Chapter 11
Role of Embedded Finance in Increasing Financial Inclusion

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ABSTRACT

The chapter examines the role of embedded finance in increasing financial inclusion. The author shows that embedded finance increases financial inclusion by changing the way banked adults, unbanked adults, and SMEs interact with financial services. Embedded finance also provides greater access to finance for underserved adults and businesses and generates revenue for embedded finance service providers and banks, thereby presenting a win-win opportunity for both the users and providers of embedded financial services.

1. INTRODUCTION

The paper examines the role of embedded finance in increasing financial inclusion. It explores how embedded finance can increase financial inclusion or reduce financial exclusion.

Financial exclusion is a growing problem in many countries (Devlin, 2005; Koku, 2015). Financial exclusion means that people do not have access to formal financial services, and these people are generally considered to be 'unbanked' (Koku, 2015). It is estimated that over 1.4 billion people in the world are unbanked (World Bank, 2022). Many unbanked adults can be found in countries in Asia, South America, and Africa.

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Most unbanked adults are poor and live in economically disadvantaged communities where there is limited means of livelihood, low income and ravaging poverty (Koomson, Kofinti and Laryea, 2023). This makes it difficult for them to earn a good income, rise above poverty and live a good life (Ozili, 2021; Lee, Lou and Wang, 2023). Financial inclusion is often considered to be poverty-alleviating because financial inclusion would give poor communities an opportunity to use affordable formal financial services to start a business, earn an income, rise above poverty, and live a meaningful life (Lee, Lou and Wang, 2023). This has led policymakers in several countries to adopt several strategies to reduce financial exclusion or increase the level of financial inclusion (Shaikh et al, 2023; Lee, Lou and Wang, 2023; Ozili, 2023).

Financial inclusion refers to access and use of affordable formal financial services (Zins and Weill, 2016; Ozili, 2021). Promoting financial inclusion is important in developing countries because it gives economically disadvantaged communities equal access to affordable formal financial services which they can use to improve their welfare and rise above poverty (Park and Mercado Jr, 2018; Ozili, 2018). Policymakers in developing countries are adopting several strategies that can help to increase the level of financial inclusion such as the use of information and communication technology (ICT), Fintech penetration, increasing the number of microfinance institutions, expanding bank branch network, deploying agent banking in rural areas, and using central bank digital currency to promote financial inclusion (Ozili, 2018; Milana and Ashta, 2020; Philippon, 2019; Ozili, 2023).

With regard to ICT, existing literature shows that ICT can be used to broaden financial inclusion by facilitating efficient payments, and helping banks make faster credit decisions (Chakrabarty, 2011; Lapukeni, 2015). ICT also helps to reduce the cost of financial services, thereby making it cheaper for economically disadvantaged communities to access formal financial services (Alshubiri, Jamil and Elheddad, 2019). ICT also facilitates the deployment of cost-saving tools and services (Chu, 2018).

Another ICT-based strategy for increasing the level of financial inclusion that is gaining traction among private sector agents is using embedded finance to advance financial inclusion because embedded finance provides a convenient way to access financial services.

Embedded finance is the seamless integration of financial services into a non-financial platform. Embedded finance provides an opportunity for non-financial companies to offer financial services. It allows customers to access financial services through a third-party application that is embedded in the business of non-financial companies (Ozili, 2022c). The concept of non-financial companies offering financial services or banking services to the public is known as embedded finance. The primary aim of embedded finance is to simplify the entire consumer purchase experience

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