Harnessing Innovation for Inclusive Finance

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Douglas Pearce (@DougMPearce)
Financial Inclusion
Definition and Development Challenge

What is Financial Inclusion?

- Financial inclusion promotes increased access to and usage of a broad set of safe, affordable, and efficient financial services for individuals and micro, small, and medium enterprises (MSMEs).
- Physical access to or ownership of basic payment services – termed ‘financial access’ – is a necessary but not sufficient condition for financial inclusion. Thus the financial inclusion agenda supports but extends beyond the 2020 Universal Financial Access goal.

Why is Financial Inclusion Important for Development?

- The use of a range of quality and affordable financial services allows individuals and MSMEs to safely and efficiently save, make payments, borrow, and manage risk.
- Without inclusive financial systems, individuals are limited in their ability to absorb economic shocks, smooth consumption, and invest in education or entrepreneurial activities, and newly founded enterprises must likewise depend on their constrained earnings to take advantage of promising growth opportunities.
- Financial inclusion can have beneficial impacts on managing income shocks, food security, efficient targeting of social transfers, and access to services.
- Financial inclusion is a critical enabler of poverty reduction and shared prosperity.
Financial Inclusion creates Opportunities

**Micro**

**Individual-level**
- Smooth consumption
- Manage income shocks/mitigate risks
- Investments in: education, health, services
- More convenient, higher personal savings
- Lower transaction costs
- Safe & secure payments

**Firm-level**
- Manage income shocks and/or mitigate risks
- Investments in business and assets
- Lower transaction costs
- Safe & secure payments

**Economy-level**
- Better allocation of resources
- Broader economic participation
- Job creation / more entrepreneurship and innovation
- Higher national savings
- Higher competitiveness

**Greater physical, social, and economic well-being**
**Profitability Competitiveness Firm Growth**
**Higher growth Poverty reduction Reduced inequalities (income, gender)**
Significant global progress, but huge challenges remain

700 million new account holders

1.7 more bank branches and 9.3 ATMs per 100K adults

ATMs and Commercial Bank Branches Globally

- 2012: 16.4 Branches/100K adults, 44.7 ATMs/100K adults
- 2013: 16.9 Branches/100K adults, 49.3 ATMs/100K adults
- 2014: 18.1 Branches/100K adults, 54.0 ATMs/100K adults
Barriers to Financial Inclusion - Supply and Demand side

**Demand-side (Reasons for not Owning and Account)**

- Affordability
- Lack of Need/ Family member already has an account
- Physical access/distance to nearest branch
- Lack of transparency & unpredictability of banks fees
- Eligibility requirements
- Lack of necessary documentation
- Lack of trust in financial institutions
- Religious reasons

**Supply-side (Reasons for limited supply of Appropriate products)**

- Deficient payments, credit or ICT infrastructure
- Lack of reliable information on consumers
- Underdeveloped or inappropriate legal and regulatory frameworks
- Incomplete secured transaction frameworks
- Market distortions (for example due to subsidized lending programs)
- Customer due diligence requirements which are not tailored to risk levels and unnecessarily exclude low income or dispersed population

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**Self-reported barriers to use of an account at a financial institution**

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<thead>
<tr>
<th>Reason</th>
<th>Cited as only reason</th>
<th>Cited with other reasons</th>
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<tbody>
<tr>
<td>Religious reasons</td>
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<tr>
<td>Lack of trust</td>
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<tr>
<td>Cannot get an account</td>
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<tr>
<td>Lack of necessary documentation</td>
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<td>Financial institutions too far away</td>
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<tr>
<td>Accounts too expensive</td>
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<tr>
<td>Family member already has an account</td>
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<tr>
<td>Do not need an account</td>
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<tr>
<td>Not enough money</td>
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Note: Respondents could choose more than one reason. Source: Global Findex database.
WBG Approach to Financial Inclusion

Universal Financial Access (UFA) 2020
Universal Financial Access 2020: Goal and WBG Target

**Goal:** By 2020, adults globally have access to a transaction account or electronic instrument to store money, send and receive payments as the basic building block to manage their financial lives.

**As of 2015:** still 2 billion adults to reach.

**WBG Target:** to contribute to 1 billion new accountholders by 2020

- **October 2013:** Dr Kim set forth a goal of Universal Financial Access (UFA) by 2020.
- **Goal can only be reached if technology transforms business models (costs, risks, incentives), and national authorities quickly put in place enabling framework**.
- **April 2015:** he announced that the WBG will contribute to 1bn new accountholders by 2020 (600m: IFC / 400m: WB).
- **WBG has mobilized to scale up its investment, financial, advisory, knowledge, and convening support; and to leverage partnerships.**
Payment Aspects of Financial Inclusion (PAFI) Framework

- Access to a transaction account is a stepping stone to full financial inclusion.
- Payment Aspects of Financial Inclusion (PAFI) is a key building block for UFA

**PAFI REPORT** (by CPMI and the WBG, released April 2016): examines demand and supply-side factors affecting financial inclusion in the context of payment systems and services, and suggests measures to address these issues.
Gateway to Financial Inclusion

- Broader Inclusion
- Customer-centered product innovation
- Financial capability
- Strong consumer protection
- Better financial infrastructure
- More and interoperable access points

Cash Economy
- Has no basic bank account
- Has no (or restricted) access to financial services

Transaction account

Banks
- Microfinance Institutions
- Mobile Network Operators

Card Companies
- Postal Networks
- Financial Cooperatives

Providers → Services

Put service

served

unserved
FinTech and Financial Inclusion
FinTech enabling Financial Inclusion

Digital technologies have spread rapidly in much of the world, yet, there is potential to boost digital dividends.

Global investments in Fintech ventures grew by 75% reaching $22.3bn in 2015 ($12.7bn in 2014)

Source: Accenture

M-Pesa reached 80% of households in Kenya within 4 years

Source: WDR 2016
Digital Innovation across different areas of the financial sector

**Payment services and market infrastructures**
- E-money and mobile money products
- Application program interfaces allowing overlay of services on existing products
- Use of distributed ledger technologies for new ways of structuring market infrastructures

**Leveraging transaction data and other sources of data for credit appraisals**
- Transaction data from e-commerce and payment platforms like Alibaba and Paypal
- Mobile phone usage data
- Social Network related data

**Deposits, Lending and Capital Raising**
- Crowd-sourcing ideas and funding them through crowd-funding
- Peer 2 peer lending
- Internet-only banks

**Investment Management**
- Automated processing and dissemination of investment advice

Potential to significantly enhance efficiencies, reduce costs and expand access to financial services
Digital technologies – Opportunities

Offer a powerful solution for expanding access and usage to financial services, and improve their quality, appropriateness and impact.

New Players leverage electronic data in innovative ways to create better, more customized, and more accessible digital financial inclusion.

The spread of mobile technologies, mobile network coverage, and mobile based financial services in developing countries represent a game-changer in global financial inclusion efforts.

Governments play a critical role in creating the enabling conditions for financial service providers while ensuring that risks are mitigated and consumers are properly protected.

Technological developments and increased interest from new players is leading to a fundamental re-imagining of the processes and business model of the financial services industry.
FinTech enabling Financial Inclusion
• New trends emerging that enable full financial inclusion:

1. Disintermediation and Disaggregation of the Value Chain
   • Entry of new class of institutions disintermediating role of banks - more tailored and efficient products
   • The value chain of financial services is being disaggregated through partnerships and outsourcing, in which each player focuses on a smaller, more specific set of functions.

2. Application Program Interfaces and the Opening of Platforms
   • Enabling new market players to overlay features or functionalities to existing digital programs or platforms.

3. Use of Alternative Information
   • Developing digital alternatives to traditional means of authentication for account opening, data used for assessing credit worthiness, etc.

4. Customization
   • Using digital technologies in order to more efficiently design targeted, appropriate and quality products for underserved markets.
Blockchain and Distributed Ledger Technology- Key Mechanisms and Potential Applications for Advancing Financial Inclusion

**Mechanisms**

1. Providing proof of collateral for credit risk assessment and credit scoring purposes

2. Lowering costs, improving speed and efficiency of low-value cross-border payments

3. Increasing access to robust, verifiable, identity, to help meet customer due diligence requirements of financial institutions

**Applications**

- Cross-border Payments and Remittances
- Digital Identity Systems
- Property Registers and other Asset Registers
- Government Transfers
FinTech also presents a number of challenges...

- Data privacy, Consumer protection
- Are investors in peer-to-peer lending fully aware of the risks?
- Digital Currencies have been used to pay for criminal activities
- Limited supervisory capacity to understand and monitor new applications
- New actors, products, and delivery mechanisms, inc. through non-financial institutions
- What are the implications of these on profitability of banks?

There is limited data available and a lack of international best practices and frameworks.
G20 New High Level Principles on Digital Financial Inclusion (HLPs)

The new 2016 Principles are intended to catalyze country-level actions by G20 governments to drive financial inclusion using digital technologies.

- **PRINCIPLE 1:** PROMOTE A DIGITAL APPROACH TO FINANCIAL INCLUSION
- **PRINCIPLE 2:** BALANCE INNOVATION AND RISK TO ACHIEVE DIGITAL FINANCIAL INCLUSION
- **PRINCIPLE 3:** PROVIDE AN ENABLING AND PROPORTIONATE LEGAL AND REGULATORY FRAMEWORK FOR DIGITAL FINANCIAL INCLUSION
- **PRINCIPLE 4:** EXPAND THE DIGITAL FINANCIAL SERVICES INFRASTRUCTURE ECOSYSTEM
- **PRINCIPLE 5:** ESTABLISH RESPONSIBLE DIGITAL FINANCIAL PRACTICES TO PROTECT CONSUMERS
- **PRINCIPLE 6:** STRENGTHEN DIGITAL AND FINANCIAL LITERACY AND AWARENESS
- **PRINCIPLE 7:** FACILITATE CUSTOMER IDENTIFICATION FOR DIGITAL FINANCIAL SERVICES
- **PRINCIPLE 8:** TRACK DIGITAL FINANCIAL INCLUSION PROGRESS
World Bank Group Engagement on FinTech includes:

The World Bank participates actively in SSB work streams relevant to Fintech:

- FSB FIN group [Financial Innovation]
- CPMI [Retail Payments working group and Co-manager of a Retail Payments Forum, which interfaces with the private sector]
- CPMI-IOSCO [Digital Innovations Working Group]
- FATF [Guidance on AML/CFT considerations for Digital Currencies]

**New:** G20 High Level Principles for Digital Financial Inclusion (WB as co-chair)

The WBG works with national authorities to put in place enabling frameworks for adoption of technology, market entry/level playing fields, and expansion of financial access – as technical, policy, or financing partner

IFC: investments, risk-sharing, also dialogue with private sector players in this space e.g. through SME Finance Forum
Thank you