Financial Education to Promote Bank Accounts in Indonesia

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Sector(s): Finance

Location: Various districts, Indonesia

Sample: 564 households from 41 villages

Target group: Rural population

Outcome of interest: Savings/deposits Take-up of program/social service/healthy behavior

Intervention type: Financial literacy Training Monetary incentives

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Savings and investment are widely thought to be important factors in a country's economic growth, but the determinants of demand for financial services are not well understood. Researchers worked with Bank Rakyat Indonesia and the Microfinance Innovation Center for Resources and Alternatives to measure the impact of incentives and financial education on savings account take-up. Results indicated that the financial education program was not an effective tool for promoting the use of bank accounts, but modest financial subsidies did increase the share of households that opened a formal savings account. Overall, these results suggest that take-up of formal financial services may be more easily achieved through measures designed to reduce the price of financial services, rather than through large-scale financial literacy education.

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Savings and investment are widely thought to be important factors in a country's economic growth. However, the determinants of demand for financial services are not well understood, particularly in low-income countries where a large proportion of the population still uses informal financial services such as moneylenders or savings groups. There are two plausible theories that may explain this limited demand for formal financial services in low-income countries. First, because these services involve high fixed costs and are therefore expensive to provide, low-income individuals may not find the services provide sufficient value compared to the user cost. Alternatively, limited financial literacy—knowledge or understanding of financial services and products—may serve as a barrier to demand for financial services: if individuals are not familiar or comfortable with financial products, they are unlikely to try to use them. While these two ideas are not mutually exclusive, they have significantly different implications for the development of financial markets around the world and suggest very different actions for those wishing to expand financial services use.

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In Indonesia, financial literacy is believed to be one of the most important barriers to accessing credit. This may in part be explained by low levels of education: measured as a share of GDP, education expenditures in Indonesia are the lowest in the world. However, and in contrast to many developing countries where access to credit is sparse, the Indonesian banking system has a wide geographical reach. Moreover, Indonesian banks have traditionally offered savings accounts with low minimum deposits designed to serve the needs of low-income customers. The minimum deposit to open a savings account is the nation's largest bank, Bank Rakyat Indonesia (BRI), is only US$0.53, and interest is paid on balances greater than US$1.06. This is significant, considering that the per-capita income in Indonesia is approximately US$1,918. Yet only 41 percent of the total population and 32 percent of rural Indonesia households have a formal savings account.



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In order to measure household financial literacy and its impact on demand for financial services, researchers conducted a household survey in Indonesia between July and December 2007. Around 3,300 households across 112 villages in Indonesia were randomly selected to participate in the survey, which covered financial literacy as well as other household characteristics that might be important determinants of financial behavior, including cognitive ability, educational status, risk aversion, asset ownership, and demographics. The survey results were supplemented by data from a comparable 2006 survey of 1,500 households in India.

After completing the financial literacy survey, each of the unbanked households in Indonesia was invited to participate in a follow-up field experiment, designed to directly test the relative importance of financial literacy and prices in determining demand for

banking services. If a respondent agreed to participate, he or she was subsequently randomly assigned a financial incentive level, ranging from US$3-$14, to open a savings account with Bank Rakyat Indonesia. Half of the respondents were then randomly chosen to attend a two-hour financial training session to be held in the village on a weekend within the month. Researchers worked with Microfinance Innovation Center for Resources and Alternatives (MICRA), an organization that provides consulting and training programs to banks and microfinance organizations in Indonesia, to develop a targeted training curriculum and a two-day training program for all trainers.

Household surveys were complemented by administrative data from Bank Rakyat Indonesia to measure the impact of incentives and the financial education program on savings account take-up.

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The survey results from both India and Indonesia suggest that, while financial literacy is low, especially in India, it is an important predictor of household financial behavior and well-being. Moreover, the demand for financial education seems to be quite high: 69 percent of those invited to participate in the financial education program chose to attend the course.

However, the experimental results indicate that the financial education program was not an effective tool for promoting the use of bank accounts. The program had no effect on the probability of opening a formal savings account, except for households with no schooling, for whom training increased the probability of opening an account by 12.3 percentage points.

Modest financial subsidies, in contrast, had large effects, significantly increasing the share of households that opened a formal savings account within the subsequent two months. An increase in the incentive from US$3 to US$14 increased the share of households that open a formal savings account from 3.5 percent to 12.7 percent, an almost three-fold increase. Follow-up analysis conducted two years after the intervention also showed that households that received the highest incentive were significantly more likely to still have used their bank accounts in the past year compared to those who received the lowest incentive.

Overall, the results suggest that take-up of formal financial services may be more easily achieved through measures designed to reduce the price of financial services, rather than through large-scale financial literacy education.

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