Does Digital Financial Inclusion Reduce Poverty in Developing Countries? The Role of Service Providers and DFI Dimensions

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Abstract:

Although Digital financial inclusion (DFI) has become the current finance revolution among developing countries (DCs), there is no sufficient theoretical and empirical support about its connection to overall policy objectives, among which is poverty reduction. This study tests whether this revolution is theoretically and empirically supported in DCs using fixed-effect and panel two-stage least squares on a sample of 96 DCs over the years of 2014, 2017 and 2021. This analysis leverages a new index of DFI constructed for 142 countries. The results show that DFI reduces poverty through two key channels: increase in GDP per-capita and increase in service-sector employment. Underscoring the importance of DFI providers, the results show that DFI's effect is higher when the DFI provider is non-bank and vice-versa. The results also show that the effect of DFI on poverty is non-linear, which by extension, is highest in sub-Saharan Africa, followed by South-Asia and the pacific, Latin-America and the Caribbean and finally Central-Asia, North-Africa and Middle-East. While each DFI dimension is important for poverty reduction, digitisation dimension reduces poverty more than other dimensions. These results are robust to alternative measures of poverty and DFI, alternative poverty line and control for financial inclusion and financial development.

Keywords:

Digital Finance, Financial service, Financial Markets