RESEARCH INSIGHTS

Does Adopting Digital Payment for Cash Transfers Improve the Financial Inclusion and Financial Well-Being of Low-Income Households?

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- **Switching from cash to direct deposits of recurrent government benefits into digital bank accounts reduces disbursement errors and increases access to benefits among eligible beneficiaries.**
- **Switching to direct deposits increases ownership of bank accounts, demand for formal loans, and ownership of loans from commercial banks among individuals without a financial history. Individuals without a financial history are less responsive to government encouragement to switch to direct deposits, even though adopting the technology has large potential benefits.**
- **There is no evidence of substantial or significant effects on savings, spending, trust in financial institutions, and other measures of financial well-being.**

CONTEXT

Before the Colombian Department of Social Prosperity's intervention, there was a substantial number of failed cash payment attempts to households eligible for the "*Ingreso Solidario*" program. In-person transactions were burdensome for both the government and beneficiaries and resulted in some beneficiaries losing eligibility. Forty-three percent of payment attempts in cash failed, likely because beneficiaries did not pick up transfers within three months of payment. Furthermore, the transaction cost of each wire was CPO $2,300 pesos, which increased disbursement costs by 20% per payment relative to the transaction costs of directly depositing the transfers into digital bank accounts.

PROJECT

The Colombian government implemented "*Ingreso Solidario*," an unconditional cash transfer program that delivered monthly transfers of CPO $160,000 pesos to beneficiary households from March 2020 until December 2022. The Department of Social Prosperity carried out an intervention to encourage beneficiaries to open a digital simplified saving account and receive direct deposits of their payments. Those who opened a new account also received training on how to use key features of the account. The study analyzes whether adopting digital modes of payment increases the efficiency of program payment transactions and improves the financial inclusion and financial well-being of low-income households.

RESULTS

The intervention increased direct deposits by 7.3 percentage points (pp.), an increase of 73% relative to the control group's mean. Moreover, the probability of owning a bank account 10 months after the intervention started is 6.8 pp. larger in the treatment group than in the control group. Similarly, the probability of owning a digital savings account is 7.9 pp. higher for the treatment group than the control group, representing a 28% increase in the ownership of digital savings accounts. The intervention also increased the probability of having any bank account recorded in credit bureau records during the following two years.

The intervention additionally improved efficiency in the disbursement process and increased access to transfers. In particular, the intervention likely reduced by one tenth the share of eligible beneficiaries who had not received a payment in the past 6 months; individuals who switched to direct deposit due to the intervention received an additional 2.3 payments on average. The improvements in disbursement effectiveness coincide with reductions in transaction costs for the implementing agency because the transactions costs of digital payments are less than those of payments in cash.

Key Concept

FINANCIAL INCLUSION

Access to useful and affordable financial products and services that meet people's needs and are delivered in a sustainable way.

Moreover, the intervention had positive but small overall effects on financial inclusion. There is evidence that the intervention increased ownership of bank accounts, demand for formal loans, and ownership of loans from commercial banks among individuals without a financial history. However, the estimates imply a loan application success rate of only 30%. This suggests that, while cash transfer programs can be a tool to further integrate individuals into credit markets, they will not necessarily address deeper financial failures such as moral hazard or adverse selection.

Finally, there is no evidence of substantial or significant effects on savings, spending, trust in financial institutions, and other measures of financial well-being.

POLICY IMPLICATIONS

The findings provide two important considerations for policy design. First, the individuals who might benefit most from direct deposits may not be those who are most responsive to encouragement interventions. One explanation is that the response to the intervention was very heterogeneous. Individuals who were more familiar with digital tools were more likely to adopt direct deposits. In contrast, financially marginalized individuals were less responsive, even though they were subject to more disbursement frictions and have potentially larger benefits from being integrated into the financial system.

In that sense, the study reveals that light-touch interventions to encourage individuals to adopt financial technologies may not be effective for individuals who face high barriers to financial technology adoption, despite their large potential gains from adopting such technologies. Therefore, the use of low-cost encouragements may need to be complemented with other policy tools to reduce barriers to adoption of digital financial technologies.

Second, switching program payments away from cash to direct deposits can integrate initially financially marginalized individuals into credit markets, but the effects are limited. The magnitude of the effects on loan ownership and on credit inquiries suggests that only one third of

Key Concept

DIGITAL MODES OF PAYMENT

The transfer of value from one account to another by digital means such as bank transfers, mobile money, QR codes, and payment instruments including credit, debit, and prepaid cards.

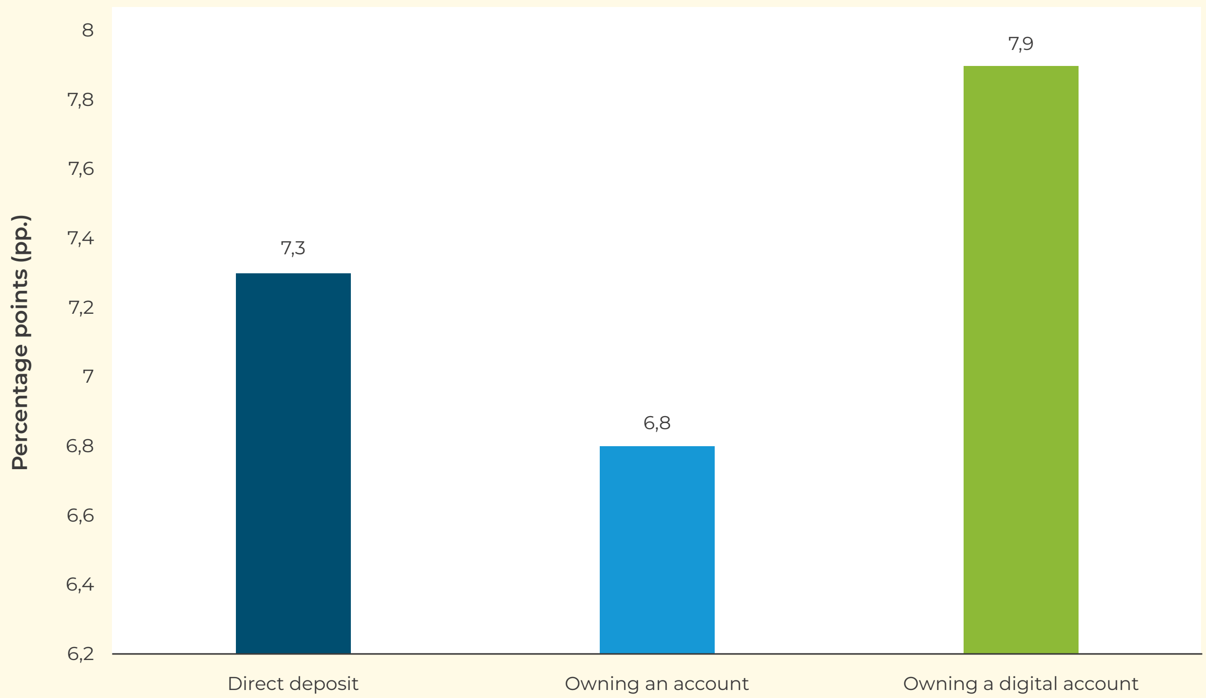
credit inquiries induced by the switch to direct deposit resulted in approved loans from commercial banks, and there was no spillover to other financial products. This suggests that simply changing the mode of payment of cash transfer programs or opening a savings account is unlikely to solve deeper problems of adverse selection of borrowers and moral hazard concerns for lenders.

Key Concept

FINANCIAL WELL-BEING

An individual's ability to manage their short-term and long-term finances and achieve present and future financial freedom. It includes savings, consumption patterns, and financial stress.

FIGURE 1. Impact of Encouragement Intervention on Direct Deposit, Account Ownership, and Digital Account Ownership



FULL STUDY

Hernández Romero, Karla, Diego A. Vera-Cossio, Bridget Hoffmann, and Camilo Pecha. 2024. "The Promises of Digital Bank Accounts for Low-Income Individuals." IDB Working Paper No. 1568. Inter-American Development Bank.

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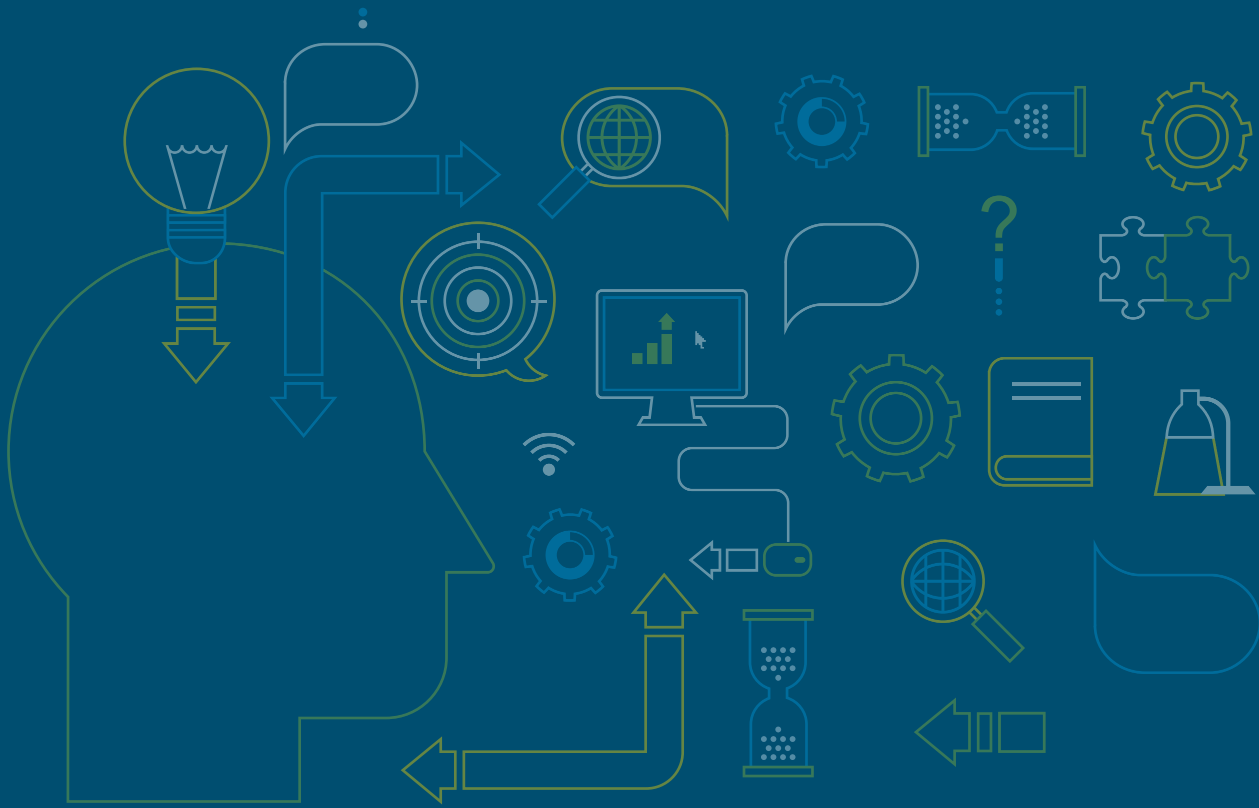

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