# Manuel Sánchez: The shared task of financial inclusion

Remarks by Mr Manuel Sánchez, Deputy Governor of the Bank of Mexico, at the Sixth Financial Education Summit, organised by Banamex, Mexico City, 19 November 2013.

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It is an honor to participate in this meeting on financial education and economic citizenship. I am pleased that Banamex has organized, once again, a forum for discussion and analysis that contributes to understanding the challenges posed by financial inclusion in our country, and to pondering viable options for promoting it.

Theory and international evidence show that financial intermediation and inclusion favor economic development and enhance living standards. Among other benefits, access to banking services allows individuals and firms to make better savings decisions, carry out economic transactions efficiently, and finance consumption and investment.

Despite these advantages, Mexico is under-banked relative to advanced countries, and also even relative to nations of similar or less development. The percentage of people with a bank account, the proportion of individuals and firms with credit, and the availability of distribution channels such as bank branches, automatic teller machines, and point-of-sale terminals for every 100,000 inhabitants reveal that Mexico is significantly behind, although the data also suggest a huge opportunity for improvement.[1]

As is well known, many savers and seekers of credit meet their needs with ingenious methods running from investments in and trading of animals to rotating savings and credit associations (*tandas*). Indeed, those with null or limited access to financial services have come up with other ways of saving, demanding loans, making financial decisions, and carrying out fairly complex operations in their own ways. In fact, the proportion of the population that uses informal financial services surpasses that using the formal system.[2]

Frequently, these schemes are effective. For example, contrary to commonly held prejudices, informal credit markets for people with low incomes tend to have a strong payment culture, partly because transactions occur in communities with strong binding ties. However, it is also true that informal vehicles hardly guarantee optimum scales and protect users from possible fraud, given that they lack adequate rules and supervision.

Low financial inclusion can obstruct or make more expensive the access to information and services indispensable to increasing people's opportunities and improving social wellbeing. To the extent that this limitation may affect broad segments of the population, generally those with the lowest incomes, it can diminish the productive potential of social groups and entire regions, making marginalization more acute.

## Obstacles to and progress on financial inclusion in Mexico

There are several factors that may explain the low level of financial inclusion in Mexico. The greatest problem for financial intermediaries appears to reside in the high costs of servicing low-income communities, especially those in isolated locations.

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[1] See BIS (2012), *Statistics on payment, clearing and settlement systems in the CPSS countries*, January; the World Bank, *Enterprise Survey*; and central banks.

[2] According to recent data, 36 percent of Mexican adults save in the formal system, while 44 percent save in the informal system. At the same time, 28 percent have formal credit, while 34 percent seek loans in the informal sector. See INEGI (2012), *Encuesta Nacional de Inclusión Financiera. Análisis de los resultados*, INEGI, pp. 20–27.

In fact, geographic distances, low population density, and the small size of the market make it more burdensome for banks to open branches and other service channels. Additionally, low balances and high-volume transactions make accounts expensive to administer. Where loans are concerned, limited information on individuals and firms as well as poor guarantees and recovery mechanisms can make lending unprofitable. On the other hand, product designs inadequate to the needs of users also limit financial inclusion.

From the perspective of potential customers, practical reasons and cultural barriers exist, as manifested by distrust in banks. Many people cite as reasons for not using financial institutions the facts that fees are high and interest rates on savings low, excessive requirements are demanded, and branches are far away. Definitely, the benefits of formal financial intermediation have not been well communicated, nor has a more effective response been offered by financial intermediaries to certain potential customer needs.[3]

Nevertheless, in recent years, Mexico has continued to increase the availability of financial services for ever greater numbers of families and businesses. For example, intermediaries have expanded their physical infrastructure to provide services, and to widen and diversify product offerings. Similarly, the use of electronic transactions has increased significantly, substituting less efficient means of payment such as checks.

One piece of remarkable progress has been the growth of commission agents, through which businesses can provide financial services on behalf of banks, allowing them to take advantage of already built infrastructure, lower their costs, and promote inclusion in faraway populations. To highlight the contribution of this phenomenon, it is enough to say that currently, in more than 10 percent of the nation's municipalities, a commission agent is the only way formal banking services are provided.[4]

In addition, mobile phones have begun to be used as a financial services medium. Even if they have not yet become a wide distribution channel, partly due to platform development and interconnection problems, their potential is enormous. With mobile phones, the use of which is widespread across all income brackets, individuals today can carry out various basic operations such as consulting savings balances and making payments to third parties.

## Shared challenges on financial inclusion

Despite this progress, a lot remains to be done to incorporate those not served by the banks. Given the fact that apparently many challenges to financial inclusion come from high costs and low profitability, the use of new technologies and the facilities brought by telecommunications will without a doubt continue to play a key role in augmenting the possibilities of banking penetration in Mexico.

Beyond the factors that drive success is the need for all players to be actively involved in the endeavor of financial inclusion. The authorities should continue to promote the interconnection of services, competition in the banking industry, and transaction safety. In an important way, they should also strengthen the prudential and supervisory frameworks so that previously informal activities become incorporated in a way that safeguards the population's wealth with due caution.

The financial intermediaries, in turn, should keep participating actively in the development of these markets, creating new ways of servicing an ever wider and more heterogeneous public.

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[3] See the key reasons for which an individual decides not to open a bank account in *Ibid*, p. 22.

[4] The CNBV reports the data on coverage by commission agents at the municipal level http://portafoliodeinformacion.cnbv.gob.mx/bm1/Paginas/infoper.aspx

In the final analysis, keeping up with the pace of society will continue to be essential to broadening the formal financial system. Throughout the world, it has been clear that many market transformations have come from social initiatives or businesses with the imagination, creativity and technology to satisfy savings, lending and payment needs.

For example, in many countries, innovations have included the creation of peer-to-peer platforms, which pinpoint matches between those who seek loans with savers who decide to lend. Another method, crowdfunding, has become a popular way for firms seeking loans and previously analyzed by the platform to sell their shares on-line and convert investors into shareholders and creditors.

Analogously, in Mexico, some firms which distribute their products in small retail establishments have facilitated the use of electronic means for cash management and payments, incorporating a significant number of very small businesses in the financial sector.

These kinds of initiatives, well-regulated and undertaken with caution, allow families and communities to build savings and start new businesses which increase basic capacities, generate income, and help them fight against inefficiency and poverty. At the same time, formal financial intermediaries can complement and develop these projects to generate permanent customers.

## Conclusion

Financial inclusion engenders benefits for the population as well as for intermediaries. The lowering of costs through technology can allow the harmonization of popular forms of finance with formal services.

We should learn, then, to assimilate financial schemes which originate in society. Numerous experiences prove that modifying paradigms and using creativity to extend financial services is not only an activity with enormous social impact, but also, good business.