

Global Partnership for Financial Inclusion

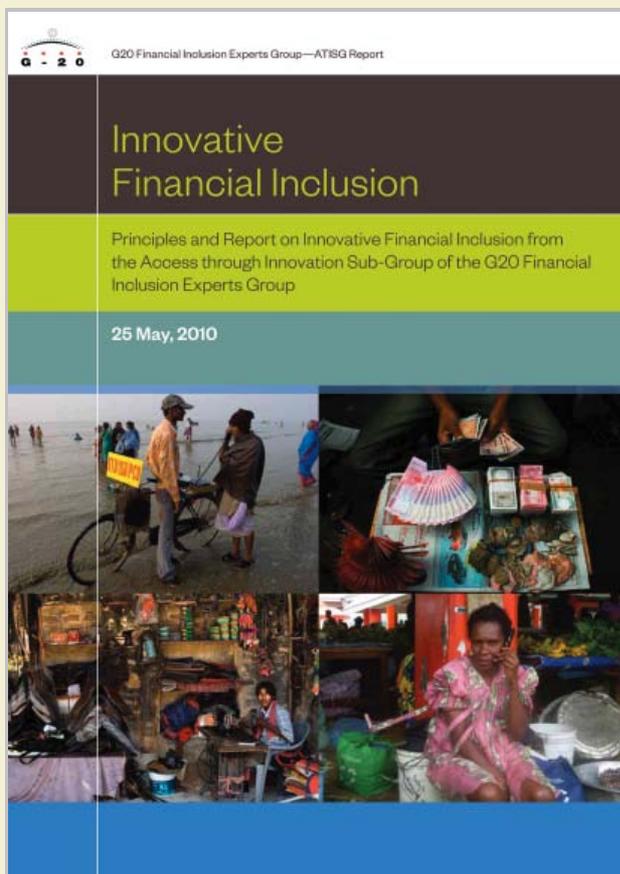
G20 Principles for Innovative Financial Inclusion

Despite advances in financial inclusion across the globe, more than 2.5 billion people worldwide remain excluded from access to financial services. This restricts their ability to save, to borrow and to protect themselves and their families against hunger, crime and natural disaster. To counteract this, and increase access to and usage of financial services for the poor, many innovative approaches have been adopted – particularly in developing countries. These range from agent banking to delivering financial services through the mobile phone networks. New institutions have been established, new products devised and new technologies harnessed to reach un- or underserved markets. Behind the scenes, changes in legislation and regulation have helped provide the right conditions for innovation to thrive while protecting consumers and the financial system.

The experiences of those countries that have adopted such models are now available to inform future strategies to increase financial inclusion. The G20 Principles for Innovative Financial Inclusion bring those experiences together to produce a set of practical recommendations for policymakers worldwide. They are not rigid requirements, but rather nine valuable insights that together form a set of conditions that spur innovation for financial inclusion while safeguarding financial stability and protecting consumers. The document also includes examples of countries that have followed these principles successfully.

The Principles

1. Leadership
2. Diversity
3. Innovation
4. Protection
5. Empowerment
6. Cooperation
7. Knowledge
8. Proportionality
9. Framework



About the Principles and the Global Partnership for Financial Inclusion (GPFII)

The Principles were developed in 2010 by the Access Through Innovation Sub-Group (ATISG) of the G20 Financial Inclusion Experts Group (FIEG). The Principles were originally published in the Sub-Group's official report to the G20 and endorsed at the Toronto Summit in May 2010, and underpin the Financial Inclusion Action Plan endorsed at the Korea Summit in November 2010.

The year-long FIEG process resulted in the establishment of the Global Partnership for Financial Inclusion (GPFII) by G20 leaders at the Seoul Summit in November 2010 to take forward its various commitments on financial inclusion with broad stakeholder participation.

AFI participates as an implementing partner in several GPFII workstreams. This includes supporting the subgroup that promotes awareness and use of the G20 Principles together with CGAP.

Tasked with raising awareness and collecting further examples of the Principles in action, AFI has reprinted the G20 Principles in this executive brief, along with some examples of how developing country policymakers are bringing these Principles to life. Helping to make the Principles more widely available to its network is one step towards AFI's aim to compile a comprehensive report on the application of the Principles through a number of country case studies.

Access the full ATISG report, including the Principles as originally published, at www.usaid.gov/au/publications/

The Principles

Principle 1: Leadership

Cultivate a broad-based government commitment to financial inclusion to help alleviate poverty.

Experience from around the world has underlined that government leadership and commitment at the highest level is an essential condition for increasing financial inclusion. More importantly still, that leadership is vital to ensuring that increased financial inclusion successfully translates into progress in alleviating poverty.

The best results have been seen when financial inclusion is viewed as an integral component of overall financial sector growth and development strategies. In practice, this has meant that governments that have successfully increased financial inclusion have shown leadership in some or all of the following ways:

- addressing policy and regulatory issues related to innovation, consumer protection and payments, facilitating new approaches and ensuring that excessive regulation does not stifle growth
- adopting a collaborative approach to financial inclusion that engages all players, including the private sector and auditing authorities
- supporting inclusion programs with financial education and/or by developing payment systems and infrastructures, and
- collecting data to support proportionate and evidence-based policy, which in turn maintains the safety and soundness of the system.

Mexico's inclusive approach to leadership

Led by the Secretariat of Finance and Public Credit, the Mexican government established a National Development Plan for 2007-2012 that addressed financial inclusion, consumer protection, and financial literacy.

To formulate the Plan, the Secretariat worked in close collaboration with the Central Bank of Mexico, national savings banks, the National Banking and Securities Commission, and other key stakeholders. This not only ensured their commitment from the start, but also means they have maintained a direct interest and involvement throughout the Plan's duration and ensured that financial inclusion has remained on the overall policy agenda.

One of the first and most important activities under the Plan was reforming the banking law to enable the use of non-financial entities, such as banking agents, to provide financial services in rural areas. The law also allowed the creation of specialized niche banks which could offer different services and were subject to different regulations. Under the Plan, small savings and credit institutions were offered assistance to help them develop into regulated deposit-taking entities, and a new national savings and financial services system was created to provide back office support to these providers.

Principle 2: Diversity

Implement policy approaches that promote competition and provide market-based incentives for delivery of sustainable financial access and usage of a broad range of affordable services (savings, credit, payments and transfers, insurance) as well as a diversity of service providers.

It's widely recognized that competition in a market produces greater value, choice and opportunities for customers, and the financial services market is no exception. However, when it comes to reaching the unbanked, diversity of products, providers and delivery methods is more important than ever. Services need to be offered outside of the traditional channels to reach a wider customer base.

For governments, this means there is a crucial role to play in facilitating the development of market structures that promote entry. One key aspect is the design of appropriate market-based incentives for all parties – from traditional banks to prospective 'agents' to telecoms companies, microfinance institutions and customers themselves – that encourage the development of a broad range of sustainable, secured, and affordable financial services, such as savings, credit, payments, and transfers. At the same time, these incentives should aim to attract a wide range of providers, as this can help improve both access and usage.

Encouraging diversity in India's insurance market

To build a broader and more diverse domestic insurance market, India's Insurance and Regulatory Development Authority relaxed agent banking regulations, promoted linkages between insurers and non-governmental organizations, and allowed composite insurance services to be offered through micro-insurers. It also allowed self-help groups (SHG) to partner with insurers to assist with the claims settlement process, including collecting proposal forms, collecting and remitting premiums, and providing insurance policy administration services. The result was that many more people and small groups were able to afford and access insurance and so increase their financial security.

Principle 3: Innovation Promote technological and institutional innovation as a means to expand financial system access and usage, including addressing infrastructure weaknesses.

Many of the most effective methods of increasing financial inclusion have been based on the application of new technologies, such as mobile phones, or the introduction of new institutional arrangements, such as banking agents. These allow rapid expansion of services to reach excluded populations, while at the same time reducing the costs of service delivery. For example, the massive global growth in mobile phone use means that financial services offered through the mobile phone networks can be delivered cost-effectively to a wide population.

Experience has shown that in some cases the existing financial services infrastructure can be a barrier to innovation. For example, the interbank payments system might make it difficult for new providers to enter the market. Policymakers need to address such barriers as part of a holistic financial inclusion strategy.

Overcoming regulatory hurdles to mobile banking in the Philippines

Financial inclusion in the Philippines has received a significant boost through the introduction of two mobile phone financial services: the bank-based Smart Money and the non-bank based G-Cash.

The two services received initial authorization to launch from the Central Bank (Bangko Sentral ng Pilipinas, BSP) even though there was little regulation in place. Instead, the Central Bank chose to allow a carefully controlled pilot phase to test different business models, and used their learnings from this phase to develop relevant and effective e-money regulations. The regulations now address the risks arising from new mobile channels and allow a variety of models to flourish, while maintaining the safety and soundness of the system. The Central Bank maintains an open dialogue with industry and civil society players to foster an environment conducive to innovation.

Principle 4: Protection Encourage a comprehensive approach to consumer protection that recognizes the roles of government, providers, and consumers.

The mix of innovation, new service providers, and inexperienced consumers brings new risks of consumer fraud and abuse, as well as the possibility of technical or human error around financial services. An equitable and transparent consumer protection infrastructure is therefore vital part of a broad financial inclusion framework.

To establish protections and promote trust in new and innovative services, government, regulators, and supervisors need to take responsibility for:

- establishing regulations that promote transparency in pricing and services
- creating a dispute resolution mechanism for consumers
- identifying an appropriate authority to enforce this protection

Safeguarding customers of agent banks in Colombia

Agent-led services have played an important role in extending financial inclusion in Colombia. As an incentive to promote the highest standards of consumer protection, the Colombian government designed regulations that made the service provider fully liable for their agents. Adopting a similar approach to Mexico, the government has also required providers to:

- establish out-of-court redress mechanisms
- ensure that agents maintain data privacy standards on par with banks
- train agents in Anti-Money Laundering (AML) best practices
- post their customer service contact channels and disclose all applicable fees and charges at the agent's facilities, and
- ensure that safety and privacy features of data storage and transmission are robust enough to protect customer funds and information.

Principle 5: Empowerment Develop financial literacy and financial capability.

For consumers to make the most of new financial services, it is important that they have:

- financial literacy – the ability to understand basic information about financial products and services
- financial capability – the ability to apply that understanding to make informed choices about their finances
- redress mechanisms – the ability to resolve disputes through a safe and recognized mechanism

These are an essential complement to consumer protection regulation: without financial literacy and capability, the regulation itself cannot adequately protect consumers and moreover can increase operational costs.

Experience has shown that low levels of financial literacy and capability in developing countries form a significant barrier to accessing and properly using financial services. By contrast, increased financial literacy and capability lead to increased demand for relevant services.

The Principles

For governments, this means that building financial capability is an integral part of increasing inclusion. Best practice indicates that effective financial capability initiatives focus on providing practical, easy-to-understand and impartial advice so that consumers can make informed choices.

Ghana's national strategy for financial literacy

A Ghanaian government survey in 2007 revealed a low level of knowledge among adults of financial institutions, services, and products. Even in instances where adults were knowledgeable about products and services, they were not necessarily taking advantage of them. As a result, the government launched a financial literacy program in 2008 to create awareness and build trust between consumers and service providers. In 2009, a national strategy for financial literacy and consumer protection in the microfinance sector was adopted that addressed the three pillars of financial capability: knowing, understanding, and behavior change. The strategy featured the development of educational materials on key product types, and a road-show that visited rural areas.

Principle 6: Cooperation

Create an institutional environment with clear lines of accountability and coordination within government; and also encourage partnerships and direct consultation across government, business, and other stakeholders.

The nature of innovative financial services and new delivery channels is that they span multiple public institutions and regulatory agencies — as well as a range of different private sector organizations. While there is an understandable desire to provide adequate policy across the value chain, this needs to be coordinated across the different institutions involved to avoid conflicting or inconsistent approaches. To achieve this coordination and increase global partnership, countries that have successfully increased financial inclusion have identified a lead agency to coordinate among government agencies and manage the consultative process with stakeholders.

One essential consideration in developing coordinated policy is to understand the incentives of each player in the value chain, and how these could be affected by regulation.

Cooperation improves technical and financial oversight in Pakistan

In Pakistan, the overall responsibility for increasing financial inclusion sits with the State Bank. In 2007, it launched a strategy for this, of which branchless banking was an important component. To oversee implementation of that strategy and in particular to develop effective regulation for branchless banking, the State Bank set up a committee of interested parties, led by the Governor of the State Bank. The committee included not only representatives from relevant units within the bank but also members of the Ministry of Information Technology, which is the primary regulator of mobile networks in Pakistan. This meant that any proposed policy could be scrutinized not only from the core financial perspective, but also a technical one — and one which understood the interests of the mobile operators.

Principle 7: Knowledge

Utilize improved data to make evidence-based policy, measure progress, and consider an incremental "test and learn" approach by both regulators and service providers.

As with any area of policymaking, appropriate and reliable data are needed to support the design of financial inclusion policy and to monitor and measure the impact of policy over time. Currently, few countries have sufficient data on financial inclusion. This is changing fast, and many governments are seeking to improve the data available.

A lack of data however, need not necessarily delay the introduction of new services and business models. A number of countries have overcome this by adopting a "test and learn" approach that has enabled them to examine new services and untried business models under carefully controlled conditions. As a result, they are better able to strike an appropriate policy-regulatory balance between safety and soundness on one hand, and growth and development on the other. In order to increase the role of monitoring and assessment in this 'test and learn' approach, data and knowledge management play crucial role.

Audit trails enable Kenya to refine its regulation

Kenya has become renowned as a world leader in the adoption of mobile phone financial services, with huge numbers of users and a competitive marketplace. But it began with little regulation in place, and very little data to work with to support evidence-based policy making.

When the first network operator requested permission from the Central Bank of Kenya to launch mobile money services, the Bank replied in a private letter that set out essential conditions for the operator to follow. In particular, the operator was required to provide the bank with a comprehensive audit trail of all transactions and abide by the terms of the draft Anti-Money Laundering Bill and National Payment System Bill, which were shortly to be enacted.

In this way, the Central Bank not only mitigated the main risks around launching mobile financial services but also ensured there would be a stream of data that they could monitor, assess and use to refine policies. Today, Kenya is drafting e-money regulations that reflect a better understanding of the market, risks and opportunities that mobile money provides.

Principle 8: Proportionality

Build a policy and regulatory framework that is proportionate with the risks involved in such innovative products and services, and is based on an understanding of the gaps and barriers in existing regulation.

Any innovation involves risks. The challenge is to create a regulatory framework that is strong enough to protect the financial system and institutions against those risks, yet not so severe that the costs of regulatory compliance deter service-providers from entering the market.

To strike the right balance, existing regulations should be carefully analyzed to establish whether their demands on service-providers and customers are proportionate to the risks. This diagnostic exercise will also pinpoint regulatory gaps that need to be filled to enable innovations to flourish and to develop effective tools to mitigate these risks. Greater knowledge (principle 6) and greater cooperation (principle 7) are also, of course, important for a proportionate framework.

Diagnosing barriers to inclusion in Argentina

A diagnostic exercise conducted by the government of Argentina revealed that existing regulation did not permit the use of agents. This meant that the cost of providing financial services to the poorest was often prohibitive for commercial banks. The regulations were revised and branchless banking via agents is now at the heart of the country's financial inclusion strategy.

Principle 9: Framework

Consider the following in the regulatory framework, reflecting international standards, national circumstances and support for a competitive landscape: an appropriate, flexible, riskbased AML/CFT regime; conditions for the use of agents as a customer interface; a clear regulatory regime for electronically stored value; and marketbased incentives to achieve the longterm goal of broad interoperability and interconnection.

Principle 9 draws together many of the preceding principles to summarize the key constituents of an effective regulatory framework for innovative financial inclusion. One of the key issues is how to address risk without stifling innovative services. The international financial standards provide the basic framework. However, they are very broad and designed to be flexible in their application. Thus, it is not always clear how to apply the standards to innovative financial inclusion services. The international financial standard setters are working to provide greater clarity and fill any gaps.

Experience shows that in fact increasing inclusion often improves compliance with international standards: AML/CFT recommendations in particular have been better served by a more inclusive financial sector which provides increased ability to trace and monitor transactions.

How a risk-based approach to AML regulation helped South Africa

South Africa's Financial Intelligence Centre Act requires that service providers (accountable institutions) confirm the identity of their clients before allowing them to open an account, and record and verify the documents they use to do so, as a means of complying with international AML/CFT standards. However, this proved to be a barrier to financial inclusion: many of the poorest prospective clients do not possess formal identification or proof of residence.

The government decided to introduce an exemption to the Act which would allow service providers to open accounts without requiring such verification. Instead, strict limits on transactions were introduced, based on risk analysis, that reduced banks' potential exposure and the prospect of money laundering.

This led to the introduction of a basic bank account, the Mzansi Account, which brought millions of people into the formal financial system. Further reforms to the Act have now also allowed banks to open mobile phone-accessible bank accounts on a non face-to-face basis, but with lower transaction limits than accounts opened face-to-face in a bank.

The principles in action: Brazil

In 1997, as many as 40 million Brazilians – about two-thirds of the total population – did not have access to financial services. Over the last decade, that figure has been reduced significantly. Between 2000 and 2008, the number of bank accounts in Brazil doubled from 63.7 million to 125.7 million. At the heart of this has been a dramatic expansion of the country's "correspondent" model, backed by a supportive government that has prioritized financial inclusion following many of the principles in this document.

Correspondents are Brazil's equivalent of banking agents, and they have operated in the country since the 1970s. However, a little over a decade ago, the government changed regulations governing correspondents, allowing them to diversify (principle 2) and provide a wider range of services. This was at a time when conventional banking services in Brazil had very low penetration.

Over the last decade, the correspondent model has grown rapidly, with Brazil's 150,000 correspondents now accounting for about 62% of the total number of service points in the financial system – making it the world's largest network of this kind.

As well as diversification, the Brazilian approach is also characterized by innovation (principle 3) particularly in the way that correspondents and service providers have overcome the physical barriers to having bank branches in certain locations (eg in the Amazon region). Now, retail stores, post offices, and lottery outlets all act as correspondents for institutions, using point-of-sale devices and mobile phones to transact. Banco Central do Brasil (BCB) created an enabling environment for such institutional arrangements, providing regulatory clarity on what agents/correspondents are permitted to do and setting reporting requirements for accountable institutions.

Brazil took a cooperative approach (principle 6), setting up an interdisciplinary Micro-insurance Commission comprised of relevant government entities, the insurance industry, and other private sector players, including industry networks and academic institutions that promote micro-insurance.

Having supervised correspondent banking for over a decade, the Central Bank has concluded that most agency-related risks are minimal particularly since the main service provider is fully liable for the actions of their agents. The regulatory approach is proportionate to this risk (principle 8) with its focus on requiring regulated banking institutions to manage their own risks via transaction limits or submitting agency agreements.

Timeline of the development of G20 Principles for Innovative Financial Inclusion

Pittsburgh G20 Summit

September 2009 G20 leaders recognized the mutually reinforcing policy objectives of financial stability, financial inclusion, and consumer protection. Leaders committed to improving access to financial services for the poor by supporting the safe and sound expansion of new modes of financial service and formed the Financial Inclusion Experts Group (FIEG) to achieve this aim.

Toronto G20 Summit

June 2010 The FIEG subgroup on Access Through Innovation explored policy and regulatory approaches that aimed to encourage the safe adoption of innovative, low-cost financial service delivery models; help provide a framework of incentives and competition for the various bank, insurance, and non-bank actors involved; and foster affordable financial services that respond to customer needs. Their outputs culminated in the Principles for Innovative Financial Inclusion, which the G20 leaders endorsed in their Toronto communiqué.

Seoul G20 Summit

November 2010 G20 leaders announced the Global Partnership for Financial Inclusion (GPFI) to move the financial inclusion agenda forward. AFI was appointed as an implementing partner within the GPFI, and was tasked specifically to engage non-G20 developing country policymakers and to bring their experiences and voice to the table. The GPFI has several work streams, including a subgroup dedicated to the Principles that is tasked with promoting and creating awareness about the nine Principles.

Towards the Cannes G20 Summit

November 2011 As an implementing partner of the GPFI, AFI will promote the use of the Principles and work with member institutions to document successful cases where the Principles have been applied. Lessons learned and useful examples will be captured and shared with the GPFI community, to unlock the knowledge and expertise of developing countries, where the challenge of financial inclusion is the greatest.

For more information about the Principles and the wider mandate of the GPFI visit: www.gpfi.org

About the GPFI

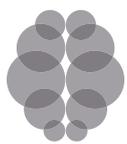
The Global Partnership for Financial Inclusion (GPFI) was established by the G20, and it is the main implementing platform for the G20 Financial Inclusion Action Plan. The group engages partners from G20 and non-G20 countries, private sector, civil society, and various regional, national and international bodies for systematic coordination and implementation of the Action Plan, and to raise awareness of financial inclusion. The GPFI relies on three implementing partners: AFI, CGAP and IFC, and builds on the strength and the process of the G20 Financial Inclusion Experts Group (FIEG) (2009-2010). At the launch of the GPFI in Korea in 2010, three sub-groups were formed to implement concrete actions:

- Sub-group on the G20 Principles and Standard Setting Bodies (SSBs)
- Sub-group on SME finance
- Sub-group on financial inclusion data and target setting

The three work streams are interrelated. The Principles are relevant to all three and help underpin the synergies.

About AFI

The Alliance for Financial Inclusion (AFI) is a global network of central banks and other financial inclusion policymaking bodies in developing countries. AFI provides its members with the tools and resources to share, develop and implement their knowledge of financial inclusion policies. AFI connects policymakers through online and face-to-face channels, supported by grants and links to strategic partners, so that policymakers can share their insights and implement the most appropriate financial inclusion policies for their countries' individual circumstances. Learn more: www.afi-global.org



afi Alliance for
Financial Inclusion

Bringing smart policies to life

AFI is an implementing partner of the Global Partnership for Financial Inclusion

AFI, 399 Interchange Building, 24th floor, Sukhumvit Road, Klongtoey - Nua, Wattana, Bangkok 10110, Thailand
t +66 (0)2 401 9370 f +66 (0)2 402 1122 e info@afi-global.org www.afi-global.org

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