

Chapter 13


Revolutionizing Digital Financial Inclusion With Central Bank Digital Currencies

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ABSTRACT

The new era of digital finance is revolutionizing traditional banking systems and payment methods. Central bank digital currency (CBDC) has emerged as a technology offering potential solutions to longstanding challenges in financial inclusion. This chapter explores the evolving landscape of digital finance and the transformative role of CBDC in promoting financial inclusion. The chapter begins with an overview of the evolving digital finance ecosystem and highlights the significance of financial inclusion as a catalyst for economic growth. Subsequently, the authors explore the key features and design principles of inclusive CBDC. Further, they critically assess the challenges and risks associated with CBDC implementation, addressing regulatory, technological, and operational considerations. They then analyse the potential role of CBDC in addressing financial inclusion through case studies of successful CBDC implementations. Finally, they conclude by outlining the future trajectory of CBDC as a catalyst for inclusive economic growth.

INTRODUCTION

One of the pressing issue the world is trying to address is the problem of financial exclusion. It indicates the lack of access of essential financial services to individuals or business. This has an impeding impact on the economic growth and social development of excluded population. This highlights the need for tools which can enhance the access of formal financial services to the marginalised communities. Financial inclusion enables people to invest in education and other means which help them come out of poverty. Financial inclusion creates scope for savings and fosters financial stability and economic growth.

Rapid digitalization of financial activity has led to the emergence of digital finance. Financial activity in digital finance includes various transactions and activities conducted through digital platforms and technologies. Hence, digital technology helps develop new business models and is pivotal in transforming the financial system's value chain and new product delivery (Gazi, 2022). Digital finance has proved its potential to bring the financial services to the underserved population.

Digital financial inclusion can empower individuals to save, invest, and manage their finances more effectively even from remote locations thus saving time and effort. Thus, solving the supply side issues which lead to financial exclusion. Similarly, low-cost digital technology has enabled banks to provide financial services at a cheaper cost. Digital financial services with their user-friendly interface and user tailored services have enhanced the flexibility and useability of financial services. These benefits of digital financial solved the demand side challenges that lead to financial exclusion. Technological advancements in the financial sector have significantly improved financial inclusion through secure digital payment solutions facilitating online and offline transactions, especially in regions without banks. The recent financial technology that has gained the attention of users, governments and policy makers alike is the Central Bank Digital Currencies (CBDCs).

CBDCs stand out as blockchain-based digital tools that represent a centralized digital form of a nation's fiat currency. CBDCs aspire to emulate traditional cash by offering attributes such as privacy, transferability, convenience, and financial security. Central banks around the world have already started conducting pilots and trials to test the feasibility of implementing and adopting CBDCs. CBDCs has the potential to act as an affordable and user-friendly payment platform thus enabling people to experience financial services in a better way. It also has the capability to ensure safer payments and enhance financial stability Gazi (2022). Thus, CBDC is a transformative technology which can improve financial inclusion in an economy. It is a robust system with a value chain digitalization that can enhance access to financial services at a reduced cost (Ozili, 2022). Central banks of countries issue retail CBDCs as a substitute for fiat currency. These digital currencies can be held and used by both consumers and companies as a substitute for physical currency or coins. Central banks of many countries have already initiated integrating the same in their financial system.

Recently, countries started understanding the relevance of CBDCs in the changing financial landscape. The number of countries focusing on developing CBDCs is increasing steadily from 65 countries in 2017 to more than 100 countries by the end of 2022 (see. Fig.1). Out of 105 countries involved in CBDC development only Nigeria, the Bahamas, Jamaica and the Eastern Caribbean Currency Union (Anguilla, Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines) had a “live” CBDC. Developed Countries like the UK, USA, and the European Union have started exploring CBDCs by the end of 2022. According to the Bank for International Settlements (2024), the United Kingdom aims for a “digital pound” around 2026.

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