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The Challenges of Financial Inclusion in Developing Countries: A Review

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Abstract

This article examines contemporary research concerning the advancement and difficulties of financial inclusion within developing nations since 2015. It underscores the profound role of digital technology, specifically mobile banking and fintech innovations, in substantially widening the reach of formal financial services and lowering the global population of unbanked adults. Nevertheless, a considerable gap remains between simply having access to these services and their consistent, practical usage. The full, transformative potential of financial inclusion continues to be hindered by systemic obstacles, including weak regulatory systems, deficient infrastructure, and cultural or social limitations. The analysis distinguishes two primary forms of exclusion: involuntary exclusion, which stems from systemic and policy-related hurdles like strict KYC/AML rules; and voluntary exclusion, which is rooted in low financial literacy, a lack of trust, and prevailing cultural attitudes. Although financial inclusion is shown to promote poverty reduction, economic expansion, gender equality, and climate resilience, its benefits cannot be fully realized without extensive, organized reforms. The research emphasizes the critical need for flexible regulatory models, investment in public digital infrastructure, and consumer-focused approaches that cultivate confidence and financial capability. It concludes that financial inclusion should be viewed not as an end in itself, but as a means to achieving equitable and sustainable development. A holistic approach (integrating technology, sound regulation, and inclusive policies) is essential for ensuring that financial inclusion becomes a genuine driver of economic and social transformation in developing economies.

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Introduction

The period since 2015 has marked a pivotal era in the global effort to advance financial inclusion. Driven by rapid technological innovation, the formal financial system has expanded its reach into previously underserved populations at an unprecedented rate. According to Global Findex data, the number of adults without a formal financial account decreased significantly from 2.5 billion in 2011 to 1.4 billion in 2021 (World Bank, 2025) ^[26]. This represents a powerful trend, with 76% of the global adult population now owning a financial account. In developing economies, this momentum is particularly evident, with a 16% increase in the number of adults saving in a financial account between 2021 and 2024, the fastest rise in over a decade (Klapper, Singer, Starita, & Norris, 2025) ^[10].

The engine behind this progress is the widespread adoption of digital technology. An estimated 84% of adults in low- and middle-income countries (LMICs) own a mobile phone, and 3 billion have smartphones, creating a robust channel for the delivery of digitally enabled financial services (Klapper *et al.*, 2025) ^[10]. Mobile money and digital payment systems have been particularly transformative, with their adoption in regions like Sub-Saharan Africa playing a key role in increasing access and successfully

closing the gender gap in financial inclusion (World Bank Group, 2025a) ^[26].

Despite these impressive gains in account ownership, a closer examination of the data reveals persistent and widening disparities. While access has increased, the substantive use of financial services remains a significant challenge. Between 2011 and 2021, the gap in savings rates between advanced economies (58%) and emerging market and developing economies (EMDEs) (25%) widened, as did the gap in borrowing rates, which stood at 56% for advanced economies and 23% for EMDEs (World Bank Group, 2025a) ^[26]. These metrics suggest that having an account does not always translate into meaningful financial activity or improved financial health for many in developing countries (World Bank Group, 2025b) ^[27]. The significant and growing financing gap for micro-, small-, and medium-sized enterprises (MSMEs), estimated at \$5.7 trillion—or 1.5 times the current supply of funding—further underscores this challenge (World Bank Group, 2025a) ^[26]. This shortfall affects 40% of formal MSMEs in developing regions, severely restricting their ability to expand operations, invest in new technologies, and contribute to job creation (World Bank Group, 2025a) ^[26]. This financing gap highlights that the expansion of financial inclusion is not uniform across all segments of the economy; it is a critical point of failure that could undermine overall economic development, even with high individual inclusion rates.

This review provides a comprehensive, evidence-based synthesis of the subject, moving beyond a simple summary of progress to a critical examination of the conceptual debates, strategic policy interventions, and enduring challenges. The report aims to offer a nuanced understanding of the complexities of financial exclusion, drawing connections between disparate findings to inform policymakers, development practitioners, and researchers.

The Concept of Financial Inclusion: A Multi-Stakeholder Perspective

Financial inclusion is broadly defined as the process of ensuring that all individuals and businesses have access to, and are empowered to use, affordable, responsible financial services that meet their needs (CGAP, 2025) ^[6]. This encompasses a wide array of products, including payments, savings, credit, and insurance (World Bank Group, 2025a) ^[26]. Key international organizations, such as the World Bank, IMF, and the Consultative Group to Assist the Poor (CGAP, 2025), have championed this concept as a central pillar of their development agendas (World Bank Group, 2025a) ^[6, 26]. The World Bank, for instance, emphasizes the delivery of these services in a "responsible and sustainable way" to "disadvantaged and low-income segments of society" (Shihadeh, 2021) ^[23]. This collective emphasis on the quality-of-service delivery, its affordability, responsibility, and sustainability, is a crucial and often overlooked aspect of the concept. Merely providing access is insufficient; the services must be tailored to be genuinely useful and ethical for the end-user. The target demographics for these initiatives are consistently identified as marginalized groups, including women, youth, the poor, and small- and medium-sized enterprises (SMEs) (Shihadeh, 2021) ^[23].

A central conceptual development in the field is the shift from a simple focus on financial access to a more profound understanding of usage and quality. The literature clearly distinguishes between having a financial account—a measure

of access—and actively using that account for meaningful transactions, savings, or investments (CGAP, 2025) ^[6]. The Global Findex data itself acknowledges that many individuals with accounts find them to be of little value and consequently do not use them (Klapper *et al.*, 2025) ^[10]. For financial inclusion to lead to substantive economic development, individuals and firms must be motivated to use the services, which requires developing products that genuinely meet their needs (Shihadeh, 2021) ^[23]. This shift in focus, from the quantitative measure of account ownership to the qualitative metrics of usage and utility, indicates a maturing understanding of the subject. The field is moving from a volume-based strategy to a value-based one, recognizing that the ultimate goal is not just to open accounts but to empower people to improve their financial lives. This is a direct response to the observation that high rates of financial access do not automatically translate to improved financial health, as evidenced by the widening gaps in savings and borrowing rates between developing and advanced economies (World Bank Group, 2025a) ^[26]. The underuse of accounts in developing countries suggests a fundamental misalignment between the services offered and the actual needs of the people. This highlights a market failure where financial institutions are not adequately serving the nuanced financial behaviors of marginalized groups (World Bank Group, 2025b) ^[27].

The conceptual framework of financial exclusion has been refined to distinguish between two primary types of barriers: involuntary and voluntary exclusion.

Involuntary Exclusion: This occurs when individuals are unable to access formal financial services due to external factors beyond their control (Ozili, 2021) ^[19]. These barriers are often structural and systemic, including a lack of required documentation for account opening, stringent and burdensome Know Your Customer (KYC) and Anti-Money Laundering (AML) regulations, high service costs, and a lack of physical or digital infrastructure (Gorge & Lazar, 2025) ^[8]. For example, the lack of a formal address system or a national digital ID can effectively lock out a large segment of the population from the banking system (Aidoo, 2025) ^[11].

Voluntary Exclusion: This refers to the deliberate choice by individuals or households to not participate in the formal financial sector (Ozili, 2021) ^[19]. The reasons for this choice are often rooted in personal perceptions and beliefs, such as a general lack of trust in financial institutions, past negative experiences with banks, or cultural and religious beliefs that are hostile to formal finance (Gorge & Lazar, 2025) ^[8]. A preference for informal savings methods, which may feel more secure and accessible, also contributes to voluntary exclusion (Ngonyani, 2022) ^[15].

While conceptually distinct, these two types of exclusion are often intertwined. A lack of money, for instance, can be an involuntary barrier (poverty prevents saving) as well as a voluntary one (one might choose not to use an account due to the perceived high costs) (Gorge & Lazar, 2025) ^[8]. The existence of voluntary exclusion, particularly due to a lack of trust, highlights a systemic failure of the financial system to serve its most vulnerable citizens and underscores the need for a reform of institutional culture and a renewed focus on consumer protection.

The Relevance and Transformative Potential of Financial

Inclusion

Driving Poverty Reduction and Inclusive Economic Growth

The evidence from the literature overwhelmingly supports a positive correlation between financial inclusion and both poverty reduction and inclusive economic growth in developing countries (Saha, Qin, & Inaba, 2023) ^[22]. At the micro-level, access to financial services like savings accounts, credit, and insurance allows households to cope with emergencies, plan for the long term, and invest in productive activities (Omenihu *et al.*, 2024) ^[17].

At the macro-level, financial inclusion plays a critical role in fostering economic growth. A study of 104 developing countries from 2004 to 2019 found that financial inclusion positively correlates with economic growth, primarily by expanding opportunities for low-income individuals (Business Money, 2025; Saha *et al.*, 2023) ^[5, 22]. By providing affordable credit to SMEs, which are the backbone of many developing economies, financial inclusion fuels entrepreneurship and job creation (World Bank Group, 2025a) ^[26]. Examples from India and Kenya demonstrate how mobile payment systems and digital lending platforms have enabled businesses to thrive in the absence of traditional banking infrastructure (Business Money, 2025) ^[5]. This "leapfrogging" effect, where developing economies bypass traditional banking systems by adopting new technologies, is a crucial strategic consideration. It implies that the path to financial inclusion may not be to mimic Western models but to build new, digitally-native ones that can address the barriers of cost and physical distance.

Empowering Women and Enhancing Social Equity

Financial inclusion is a powerful tool for promoting gender equality and women's economic empowerment (Business Money, 2025) ^[5]. By reducing barriers to economic participation, financial services equip women with the tools to start businesses, manage household finances, and invest in their futures, thereby strengthening their decision-making power and promoting broader social and economic equality (World Bank Group, 2025a) ^[26]. The gender gap in account ownership in developing countries narrowed from 9 to 6 percentage points between 2017 and 2021, and early evidence suggests that mobile money has been instrumental in this progress, particularly in Sub-Saharan Africa (World Bank Group, 2025a) ^[26].

Building Resilience to Shocks and Climate Vulnerability

Financial inclusion plays a vital role in building resilience against unforeseen economic and environmental shocks. Financial services such as savings, insurance, and efficient payment systems help people anticipate, absorb, or recover from shocks, such as unexpected health expenses or climate change-related weather events (World Bank Group, 2025a) ^[26]. This is particularly critical in developing economies, where a single shock can trap a household in a cycle of poverty. The link between financial exclusion and climate vulnerability is a crucial, interconnected challenge. Over 80% of the world's 1.4 billion adults without financial accounts reside in places at risk from climate change, intensifying their susceptibility to economic and environmental shocks (World Bank Group, 2025a) ^[26]. Financial services can provide the capital and tools for individuals to invest in climate-resilient infrastructure, adopt sustainable agricultural practices, and speed up recovery from environmental shocks (World Bank

Group, 2025a) ^[26]. This creates a self-reinforcing loop where financial inclusion is both a tool for climate adaptation and a prerequisite for poverty alleviation in a world of increasing environmental volatility.

Financial Inclusion: Policy Instruments and Strategic Interventions

The Rise of National Financial Inclusion Strategies (NFIS)

Since 2010, more than 60 nations have either launched or developed National Financial Inclusion Strategies (NFIS) to accelerate progress (World Bank Group, 2025a) ^[26]. An NFIS provides a coordinated, multi-stakeholder platform for governments to define objectives, identify obstacles, and outline a prioritized set of actions (World Bank, 2021) ^[25]. This approach brings together diverse stakeholders, including financial regulators, ministries of telecommunications, and even agriculture and education, which is a critical innovation in policy-making (World Bank Group, 2025a) ^[26]. The move to NFISs represents a departure from ad-hoc, siloed interventions towards a more structured and collaborative approach. It acknowledges that financial exclusion is not just a banking problem but a cross-sectoral challenge with roots in infrastructure, education, and social norms.

Leveraging Digital Public Infrastructure

The development and leveraging of digital public infrastructure have emerged as key policy instruments. A prime example is India's Aadhaar initiative, a universal digital identification system that has provided over 1.2 billion residents with a digital ID, facilitating the opening of new bank accounts and addressing the primary barrier of a lack of formal documentation (World Bank Group, 2025a) ^[26]. This strategy represents a powerful example of a public good approach, where the government builds the foundational "plumbing" of a digital financial ecosystem, ensuring that the benefits of private-sector innovation are broadly accessible. Leveraging government payments has also proven to be an effective tool. In low-income countries, 35% of adults who received a government payment opened their first financial account, demonstrating a powerful and scalable way to onboard the unbanked into the formal financial system (World Bank Group, 2025a) ^[26]. Furthermore, the establishment of modern payment systems and credit information bureaus is foundational to building an efficient and inclusive financial sector, enhancing both efficiency and overall productivity (World Bank Group, 2025a) ^[26].

Regulating for Innovation: The Role of Regulatory Sandboxes

As fintech continues to evolve rapidly, regulators in developing countries face the complex challenge of balancing innovation with consumer protection (Mandic, Markovic, & Zigo, 2025) ^[12]. Overly stringent regulations can stifle new companies, while a lack of oversight can expose users to risks like fraud and data breaches (Pareek, Maidullah, & Soni, 2025) ^[20]. In response, a growing number of countries have adopted "regulatory sandboxes" (Mandic *et al.*, 2025) ^[12]. This policy instrument allows fintech companies to test new products in a controlled environment with limited regulatory obligations and built-in safeguards for consumers (Mandic *et al.*, 2025) ^[12]. Countries like Singapore, Lithuania, and the UK have successfully implemented sandboxes to foster innovation while maintaining regulatory certainty (Mandic *et*

al., 2025) ^[12]. This proactive and adaptive approach by regulators acknowledges that traditional, rigid frameworks are ill-suited to the dynamic nature of fintech, and a more collaborative, "try-and-see" model is needed to build a resilient financial system.

The Challenges and Barriers to Financial Inclusion

Despite the significant progress in expanding financial access, a range of deep-seated challenges continues to impede the path to full financial inclusion in developing countries. These barriers are multifaceted and often interconnected, spanning regulatory, infrastructural, demand-side, and socio-cultural domains.

Regulatory and Compliance Hurdles

One of the most significant challenges is the prevailing regulatory landscape. Many vulnerable nations lack a well-established regulatory framework for fintech, creating uncertainty for both service providers and consumers (Mandic *et al.*, 2025) ^[12]. The necessity to obtain licenses and adhere to stringent compliance requirements can be cumbersome for startup fintech firms, stifling innovation and limiting the range of products available to the underserved (Mandic *et al.*, 2025) ^[12].

A critical and widely discussed challenge is the unintended exclusionary impact of Anti-Money Laundering (AML) and Know-Your-Customer (KYC) regulations. While these measures are essential for national security and financial integrity, they can unintentionally marginalize low-income and underbanked populations (Aidoo, 2025) ^[1]. The requirement for formal documentation, such as proof of address, effectively locks out individuals in areas without formal address systems or those who live in the informal economy (Aidoo, 2025) ^[1]. The conflict between the goals of financial integrity and financial inclusion reveals a systemic contradiction: policies designed to fight financial crime can inadvertently exclude millions of legitimate citizens from the formal financial system. The path forward is not a simple technological fix but a fundamental re-evaluation of regulatory philosophy, moving from a rigid, one-size-fits-all approach to a risk-based framework that is more proportionate and adaptive to the realities of developing economies.

Infrastructural and Digital Divide Constraints

The expansion of digital financial services is critically dependent on a robust digital and physical infrastructure. In many developing countries, this foundation is fragile or nonexistent. A significant portion of the population faces inadequate internet connectivity, low smartphone penetration, and inconsistent or nonexistent electrical access, particularly in rural and remote areas (Mandic *et al.*, 2025) ^[12].

A GSMA report indicates that approximately 28% of individuals in Sub-Saharan Africa lack access to mobile internet services, and in countries like Nigeria and Congo, the development of mobile payment systems is often hindered by fragile energy infrastructure (Sirakaya & Erturk, 2025) ^[24]. Furthermore, the lack of robust digital identity systems prevents many individuals from registering for financial services (Sirakaya & Erturk, 2025) ^[24]. This multi-layered problem, where financial inclusion is contingent on the availability of reliable internet, consistent electricity, and a digital ID, highlights a key vulnerability in a digital-first

strategy. It demonstrates that financial inclusion and digital inclusion are two sides of the same coin, and one cannot succeed without the other, demanding integrated policy solutions across the telecommunications, energy, and finance sectors.

Demand-Side Barriers: The Human Element

Even when financial services are physically and digitally accessible, demand-side barriers can prevent their active use. A key impediment is the low level of financial and digital literacy among many populations in developing regions (Mandic *et al.*, 2025) ^[12]. A GSMA report found that 30% of mobile phone owners in Sub-Saharan Africa avoid mobile financial transactions due to a lack of basic digital skills (Sirakaya & Erturk, 2025) ^[24]. This lack of knowledge is often compounded by a pervasive lack of trust in formal financial institutions, stemming from past negative experiences, high fees, or a perception that the system is not designed for them (Gorge & Lazar, 2025) ^[8]. The cost of services and the perceived lack of money to save or afford account maintenance fees are also significant barriers (Gorge & Lazar, 2025) ^[8]. The perception of high costs and a lack of trust is often a rational response to a financial system that has historically failed to provide affordable, reliable services. This creates a causal loop where a system that fails to provide trustworthy services creates a population that is financially and digitally illiterate and deeply mistrustful. This necessitates a shift in focus from placing the burden on the user to empowering them through robust consumer protection and targeted financial education programs (World Bank Group, 2025b) ^[27].

Socio-Cultural Barriers and Persistent Inequalities

Social and cultural norms are powerful, often invisible, barriers to financial inclusion, particularly for women. While mobile money has been effective in closing the gender gap in account ownership, the research indicates that it has not automatically created equality for women without addressing the underlying cultural and structural obstacles (Sirakaya & Erturk, 2025) ^[24]. In some societies, cultural norms or the decision-making power of male family members may limit a woman's access to mobile devices or her autonomy to use her financial accounts (Sirakaya & Erturk, 2025) ^[24]. This highlights a powerful distinction: a woman may have an account registered in her name, but she may lack the control or ability to use it effectively (World Bank Group, 2025a) ^[26]. This shows that metrics like "account ownership" can be a deceptive proxy for true empowerment, and that a truly effective strategy must go beyond technology to include legal reforms and community-based interventions that challenge entrenched social norms.

Debates on Impact and Sustainability

A critical debate in the literature surrounds the actual, measurable impact of financial inclusion interventions. A systematic review of studies concluded that the effects of these interventions on core economic indicators such as incomes and assets are "small and inconsistent" and "not transformative in scope or scale" (Duvendack & Mader, 2019) ^[7]. The review cautions against the "unrealistic hype" for financial inclusion, comparing it to the earlier over-promising of microcredit and emphasizing the substantial evidence gaps (Duvendack & Mader, 2019) ^[7]. This critique serves as a vital reality check, forcing a deeper examination

of why, despite so much investment and progress, the impact has not been more profound. It suggests that a failure to measure long-term outcomes, focusing instead on simple output metrics like the number of accounts opened, may be masking the true limited effects of these interventions (World Bank Group, 2025b) [27]. The sustainability of these new systems is also questioned, as low-quality digital systems can create financial instability rather than resilience (Sirakaya & Erturk, 2025) [24].

Conclusion

The review of literature from 2015 onward reveals that financial inclusion in developing countries has advanced significantly with the rise of digital technology, yet major gaps remain. While mobile banking, fintech innovations, and supportive policies have broadened access, persistent challenges in regulation, infrastructure, and socio-cultural norms continue to constrain meaningful use of financial services. The findings suggest that financial inclusion is not merely an end goal but a pathway to inclusive economic growth and poverty reduction. Progress depends on a holistic approach that aligns technological innovation with sound regulation, robust infrastructure, and people-centered strategies that build trust, enhance financial literacy, and respect local contexts. When pursued comprehensively, financial inclusion holds the potential to drive lasting and equitable development.

Recommendations for Policy and Practice

Adaptive Regulatory Reform

Policymakers are advised to transition towards flexible, risk-based regulatory systems that encourage innovation while simultaneously safeguarding consumers. Key actions include establishing regulatory sandboxes, streamlining KYC/AML procedures through digital identity mechanisms, and guaranteeing that regulations for new fintech companies are balanced and proportional.

Investing in Digital Public Infrastructure

National governments should prioritize funding for essential infrastructure components: a reliable digital identification system, universal and affordable broadband internet service, and dependable electrical power for all digital tools and services. These three elements collectively form a stable, necessary, and accessible base for advancing a country's digital transformation and guaranteeing universal participation.

Cultivating Trust

Financial Service Providers (FSPs) must counter mistrust by prioritizing the empowerment and security of their customers. This strategy involves three critical steps: focusing on Consumer Protection (implementing clear, equitable policies regarding fees and fraud), ensuring Transparent Communication (using simple language for all service costs and features), and offering Financial Education to supply users with the required competencies. Through these steps, FSPs directly tackle barriers related to consumer demand, thereby building the necessary confidence for marginalized groups to adopt formal services.

Strategy for Integrated Impact

Development professionals should ensure that financial inclusion plans are aligned with wider development targets and evaluated based on their concrete influence on people's quality of life. This necessitates advancing an Integrated Approach through multi-sectoral initiatives that connect finance with goals such as education and gender equality. Furthermore, they must concentrate on Usage and Outcomes, moving measurement practices away from basic access statistics towards gathering reliable data on the real-world effects of services on users' lives.

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