by the Gini coefficient[10]. And they seem to be robust to country contexts, although the CGAP research did not cover Mozambique. For example, in the transition economies, The SECO found considerable positive effect of financial sector development on economic growth in the long term because a well-functioning financial sector is essential for private sector-led growth

A more recent publication, entitled: "Effect of financial inclusion on poverty and vulnerability to poverty: Evidence using a multi-dimensional measure of financial inclusion "[11] came to similar conclusions but was specifically contextualized to Ghana. The authors warned against generalizations to other countries or economies.

While interesting, these types of conclusions found in most research papers, mostly serve to confirm established hypotheses through deductive processes. Organizations such as FSDMoç would still find it a challenge to justify why it should be supporting an FI innovation intervention that could assist in reducing poverty based on these conclusions since it could not monitor the generation of the specific effects associated with poverty abatement. In the same line of thinking, FSDMoç finds it difficult to select, in a rational and evidence-based fashion, those interventions that it should support

[8] Claessens, Stijn; Feijen, Erik. 2006. "Financial Sector Development and the Millennium Development Goals". World Bank Working Paper No. 89.
[9] SECO paper, 2011
[10] Consultative Group to assist the poor (CGAP) Annual Report 2012
[11] Koomson, et al, Network for socioeconomic research and advancement, nesra/wp/20/001

from the field of requests from potential grantees.

The Government of Mozambique (GoM) generally and the Ministry of Economy and Finance (MEF) and the Central Bank of Mozambique (BoM) specifically, have, with the support of FSDMoç, been considering different tools and approaches to tackle the situation but without a great deal of evidence-supported research to help in selecting amongst competing initiatives for support and without a model to help in analyzing (i.e. the due diligence process) the potential poverty abatement effects of the proposed interventions. Logically, since they cannot do that ex ante, they cannot monitor effects or learn in a real time or ex-post context.

Overall then, financial inclusion, which is measured in terms of breadth and depth of the use of the financial system, means that people are able to use multiple products and services (money transfers, deposit accounts, savings, insurance, access to financial education). But again, no research has definitely shown how to identify and then use those variables that can link the financial inclusion outputs to poverty reduction effects in a way that can help MANAGERS to identify what possible poverty-mitigating effects their investments might have. This emphasis on “use” is important: this ToR specifically requests what could be called a “tool” (or a set of tools” to help FSDMoç identify the possible poverty-mitigation effects of its investment decisions.

The FSD programme design as used across Africa is primarily based on correlation-based evidence which shows that improvement in poor people’s access to finance occurs in tandem with reduction income inequality and poverty. For FSDMoç, it is also rooted in an assessment of the financial market in Mozambique conducted incollaboration with the Government of Mozambique (GoM), The Swedish International Development Agency (SIDA), the UK’s FCDO office, the World Bank (WB), and German Development Bank (KFW). Based on that assessment, FSDMoç decided that that its key focus areas would include: (i) macro level interventions to improve policies and regulations that govern the functioning of the financial sector and the data that supports effective policymaking; (ii) meso level interventions to build institutions and infrastructure that support the functioning of the financial sector (like credit reference bureaus, collateral registries, and mobile payment platforms) as well as facilities to support financial service providers in advocacy and training; (iii) micro level interventions focused on working with financial institutions to develop and deliver products and services targeted at poor households and MSMEs as well as working on the demand-side challenges associated with literacy and education, gender discrimination and lack of adequate collateral and property rights. Interventions which target "harder to reach" women customers will be a specific priority.

But again, much of the supporting documentation for these approaches are not necessarily based on effects of poverty in specific terms even though the Theories of Change used by some FSDs Africa are beginning to focus on impact on the poor rather than "access" or "use" of the financial system, as has been the case in the past. Many proxy measures are still used to assume poverty reduction (ex. number of households with bank accounts).

Overall, it can be stated that FSDMoç needs to better understand the causal links between the FI interventions it will support and the effects of these interventions on vulnerable individuals and households in Mozambique; in addition, this knowledge needs to include the effects on the sustainability and growth of SMSEs. FSDMoç also needs to better understand how and why the FI interventions change the way that poverty is manifested in those three cases.

Objective of the mandate:

Provide FSDMoç with a management tool that it can use to support its strategic and operational planning processes, as well as its ongoing operational monitoring and management, in terms of how should its initiatives be configured and deployed so that they directly contribute to poverty abatement for households and SMSE in Mozambique.

Deliverables:

There are five deliverables:

1. An Inception report that lays out the detailed work plans, methodologies and approaches that will be used for the mandate. This report is due four weeks after contract signing. FSDMoç will provide comments to what has been proposed within five working days. A revised version is due five working days after comments are sent back from FSDMoç
2. A progress report delivered by Videoconference and based on a MS PowerPoint package delivered three working days prior to that meeting. The meeting will take place 12 weeks after project signing. This report will deal with progress on the mandate and not on the presentation of a proposed model or its justification unless that is deemed to be a priority on the part of the research team. If decisions are required, they should be briefly outlined in an e-mail that accompanies the MS PowerPoint package.
3. A draft report that meets the objectives of the mandate. The draft report will be due 15 weeks from contract signing. The report will be written in English. No executive Summary is required at this stage. The draft should not exceed 35 pages in length excluding annexes (see next point). FSDMoç will provide comments within 05 working days. A videoconference will be set up at a mutually convenient time before comments are sent in order to exchange ideas on the model proposed and clarify issues if necessary.
4. A final report due 18 weeks after contract signing. The final report, in English, will contain a three-page Executive Summary written in English with a Portuguese translation. The entire report will be of publishable quality and will have been professionally proofread. The final report should not exceed 30 pages in length, not counting Annexes.. Contextual information, methodologies, data, references and notes, and similar content, should be placed in an Annex.
5. A videoconference-based presentation at a workshop that will be organized by FSDMoç. The contractor will have a maximum of 30 minutes to go over the report and its findings in detail, followed by a 60-minute question-and-answer period. A

broad stakeholder audience is proposed.

Proposal

The proposal shall be in two parts: technical and financial. There is no need to send separate documents; both parts may be combined in a single document.

a) The technical proposal

- Shall outline the composition and qualifications of the research team and specify the role that each member will be assigned. It is expected that the team leader will require at least 30% of the total Level of Effort proposed for the entire team.
- An approach and methodology specific to the objective of the mandate will be included, as well as a description of why the proposed approach and methodology are appropriate from a research perspective.
- Annexes will contain two examples of publications or reports (in the same or similar domains as illustrated above) written by the Team Leader (i.e. the TL is the principal author) assigned to the team.
- A table listing recent similar mandates undertaken by proposed personnel (last 10 years) shall be included. Countries where the intervention(s) was (were) carried out need to be specified. Only those mandates that were executed by the people that are being proposed for this mandate should be included.
- The proposal should outline how the model itself will be developed (by whom, based on what, how was the model validated, how was peer reviewing or quality assessment accomplished, etc).
- An updated CV of the proposed team members. The team members proposed must have performed similar studies in Africa before. Previous experience in analyzing poverty effects in grounded research is considered an advantage.
- The reports must be presented in English, with a translation of the Executive Summary to Portuguese.
- A work plan based on a simple GANTT chart that clearly identifies milestones and expected delivery dates for milestones.

- The proposal must state clearly how international team members will conduct their research and collaborate on model-building if they cannot travel.

b) Financial proposal

- The financial proposal shall be stated in Euros at the forex conversion rate found at: https://ec.europa.eu/info/funding-tenders/procedures-guidelines-tenders/information-contractors-and-beneficiaries/exchange-rate-inforeuro_en
- The financial proposal shall include all chargeable items.. The number of days worked for each member of the team, and the daily fee for each team member shall be explicitly stated. Mozambican taxes will not be included in the price.

The proposal must be sent electronically to:

fsdmoc@fsdmoc.org.mz,

The proposal must be received by July 8th, 6 p.m., Maputo time (UTC+2)

Requests for clarifications may be sent to fsdmoc@fsdmoc.org.mz, until June 27th, 6 p.m., Maputo time.

The proposal will be judged on the following basis:

Requirement	**Standard**	**Points maximum**
Methodology	Must be likely to yield valid findings and conclusions.	25
Workplan	Must fit into the timeframe specified in the ToR, represent the best allocation of most qualified team members.	5

Qualifications of team members	Relevant experience in similar mandates involving model building or strategic analysis related to poverty	15
	Relevant experience in financial sector, especially with financial inclusion or financial systems deepening.	15
	Relevant experience in poverty reduction strategies at the ground level	20
	Total technical points	**80**
	Total financial points	**20**
	Total points	**100**

Only those proposals that score a minimum of 50 technical points will be retained for further assessment.

Financial points will be awarded in the following manner: the lowest financial proposal (see condition concerning minimum points for technical proposal) will be awarded 20 points. Other proposals will be awarded the following points:

Cost of lowest proposal (divided by) Cost of "other" proposal (multiplied by) 20 points= Points awarded to "other" proposal

The financial points will be combined with the technical points and the proposal with the highest total number of points will be invited to negotiate a contract. Other firms that have submitted proposals will be advised of the results of this competitive process once the contract is signed.

The invoices will be based on results (deliverables).

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