



# From Crisis to Resilience

## The Role of Inclusive Finance in Fragile Countries

May 2024 • William Cook, Dylan Lennox, Sara Murray, and Souraya Sbeih

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# Executive Summary

**F** **RAGILE COUNTRIES ARE BEHIND—AND** falling further behind—their nonfragile peers in measures of poverty and financial inclusion.

By 2030, 26 percent of the world’s population and 86 percent of the world’s lowest income people are expected to be living in fragile countries (OECD 2022). Low-income people in these countries have lower financial and digital literacy, are more risk averse, and invest less than their nonfragile peers. Women living in fragile countries are more likely to lose their livelihoods, experience displacement, and have education interrupted during times of crisis.

Simply put, in fragile countries, those furthest behind are being left even further behind, putting in extreme peril the chances of the global community meeting its development goals.

When financial services are designed as inclusive, they play an important role in building resilience and creating opportunities for those living in poverty in fragile countries. Research shows that products like savings, insurance, and payments can help smooth consumption and allow users to better respond to crises. Yet while countries like India, Kenya, and Brazil build on decades of progress in inclusive finance, more fragile countries struggle to achieve similar gains.

This working paper is intended for development and humanitarian funders seeking to understand how financial services can work better to improve development outcomes in fragile countries. While learnings are drawn from highly fragile countries, they may apply to other fragile and nonfragile contexts facing acute capacity or governance challenges.

The paper outlines key challenges to advancing inclusive finance in these countries, including:

- **For customers:** More limited access to formal services, at higher costs, and less suited to their needs
- **For providers:** A “triple threat” of reduced revenues, higher costs, and increased risk
- **For the public sector:** Limited capacity and urgent demands, which limits focus on long-term planning
- **For funders:** Providing sustained, coordinated support throughout recurring crises

The paper offers a framework for considering how funders may think about interventions based on a range of different contexts, including dimensions of security, social cohesion, government capacity, and institutional legitimacy. Finally, it introduces some possible levers for change, including:

- Leveraging **humanitarian cash transfers** to help develop the building blocks of the enabling environment for inclusive finance in fragile countries
- Understanding how **informal financial services** can help build or rebuild consumer trust in financial products, especially for rural women
- Improving local **market facilitation** for the financial sector in fragile countries to help bridge longer term divides in market capacity and coordination

Building on this framing over the coming years, CGAP will work at both advocacy and technical levels, increasing awareness of inclusive finance and its links to resilience but also helping to provide the detailed tools and approaches that will drive change.

# What (and where) is fragility?

**T**HERE IS NO SINGLE DEFINITION FOR state fragility. The Organisation for Economic Co-operation and Development (OECD) defines fragility as “the combination of exposure to risks and insufficient coping capacities . . . to manage, absorb or mitigate those risks” (OECD 2022). The World Bank (2020) characterizes fragile situations as “high levels of exclusion, lack of capacity, and limited provision of basic services” and an “inability or unwillingness of the state to manage or mitigate risks.”

While definitions vary, the impact of fragility remains consistent. Food security, child mortality, and gender equity, among other measures, are all worse in fragile countries compared to nonfragile countries. Fragile countries are less able to respond to emergency shocks such as climate events, are more likely to face concurrent crises, and are often unable to deliver basic social, economic, legal, and security services.

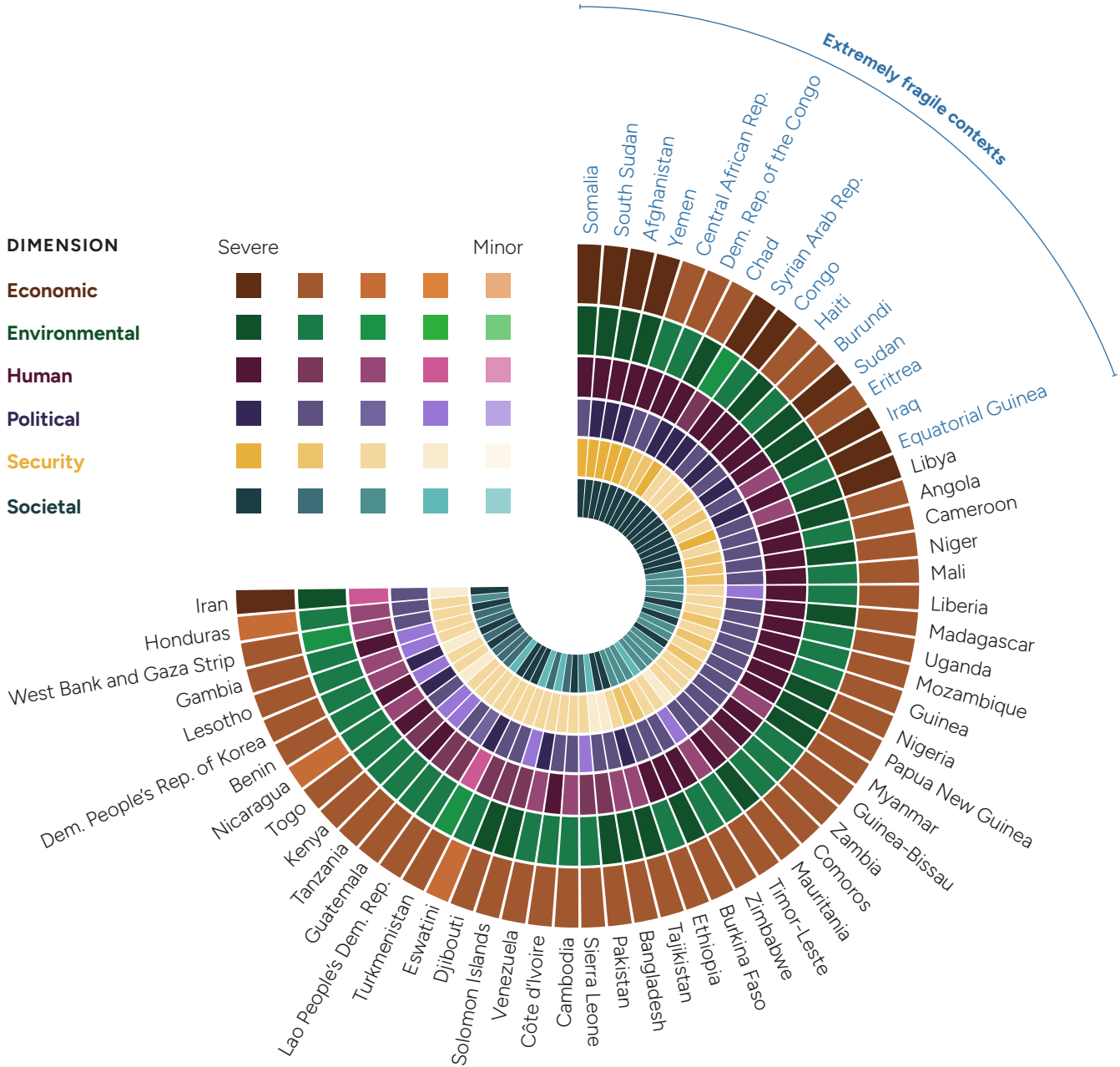
Just as there is no single definition of fragility, there is no single list of fragile countries. Many lists and frameworks exist—from the independent analysis provider ACAPS to the International Rescue Committee (IRC), and from the African Development Bank to the Georgetown Institute’s Women, Peace, and Security Index. These tools can serve very different purposes, for example, to help advocate on topics like gender equity or help prioritize limited resources. They are also dynamic, and change from year to year based on current events.

The list developed based on the OECD’s multidimensional framework tends to be the most widely referenced. It identifies 60 countries as fragile, with 15 of those classified as highly fragile (see Figure 1). Thirty-six of the 60 countries are on the African continent. Latin American countries such as Venezuela, Nicaragua, and Honduras find a place on the list. In Asia, countries as diverse as Myanmar, North Korea, and Papua New Guinea are included.

There is broad agreement on which countries are considered the most highly fragile. Syria, Yemen, and Somalia are among those that rise to the top of most lists. These countries face the most persistent conflict and instability, and are where challenges to development are the most deeply seeded. Frequently, this includes a complete lack of control over the territory, precluding the possibility of national level strategies and solutions.

The content of this working paper broadly focuses on countries the OECD defines as highly fragile. These are the places facing the greatest threats, such as Sudan and Haiti, and include a diverse range of contexts. Afghanistan faces international sanctions and a near collapse of the formal banking sector. The Democratic Republic of the Congo (DRC), despite long-term localized conflict, remains fertile ground for foreign investment with the likes of Equity Bank, Vodacom, Orange, and Airtel playing roles in retail financial services.

FIGURE 1. Fragile countries as identified by the OECD



Source: OECD 2022 (reproduced by CGAP).

Given the varied challenges these markets face, solutions must be similarly adaptable. Addressing inclusive finance requires a variety of tools and approaches depending on context, even within the

same country. The intent of this paper is to begin a discussion around the concepts with the potential to help funders better achieve gains in inclusive finance within the most complex environments.



# Why inclusive finance matters for fragile countries

**T**ODAY, MORE THAN A QUARTER OF THE world's population and three-quarters of its lowest income people live in countries impacted by fragility (OECD 2022). By 2030, the OECD projects the percentage of the lowest income customers living in these contexts will rise to 86 percent. And yet, few of today's most fragile countries are on a remotely solid track to meet the Sustainable Development Goals.

Meanwhile, the magnitude of the challenge is only becoming greater. Over the past decade, more countries have fallen into fragility than have climbed out, contributing to setbacks in development—especially for women and other groups facing social and economic vulnerability.

Climate change is making natural disasters more common, with a fivefold increase over the last half century (McKay and Zetterli 2021). The United Nations estimated that women make up 80 percent of people forcibly displaced by climate-related disasters in developing countries. Active conflict is at its globally highest levels of any time since before the end of the Cold War (Beals and Salisbury 2023). In Africa, one million young people enter the labor force each month yet less than 25 percent find employment. Such demographic shifts are labeled a “major accelerant” to instability (Walsh 2023). The International Monetary Fund (IMF) projects that by 2028, annual global gross domestic product (GDP) growth will reach 3 percent, the lowest forecast in the past 30 years.

In fragile countries, those furthest behind are being left even further behind, putting in extreme peril the chances of the global community meeting its development goals.

The World Bank (2020) notes that while “the best development strategy or program cannot win a war or ensure peace,” development can help people in fragile situations to manage risks, preserve what gains are made, and support countries throughout their transition out of fragility.

Similarly, financial services can act as an enabler to development. Evidence shows that inclusive digital financial services enable 13 of the Sustainable Developments Goals (UNSGSA et al. 2023). But for financial services to contribute to broader development outcomes, they must be designed to intentionally meet the needs of low-income people, especially women, while simultaneously minimizing consumer risk.

**In fragile countries, those furthest behind are being left even further behind, putting them in extreme peril and reducing the chances of the global community meeting its development goals.**

## BOX 1. Resilience to crisis in Sudan

Since April 2023, conflict between two military factions in Sudan has forced nearly 8.1 million people to flee from their homes, with 6.5 million internally displaced. Today, half of the country's population requires humanitarian aid (OCHA 2024). With disrupted electricity, limited supplies of food and water, and violence in the streets, those who remain juggle personal safety with meeting basic needs.

Bankak (the app of the Bank of Khartoum, the largest retail bank in Sudan) played an important role in the early days of the crisis. Customers using Bankak were able to access their funds through agents when branches were shut, digitally pay for goods when carrying cash was not safe, and transfer funds to other parts of the country when travel was not possible due to insecurity. Informal Bankak agents even began to appear in areas like Khartoum, helping to address increased demand for funds withdrawal and over-the-counter (OTC) transfers between customers without bank accounts.

However, the Sudan story is also one of missed opportunities. At the start of the crisis, only an estimated 15 percent of Sudanese held a financial

account (World Bank 2021). While major telecom operators with global experience in mobile money operate in Sudan (e.g., Zain and MTN), the mobile wallet ecosystem is still in its infancy. The policy and infrastructure needed to support these services have only incrementally matured in the face of previous crises and changes in government.

Similarly, the asset-based financing models that support small-scale solar energy in other East African markets are largely absent in Sudan. This means that while electricity is scarce even in urban areas today, the inclusive finance tools that could have helped to meet the moment are simultaneously often absent. Local start-ups had begun to explore the model before the crisis, but the private and philanthropic investment supporting asset-based financing models in nearby countries had largely viewed Sudan as too risky a proposition.

Sudan demonstrates both the potential for inclusive finance to offer resilience in times of crisis and the perils of not supporting the better and quicker development of these solutions.

## Inclusive finance can help people build resilience to cope with shocks, respond to crises, and move toward recovery

In responding to crisis, people often leverage multiple sources of resilience at the family, community, national, and international levels (McKay and Zetterli 2021). Building resilience involves supporting a “range of capabilities, resources, and networks that enable you to anticipate, plan for, and respond to the most important risks” (McKay and Zetterli 2021).

Products like savings and remittances have been shown to help households better manage expenses without

reducing consumption (Storchi et al. 2020). Research has shown that financial tools can help keep women in school (e.g., savings products in Nepal), improve health outcomes (e.g., insurance products in Rwanda and Vietnam), and help to keep the lights on (e.g., asset-based financing in Kenya) (Storchi et al. 2020).

## Inclusive finance can help create opportunity—to build livelihoods and reduce vulnerability

In fragile countries where risks are highest and the picture most dire, there is the temptation to focus the conversation solely on resilience. But without



## BOX 2. Opportunity building through savings groups in Pakistan

The Aga Khan Rural Support Program (AKRSP) is a private, not-for-profit company focused on improving development outcomes in the Gilgit-Baltistan and Chitral areas of northern Pakistan. Founded in 1982 by the Aga Khan Foundation, the organization set out to help local communities in areas that were (at the time) largely disconnected from the rest of the country and beyond the reach of government support.

Building local economic opportunity was a key priority for AKRSP from the start. It achieved this goal in part by seeding local savings groups. Over time, the savings groups became an important source of small/micro enterprise finance in otherwise unserved parts of the country. The program's intentional approach to supporting women (e.g., through support packages that enabled horticultural production) helped many women bring cash into their households

for the first time. This transition increased women's access to savings and credit while also improving their self-confidence and their ability to contribute to longer term planning within the household and community (World Bank 1996).

Today, many of these village and women's organizations (over 4,000 in number) have evolved into regional federations and formalized cooperatives, working alongside newer microfinance and bank products to provide communities with a range of financial opportunities. The program entered Gilgit-Baltistan at a time when these communities were otherwise considered too difficult to serve. AKRSP helped prove the case for financial services offering catalytic opportunity—even in the most difficult operating environments.

creating the opportunity to move beyond vulnerability, resilience is necessarily difficult to sustain. Resilience and opportunity are mutually reinforcing.

Research shows that without the buffers to manage personal financial risk, consumers are, quite logically, less likely to take the financial risks necessary to exploit growth opportunities (Storchi et al. 2020). Best practices in modern "graduation" programming,<sup>1</sup> for example, pair the transfer of productive assets (opportunity) with interventions to meet immediate needs (resilience).

Inclusive finance can also present the opportunity for positively impacting social norms. Models of community-based finance (e.g., informal savings groups) and graduation programming often pair skills-building and community development with financial services. These programs—often explicitly targeted toward women—aim to adapt norms, strengthen

community bonds, and renew social contracts (World Bank 2020).

## Financial services also present risks

Financial services can also undermine resilience, especially in highly fragile situations. Fragile countries often lack the coping mechanisms to respond to even mild shocks, and threats to resilience may be chronic (e.g., insecurity, lack of governance, ongoing conflict).

Stakeholders aiming to influence inclusive finance in fragile countries should, at minimum, ensure a "do no harm" approach, including:

- **Understanding potential impacts on customer financial resilience as new risks emerge.** Products benign in other contexts may threaten

<sup>1</sup> Graduation programming refers to an integrated, carefully sequenced, multi-dimensional intervention to address extreme poverty.

customer resilience in more fragile situations. Political risk, currency instability, and other factors can undermine, for example, the ability to meet repayment obligations as facts on the ground change, particularly for women—who are more likely to lose their livelihoods during times of crisis. Interventions should be assessed for their potential benefits, but also potential risks in the case situations deteriorate.

- **Remaining aware of the institutions and actors that stand to gain.** Fragile countries often have complex political economies, with financial sectors dominated by a small elite with close ties to political circles. An investigation into Lebanon’s 15 largest banks, for example, found that a quarter of all board members met the definition of a politically exposed person (Badil 2023). Interventions should be assessed for how they may inadvertently contribute to the drivers of fragility.

# Challenges to inclusive finance services in fragile countries

**T**HE COMPONENTS OF FINANCIAL market ecosystems must work in tandem to foster financial sector growth (see Figure 2).

Financial services providers (FSPs) need robust, sustainable business models to reach the last mile. Sustainable business models require a strong enabling environment. And both the private and public sector require right-sized support to scale equitable solutions for the lowest income customers. In fragile countries, every aspect of this ecosystem can face challenges (see Figure 3).

## Customers face financial products that are more limited and less suited to their needs

Formal account ownership is 50 percent lower in highly fragile countries as compared to peer countries.<sup>2</sup> Despite similarly vibrant economic lives, individuals in fragile countries are less likely to save or borrow from formal financial institutions, yet only marginally less likely to send or receive remittances (World Bank 2022). Several factors contribute to making individuals less likely to use formal financial services:

- **Lower trust in formal products due to past crises.** Fragile countries more often experience financial

crisis, bank fraud or insolvency, currency depreciation, and similar events that can destroy wealth held in formal financial institutions. While the political elite are more likely able to time the market or maintain offshore holdings, ordinary customers typically feel the full impact of exposure to local markets. Low-income customers can understandably be risk averse to putting money into products that have failed them in the past (see Box 3).

- **Products less suited to their needs.** Despite hosting a disproportionate percentage of the lowest income customers, formal financial products in fragile countries—as in most countries—are typically designed by and for the wealthiest quartile. The lower incomes, less financial and digital literacy, and wider diversity of social norms and constraints experienced by low-income customers mean traditional financial products are often less well-suited to meet their needs. For example, restrictive gender norms and gender-based violence in Papua New Guinea affects 60 percent of its women and girls. Owning a phone or generating income can be a sensitive issue for women in the country. Consequently, designing financial products and services that enable women to save, take loans, or make payments requires special focus. In 2018, Mama Bank took this challenge seriously when it used biometric-enabled solutions to roll out new access points in several markets. This

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<sup>2</sup> Comparisons are based on all countries with available Findex data, comparing highly fragile countries as per the OECD 2022 list and non-highly fragile countries with similar income levels.

FIGURE 2. **The market ecosystem for inclusive finance**

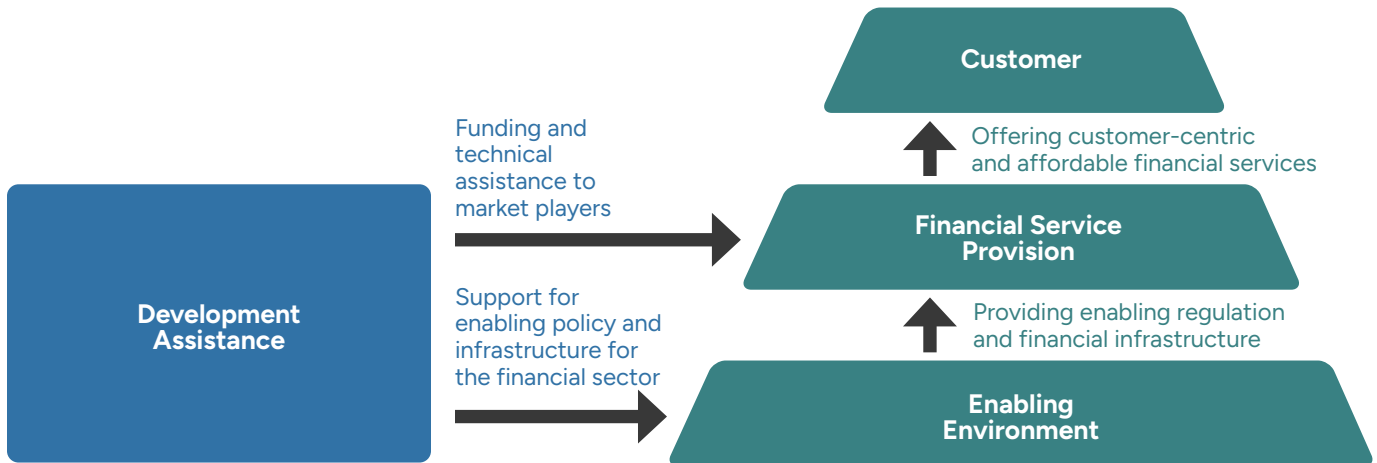
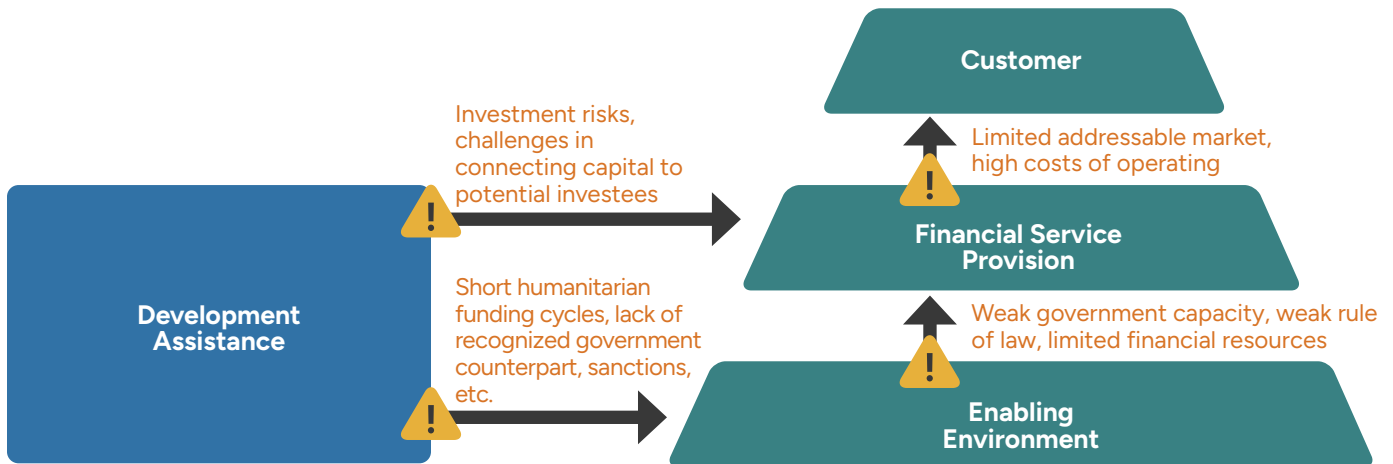


FIGURE 3. **Where inclusive finance market ecosystems can break down in fragile countries**



safety feature helped female account holders identify themselves and prevents male partners from making unauthorized withdrawals from their accounts. Mama Bank grew its mainly female customer base tenfold between 2018 and 2023 due to this safety feature and other gender-led initiatives (CGAP 2022).

- **More limited access to existing products.** For all the reasons noted above, customers in fragile countries are simply less likely to have access to

formal products. The number of commercial banks, microfinance institutions, insurance companies, and mobile money agents are all lower in fragile countries as compared with peer countries.<sup>3</sup> For example, while Mbuji-Mayi, the DRC’s second largest city, has an estimated population of over 2.5 million, the entire Kasai-Oriental region, of which Mbuji-Mayi is the capital, has only seven bank branches.

<sup>3</sup> The International Monetary Fund (IMF) Financial Access Survey data indicates that fragile countries have 8.35 commercial bank branches per 100,000 adults, while non-fragile countries have 21.79 bank branches per 100,000 adults. Similarly, the number of active mobile money agent outlets per 100,000 adults is more than six times lower in fragile countries.

### BOX 3. Losing customer trust in formal products in Lebanon

In 2019, Lebanon was an upper-middle-income country with a vibrant, albeit opaque, financial sector. According to the Global Findex Database, nearly half of the population held a bank account (World Bank 2021). However, cracks in the system began to show as financial engineering by the central bank could no longer mask an emerging banking crisis.

By March 2020, Lebanon's government had defaulted on its debt obligations, sending the financial sector into crisis. Today, poverty in Lebanon has doubled, GDP has contracted by 40 percent, and the country has been downgraded to lower-middle income. The Lebanese currency has lost more than 90 percent of its value, with funds from before the crisis often inaccessible. Some customers have taken buyout offers from banks, earning a fraction of their life savings. Others have resorted to more extreme tactics, such as armed robbery of their own banks to retrieve their savings (Al Jazeera 2022; Goldbaum and Bieber 2023).

Not surprisingly, financial inclusion measured by account ownership has fallen by nearly 60 percent

between 2014 and 2021 as consumers in Lebanon have given up on banks and closed their accounts. Cash is now the norm, and even as banks stabilize and seek to attract new deposits, many customers are choosing to stay out of the formal banking sector as they view financial inclusion as simply not worth the risk. As microfinance actors struggle to raise new lending capital in an environment still deemed too risky, customer demand has also redirected to other sources of politically motivated lending.

"In September 2019, Al Majmoua had \$25 million deposited in local banks in Lebanon. Unfortunately, when the crisis began . . . banks restricted access to deposited dollars, resulting in the devaluation of our funds. Today, the value of what remains of these bank deposits is \$0.10 on the dollar, and we cannot even get them out of the bank. This devastating loss . . . has also pushed us back by 25 years."

—Youssef Fawaz, Executive Director of the Lebanese microfinance institution Al Majmoua, 2024 FinDev interview

## Financial services providers face a triple threat of reduced revenues, higher operating costs, and increased investment risk

For FSPs in fragile countries, a triple threat of reduced revenues, higher operating costs, and increased investment risk hinders the ability to sustainably serve low-income customers. Some of these challenges can be unique to fragile countries while others are merely supersized, including:

- **Reduced revenue.** Customers fleeing the country, customers losing wealth due to factors like inflation, and reduced consumption amid uncertain times can all voluntarily or involuntarily put downward pressure

on financial sector revenue. Banks in Sudan, Haiti, and Lebanon, for example, have tightened lending criteria and voluntarily shrunk their portfolios due to concerns about reduced repayment capacity in the face of crisis.

- **Higher operating costs.** Poor infrastructure, reduced human capital, insecurity, and currency instability can increase operating costs in fragile countries. Providers consistently need to "go it alone" outside major cities, absent roads, cellular towers, and other infrastructure. In Haiti, one former executive stated that running a financial institution felt "more like running a logistics company," where operational needs meant "always firefighting, never building."<sup>4</sup> (See Box 4.)
- **Increased investment risk.** Conflict, insecurity, and corruption make it more challenging to attract

4 CGAP conducted interviews with several representatives from funder organizations and FSPs in some of the projects' countries of focus, namely Haiti, DRC, Mali, Sudan, Yemen, Papua New Guinea, and Afghanistan.

foreign investors. These risks can vary, depending on context: ambiguous land titles creating expropriation risk, security risks making growth unpredictable, or simply uncertainty in regulation and taxation. As a result, financial institutions in fragile countries finance a higher share of investment from retained earnings, often cross-subsidized from other in-country revenue.

#### BOX 4. **Operating challenges in the Democratic Republic of the Congo**

Congolese often jokingly refer to the wealthiest area of their capital, Kinshasa, as the “République de la Gombe” because outside that area, one meets another reality. Public infrastructure is largely deficient in other parts of the city, and more likely absent outside of it. Half of the DRC is inaccessible by road, and only a fifth of the population has access to electricity (World Bank 2021).

This means that in Africa’s third most populous country, as much as 70 percent of potential customers in its population of nearly 100 million are difficult to reach. FSPs operating in more remote areas of the DRC must provide their own power via generators or solar panels, their own security services, and their own telecommunications via satellite links.

Even where infrastructure exists, such as in Kinshasa, FSPs face other challenges. The limited pool of skilled labor makes operating a business a challenge. High, often erratic taxation inflates operating costs, with some providers reporting as many as 111 different taxes. The tax on the profits of telecom operators, for example, reached 50 percent in 2021, making it among the highest in the world.<sup>a</sup> Unsurprisingly, dual accounting is widespread and informality pervasive, creating an even greater challenge for investors supporting the financial sector.

a As per Ministerial Decree 22/11 of March 9, 2022, Democratic Republic of the Congo: <http://www.leganet.cd/Legislation/Dfiscal/Ministeres/AM.009.2022.04.04.2022.html>

## **The public sector faces limited capacity and urgent demands, creating a focus on the day-to-day over long-term market building**

Public institutions in fragile countries are often characterized by limited capacity and weak governance. Limited budgets, along with a flight of human capital, constrain the public sector—even where public servants have the best intentions. In too many countries, this can result in abuse of power for personal enrichment, further deteriorating the public sector’s ability to support sector growth. Challenges include:

- **Limited market planning.** National financial inclusion strategies, national payment strategies, digital strategies, and similar frameworks are all less likely to be found in fragile countries as compared to their nonfragile peers. The market data to monitor progress against goals is similarly often lacking. Financial institutions in countries like the DRC and Afghanistan note a lack of supply-side data to provide even basic information on market positioning or financial inclusion.
- **Limited supervision and enforcement.** While financial regulation in these environments is often better than might be expected, there is typically a wide gulf between what exists on paper and what is enforced in practice. Financial resources, technical capability, and human resources are often too limited to allow for effective oversight. Some regions may also simply be too remote or unsafe to conduct on-site inspections.
- **Limited financial market infrastructure.** In fragile countries, every component of digital public infrastructure (DPI) is less likely to exist or to be well-functioning—from ID to payments interoperability to data sharing. The implication is that the lowest capacity countries, where the focusing of scarce resources is most important, are also the least likely places to find market infrastructure coordination.



## Funders struggle to provide sustained and coordinated support for the financial sector for reasons of strategy, mandate, and incentives

Direct foreign investment makes up a small and shrinking percentage of financing in fragile countries, giving development assistance outsized importance. Yet funders often struggle to provide sustained support to the inclusive finance sector in several ways:

- **Focus on more urgent humanitarian needs leads to shorter term thinking and funding cycles.** A higher share of official development assistance in fragile countries comes as humanitarian aid (OECD 2022, 2023). Such assistance generally does not seek to address longer term ecosystem building and is often programmed in shorter term cycles of six months to one year (Metcalf-Hough et al. 2023).<sup>5</sup> This short-term approach persists despite 92 percent of humanitarian funding (\$32.8 billion) being allocated to protracted crises in 2022 (Development Initiatives 2023). For reasons of both mandate and operational constraints, humanitarian support is often limited in its ability to support sustainable, locally-led growth.
- **Prioritization of scarce resources can direct development financing to less fragile countries where impact is more assured.** Internal investment frameworks, reputational concerns, and shareholder requirements all limit the ability of development institutions to support fragile countries. Especially where resources are constrained and more stable countries offered better chances of impact, financial sector support can be steered away from the most fragile environments. As the Council

on State Fragility notes, “there is a gap between aspiration and reality” such that support remains “limited and broadly unsatisfactory” (IGC 2022).

- **Coordination mechanisms for funder support are more often absent.** Local market facilitators, such as the Financial Sector Deepening (FSD) Network in Africa, are less often found in fragile countries. This means that in situations where roles for neutral, nongovernmental support and coordination are even more important (e.g., in countries where development funders are unable to work directly with the government), these channels are also more likely to be missing or under-resourced.

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<sup>5</sup> Humanitarian funding is generally organized around single-year humanitarian response plans (see <https://response.reliefweb.int/locations>). Donors have committed to increasing multi-year funding under the Grand Bargain humanitarian reform agenda, an agreement between 67 of the largest donors and humanitarian organizations that have committed to improving the effectiveness and efficiency of humanitarian action. But in 2022, there were just five multi-year response plans. Even where donors increase multi-year funding, it often gets passed down to front-line responders in single-year agreements. UNHCR reported that just 1.6 percent of its total 2022 partnership expenditure was passed through multi-year agreements, and major international NGOs reported receiving a fraction of their assistance as multi-year support in 2022.

# Supporting new approaches for inclusive finance in fragile countries

**S**UPPORTING INCLUSIVE FINANCE IN fragile countries is difficult and the challenges facing the financial sector are several. They can vary between countries and within countries, and change over time.

However, understanding the elements of fragile situations can help provide a basis for understanding the available tools to support sector development. The World Bank's Fragility, Conflict, and Violence (FCV) unit offers one such framework for understanding these elements, which include:

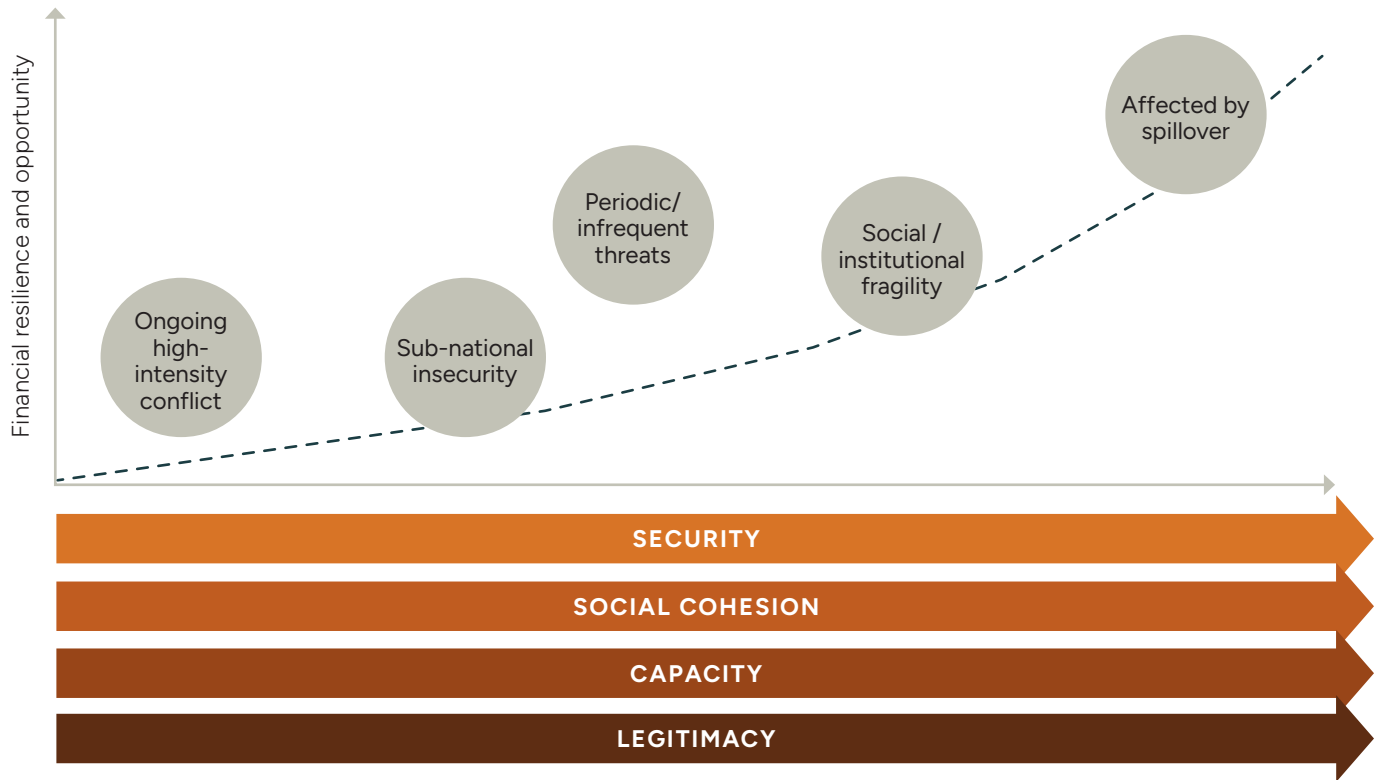
1. **Security:** The degree to which governments are able to protect citizens from violence and insecurity
2. **Capacity:** The extent to which governments and other stakeholders can provide basic services and effectively respond to crises
3. **Legitimacy:** Whether citizens accept and are meaningfully and fairly served by governing arrangements
4. **Social cohesion:** Whether citizens are willing to cooperate among societal groups as well as between society and the government

These elements can come together in various combinations across times and places to inform unique situations, each with its own implications for supporting inclusive finance (see Figure 4).

For example, situations involving **ongoing high-intensity conflict** are likely to involve insecurity in most areas of a country, along with low social cohesion, government capacity, and institutional legitimacy. During times of active conflict in countries like Syria or Sudan, there may be few tools available to advance the inclusive finance discussion.

Alternatively, situations involving **periodic or infrequent threats** may present more targeted challenges to security or social cohesion while maintaining higher levels of government capacity and institutional legitimacy. For example, election violence and climate events periodically impact Papua New Guinea, yet sufficient stability persists that allows the international community to support the expansion of rural financial services and the modernization of government-led social protection systems.

FIGURE 4. Financial resilience and opportunity in the context of fragile situations



### BOX 5. Sudan's journey

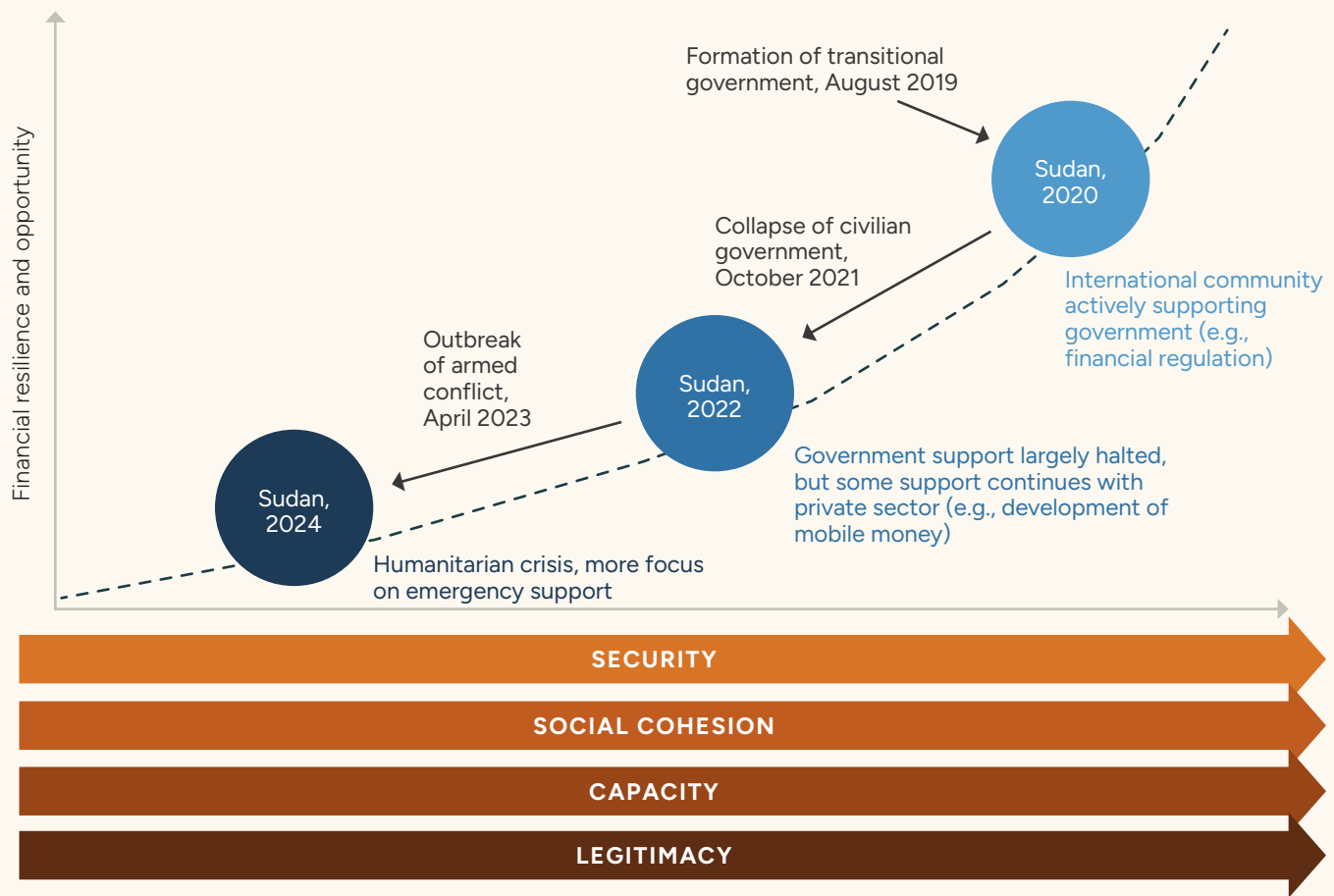
In 2019, hopes for Sudan's future seemed high. Civilian protests had led to President Omar al-Bashir's removal from office. Al-Bashir had led Sudan for the previous 30 years. A transitional government was formed, plans were being made for longer term civilian rule, and the international community reengaged with the country. Support for the new government included work to reform financial regulation and to help design a large-scale social protection scheme (see Figure 5).

However, tensions between factions remained high. In October 2021, a military coup resulted in yet another change in government. The coup was widely condemned by the international community and support to the government was once again paused as a result. Some support for inclusive finance continued

in the country, but efforts were largely limited to programs implemented through the private sector or U.N. partners (e.g., support to telecommunications operators in launching mobile wallets).

By April 2023, a further rivalry between two leading military generals had spilled into open conflict (see Box 1). As open conflict consumed much of the country, the limited international support that had persisted since 2021 was largely halted due to pervasive insecurity and more urgent humanitarian demands. Today, support for Sudan is almost exclusively focused on the emerging humanitarian crisis, with little room for discussion of financial resilience or opportunity.

FIGURE 5. Financial resilience and opportunity in the context of Sudan



Approaches for supporting inclusive finance in fragile countries must be tailored to the environment, which itself can evolve rapidly, including at the subnational level (see Figure 6).

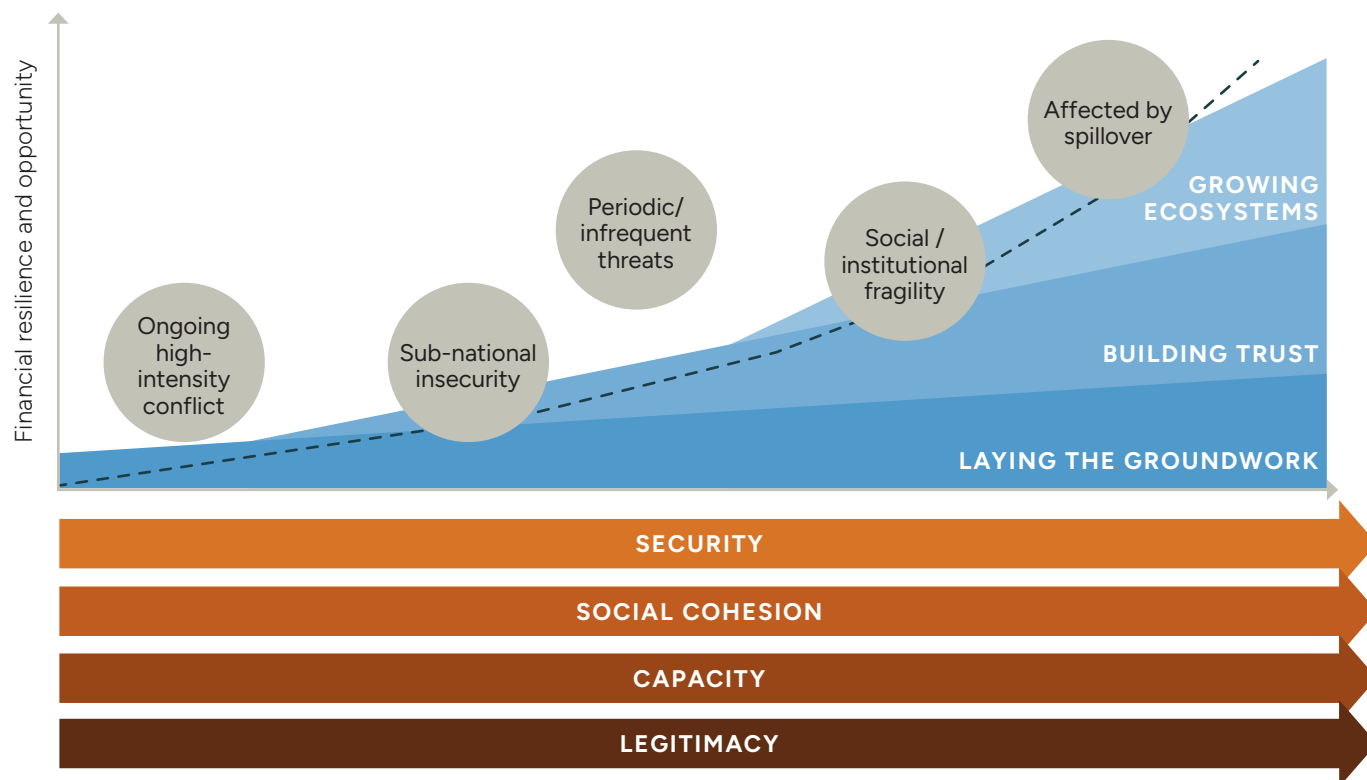
In the most difficult contexts (e.g., situations of ongoing, high-intensity conflict), little may function beyond humanitarian aid. In these situations, the best-case scenario may be to help lay the groundwork for future growth. This may include helping to prevent the destruction of existing financial infrastructure, asking how humanitarian organizations can support local systems or institutions within the mandate of their programs, or helping microfinance institutions to survive a crisis.

It may be possible to support the expansion of financial services in more stable situations, including where basic security is present even if formal institutions are weak or absent. This may include supporting the introduction of new business models (e.g., mobile wallets) where

they do not already exist, supporting last-mile customer engagement through agent networks, or understanding how to work with informal FSPs.

In the most stable conditions, including where formal institutions are recognized even if capacity and popular legitimacy are weak, emphasis can shift toward supporting a wider formal ecosystem. This may include more formal support for the policy and regulatory environment in partnership with financial authorities, the modernization of government social protection systems, or supporting local sector support institutions to help drive ongoing coordination of development community support.

FIGURE 6. **Potential for building financial resilience and opportunity**

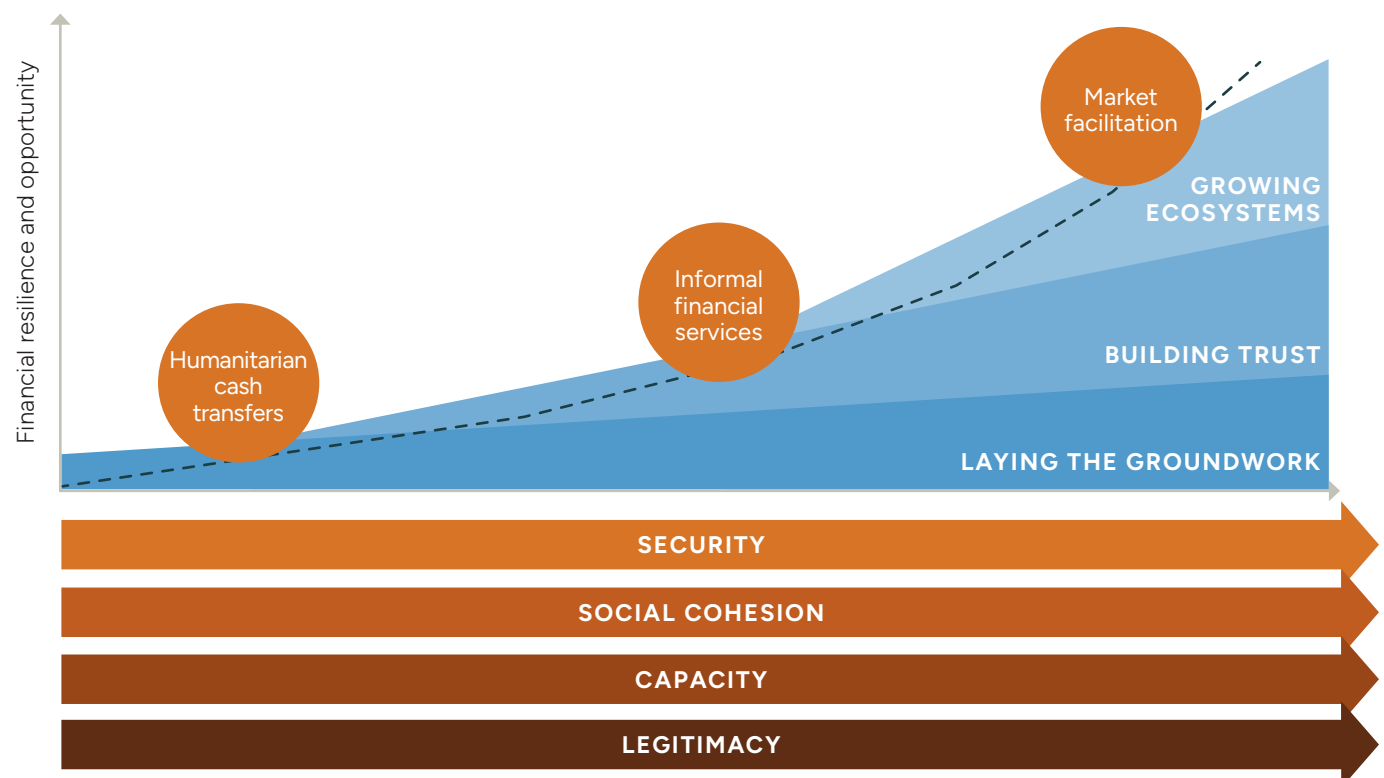


# Moving forward: Focusing on three key levers for financial inclusion

**C** GAP HAS IDENTIFIED THREE potential levers which can support the development of inclusive finance in countries at different stages of consumer trust and financial inclusion. CGAP will conduct research in each area as it supports inclusive finance in fragile countries through both advocacy and technical work (see Figure 7):

1. Leveraging **humanitarian cash transfers** to develop the building blocks of the enabling environment for inclusive finance, especially in situations where security, social cohesion, government capacity, and institutional legitimacy are at their lowest levels.
2. Understanding how **informal financial services** can help build or rebuild consumer trust in financial

FIGURE 7. Areas of CGAP focus in supporting inclusive finance in fragile countries





products, especially for rural women. This is most relevant in situations where security and social cohesion may be higher yet institutional legitimacy remains weak.

3. Improving local **market facilitation** for the financial sector in fragile countries to help bridge longer term divides in market capacity and coordination. This is most relevant in situations where security and social cohesion are higher and where institutional legitimacy is sufficient to support better partnerships with authorities and formal FSPs.

## Humanitarian cash transfers

Humanitarian cash transfer programs are significant and growing in fragile countries, especially where governments are unable to deliver on social protection. Humanitarian cash transfers from United Nations and NGO agencies have nearly doubled as a proportion of humanitarian assistance since 2016 (CALP Network 2022). Beyond helping fragile communities meet basic needs such as food security, cash transfers can offer a first experience with formal financial services.

However, humanitarian solutions often focus on immediate needs over long-term market building. The idea that humanitarian assistance can link to development outcomes has gained attention over the years, resulting in approaches like the humanitarian/development nexus, triple nexus, and cash plus programming. Yet funders often struggle to meet targets for localization of cash programming and similar goals that are steppingstones to supporting longer term resilience (see Box 6).

## Informal financial services

Absent formal financial services that have earned customer trust and reached the last mile, informal services often fill the gap. Some of these tools—such as hawala networks for domestic and international remittances—are fueled by trusted relationships developed over centuries. Other tools, such as informal

### BOX 6. Developing lasting systems in Sudan

In 2020, the World Bank funded the \$400 million Sudan Family Support Program, partnering with Sudan's government with the aim to reach 80 percent of Sudanese families with cash transfers (World Bank 2023). The program involved a range of support to the enabling systems for effective cash transfers, including policy reform, support for financial infrastructure, and work with private FSPs.

However, Sudan's 2021 coup soon forced the program to shut down (see Box 5). Instead of fully transitioning to humanitarian models, the World Bank prepared a program to be implemented through a U.N. partner, the World Food Program (WFP), emphasizing a "build, manage, and transfer" approach. The Resilience Safety Nets Project involved a mandate to develop local systems and maintain a program office staffed by local consultants, with the explicit aim of transferring these resources over to a civilian government once such a partner existed again.

While the subsequent events of April 2023 further disrupted these plans, the resilience project approach from 2021 remains a good example of meeting immediate needs while also planning to support future financial resilience.

savings groups, use localized community trust and present low barriers to entry for rural women.

The commonality among these tools is that they leverage relationships and reputation to operate in situations where trust in formal FSPs may be fundamentally broken. Informal providers also offer products that the formal sector may struggle to deliver efficiently (e.g., low-value loans for women without formal IDs or connectivity). And while informal solutions fill important gaps, they present limitations (including expectations for reciprocity and smaller pools of capital) and risks (including limited oversight, consumer protections, or adherence to global standards including anti-money laundering compliance).

In some fragile markets, informal mechanisms are laying a foundation for more inclusive and longer term financial sector development. For example, formal FSPs are turning toward informal savings groups to help build the trust necessary for agent acquiring in India and loan qualification in Pakistan. Informal money transfer businesses are transitioning into a next generation of formal services providers in Somalia. The international community can do more to embrace these types of linkages in fragile contexts, expanding opportunities for women and other underserved customers whose financial lives are currently dominated by informality (see Box 7).

## Market facilitation

In many developing countries, governments are supported by local market facilitators to help drive progress in the financial sector. These facilitators (e.g., the FSD Network in Africa) help identify and resolve barriers to progress in inclusive finance. They provide institutional memory and often lead the charge in driving change at the country level (e.g., adapted policy, improved business models).

In fragile countries, these institutions can be even more important (see Box 8). The international community may lack the ability to partner with government, financial sector data can be more limited, and private sector partners often need more intensive technical support to grow. Unfortunately, these institutions are also more often absent or under-supported in fragile countries.

### BOX 7. Informal financial services supporting women in Yemen

After ten years of conflict, Yemen has some of the world's lowest gender equity and financial inclusion indicators. To improve access to credit in areas where formal services have struggled to support a business case, Yemen's Social Fund for Development (SFD) has leveraged donor support to establish over 360 village savings and loan associations (VSLAs) with over 8,000 members. Informal financial services like those offered by Yemen's VSLAs are particularly important for advancing economic inclusion among rural women, who can face more restrictive gender norms. By design, VSLAs offer women opportunities to take on new and expanded roles: as entrepreneurs, as leaders within women-only savings groups, and as community leaders through group-funded solidarity projects. And while the average VSLA loan size is smaller for women vs. men (\$91 vs. \$145), it still offers potential for transforming women's futures.

However, credit offered through VSLA group funds is limited and some women are now ready for larger loans and new financial products. Today, SFD is trying to connect VSLA members ready to "graduate" to larger value products with microfinance banks ready to expand. Providers like Al Azal Microfinance Bank and Al-Kuraimi Microfinance Bank are exploring using SFD's VSLA data to reach new client segments with more certainty about who is ready to take on new products and services.

#### BOX 8. MISFA managing through crisis in Afghanistan

The Microfinance Investment Support Facility for Afghanistan (MISFA) was established in 2003, shortly after the end of the first Taliban regime, to help provide technical assistance and funding to Afghanistan's microfinance sector. MISFA was created at the invitation of the Afghan government and funded by international donors to help support the sector's growth in a time of transition.

Flash forward almost 20 years and MISFA once again found itself a key line of support to a microfinance sector in transition. Following the much-publicized U.S. military withdrawal from Afghanistan in August 2021, the country's financial sector was thrown into crisis. Banks limited customer withdrawals. Correspondent banking relations were severed. Exchange rates destabilized. And for the microfinance sector, the installation of an Islamic government under the Taliban put in doubt whether existing lending models could continue or whether collections could be made on existing loans.

By March 2022 it became clear that legacy non-Islamic portfolios would indeed be uncollectable and that moving forward, only Islamic products would be permitted. Absent other revenue streams, local institutions were facing solvency issues. There were also few places to turn for support, with most development assistance to the country halted as of the Taliban's takeover.

MISFA quickly began working with the microfinance sector to help develop a solution. MISFA indefinitely postponed repayment requirements and waived interest on the lines of credit it had extended to the sector. It then began research on new models in Sharia compliant lending, consulting with local actors and making proposals for what might work best in Afghanistan. By September 2022, MISFA had secured approval from the new government for microfinance institutions to resume lending. The microfinance sector had found a way to restart operations even as commercial banks struggled to find their footing.

While Afghanistan's microfinance sector remains under stress from the weight of legacy non-Islamic portfolios on which interest remains uncollectable, the sector has been able to reboot. Today, more than 35,000 clients (37 percent of whom are women) have received loans as part of the newly launched Islamic products. The fast return to lending for the microfinance sector was only possible with the support of a strong local support organization capable of navigating transitions in government, resilient to the flight of the international development community, and technically adept enough to help chart a course forward out of crisis.

# Conclusion

**INCLUSIVE FINANCIAL SERVICES PLAY AN** important role in helping low-income people build resilience and capture opportunities in fragile countries. Financial products may not be able to prevent conflict or bring peace, but when designed as inclusive, they can help low-income people better manage risks during crisis, preserve what gains are made during better times, and achieve the economic growth necessary to support a lasting transition out of fragility.

No single blueprint can address the severity and diversity of challenges to building an inclusive financial ecosystem in fragile contexts. Barriers differ across countries, vary within countries, and change over time. They also span the breadth of ecosystems, including private sector, public sector, and international organizations constraints.

However, for funders supporting inclusive finance in fragile countries, the following basic questions can help guide their approaches.

**In the most difficult situations**, including situations of active conflict, ask:

- What can be done to help prevent the loss of and damage to existing financial infrastructure?
- How can local financial institutions be supported to survive the crisis?
- How can humanitarian organizations support local systems/institutions within the scope of their mandate?

**In more stable situations** where basic security exists even if public institutions are not recognized, ask:

- How does evolving context present new opportunities/constraints for formal financial services, and how can financial institutions be supported to adapt to changing realities on the ground?
- How can funders help inform a rational, risk-based view on informal financial services to help bridge the gap in serving low-income customers?

**In the most stable conditions** where more traditional program-based approaches are possible, including formal engagement with the public sector, ask:

- How can program-based support to financial authorities also serve to improve longer term capacity and legitimacy?
- How can local, nongovernmental sector support organizations be supported to help improve coordination, efficiency, and effectiveness in funder programs?

In the meantime, CGAP will explore in depth the three potential levers identified—humanitarian cash transfers, informal financial services, and market facilitation—across a range of fragile situations to illustrate how funders can support inclusive finance in different contexts.

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