## Muhammad bin Ibrahim: Towards proportionality in practice – financial inclusion and implementation of global standards

Opening remarks by Mr Muhammad bin Ibrahim, Deputy Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the Global Symposium on Proportionality in Practice, Kuala Lumpur, 28 May 2015.

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Ladies and gentlemen, thank you for the opportunity to speak today at the opening of the Global Symposium, with the theme "Towards Proportionality in Practice: Financial Inclusion & Implementation of Global Standards".

Financial inclusion has captured the attention of many decision makers around the globe. We can confidently say that we have been successful in educating the world on the importance of ensuring access and usage of quality financial services by all segments of society. I think it has dawn to the power that be that financial inclusion empowers low income households and SMEs to improve their livelihood and because financial inclusion provides equal opportunities (and hopefully, it appropriately designed, equal outcomes), it also enables the under served to save in a secure manner, invest in productive activities and protect against unforeseen shocks. Financial inclusion, based on empirical evidence also reduces ***inequality***[1], which in turn supports inclusive and sustainable growth, by allowing the poor to stay healthy, stay out of poverty, pay for education and accumulate human ***capital***[2]. It is, a very worthwhile agenda to pursue.

The scale of the unbanked in term of numbers is still significant globally and financial inclusion as a development agenda can contribute immensely towards resolution of this matter, but it requires collective and concerted efforts among diverse group of people. According to the FINDEX 2014 data by the World Bank, 2 billion adults worldwide do not have access to financial services. The International Finance Corporation and McKinsey reports that 380 million Micro, Small and Medium Enterprises in developing countries do not have adequate access to credit. The extent of financial exclusion is still formidable.

Recognising the scale and extent of financial exclusion, national authorities, regional groupings and international organisations have elevated financial inclusion as a policy priority. In Malaysia, we had decided to legislate this agenda into our statute as one of Bank Negara Malaysia's primary functions, embedded in the Central Bank Act 2013. Recently, at the regional level, the ASEAN Finance Ministers and Central Bank Governors agreed to establish a Financial Inclusion Working Committee to deliberate and coordinate efforts to enhance financial inclusion within its member countries. International organisations such as the Alliance for Financial Inclusion (AFI), the World Bank and the United Nations Capital Development Fund (UNCDF) are also actively developing financial inclusion knowledge, and supporting countries in implementing financial inclusion strategies globally.

Over the years, we have since witnessed the rapid deployment of innovative financial inclusion solutions that have changed the lives of many. Since the introduction of the MPESA mobile banking service in Kenya, the number of adults with access to financial services has increased from 42% in 2011 to 75% today. Agent banking in Malaysia has provided consumers with an innovative and alternative channel to access financial services, resulting in the percentage of sub-districts served by financial services access point to increase from 46% in 2011 to 96% in 2014. This has enabled 99% of Malaysians, particularly those in rural areas, to conveniently access and benefit from financial services. The microfinance

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1 "Global Financial Development Report 2014", World Bank, 2014.

2 Discussion note "Redistribution, Inequality, and Growth", IMF, 2014.

institution Grameen Bank in Bangladesh has extended credit through its 2,500 branches to almost 8 million people, with 60% of them lifted from poverty. The loan recovery rate is higher than 98 percent. The experience in Bangladesh, in particular, dispels the myth that the poor is not bankable.

## Of proportionate regulation and the global standards

The proportionate application of Global Standards for financial regulation is a critical factor in enabling innovative financial inclusion solutions, ensuring its delivery in a safe and sound manner. My remarks today will touch on the following topics:

Recent developments in global standards and financial inclusion;

Focus areas to advance Proportionality in Practice; and

The importance of the Global Symposium to galvanise action.

## Recent developments in global standards and financial inclusion

Global standards developed after the Global Financial Crisis were designed to address the financial stability and integrity issues that came to the fore in developed countries. Many of these issues involved the activities of Global Systemically Important Financial Institutions. The effects of these standards on financial inclusion, such as the impact on smaller financial institutions in developing countries most likely were not taken into consideration. Fortunately, Standard-Setting Bodies have now recognised the principle of proportionality, emphasising on the balance between objectives of financial stability, integrity and inclusion.

However, the real challenge lies in implementing proportionality in practice. If principles are not implemented in a proportionate manner, there could be unintended consequences for financial inclusion. For example, despite the Financial Action Task Force's guidance on the implementation of a risk-based approach to Anti Money Laundering/ Counter Terrorist Financing regulation, we have seen large-scale de-risking by international banks, where banks have indiscriminately terminated businesses in certain segments rather than on a case-by-case basis, or based on proper assessments of risk. In particular, international banks have exited entire areas of businesses, such as relationships with Money Transfer Operators, resulting in Money Transfer Operators no longer being able to provide remittances services for customers, mostly migrant workers remitting money to low-income family members. This indiscriminate de-risking deprives poor families of vital financial resources to live healthily, support and educate their children for a better future. Such unintended consequences have been further compounded by a lack of clarity around acceptable standards for applying simplified customer due diligence processes, and the fear of steep fines imposed by some regulators for non-compliance with anti-money laundering requirements.

These problems will only increase unless the gap between principle and practice is bridged, or else the millions that remain unbanked would bear the brunt of this unintended consequence. These developments also highlight the need for us to rethink the suitability of overdependence on foreign-owned institutions in expanding financial inclusion initiatives in domestic markets or the strategy, to develop 'domestic champions' for such initiatives.

## Focus areas to advance proportionality in practice

Allow me to now share three ideas that could further enhance proportionality in practice. First, further coordinated efforts are needed to develop and propagate more widely frameworks for measuring the impact of regulation on financial inclusion. Such frameworks should be able to objectively assess, based on a well-defined and consistently applied measures, how regulation either increases or reduces barriers to financial inclusion. Such barriers could be in the form of reduced geographical access, exclusive criteria to qualify for financial services, prohibitive costs of financial services or a concentration of products designed only for affluent customer segments.

It is important for policymakers to collect data to facilitate cross country comparisons. In particular, the data should measure the impact of proportionate regulation on financial inclusion, financial stability and integrity. Comparability is key, because it allows policymakers to assess how different proportionate regulation approaches affect intended outcomes in different jurisdictions. The goal here is to identify and disseminate tested and proven proportionate regulation best practices, well supported by empirical evidence. The evidence on proportionality in practice facilitates regulators and financial institutions in implementing innovative solutions because they have the confidence that there would be no adverse unintended consequences to financial stability and integrity. Empirical data can also support Standard-Setting Bodies in designing differentiated guidance for financial services for low-income households and SMEs. While the importance of data collection is obvious, there tends to be under investment and an 'attention deficit' among decision makers on such a critical matter.

Second, it is crucial to build the capacity of regulators, supervisors and financial institutions so that the ecosystem has the requisite capacity to implement proportionality in practice. The Basel Range of Practice Survey highlights supervisors' unmet demand for capacity building, as only 30% of supervisors globally had received training on supervision of banking services for the low income segment. The Basel Meeting with Standard-Setting Bodies on 2 October 2014 chaired by Her Majesty Queen Maxima, the United Nations Secretary General's Special Advocate, also highlighted the importance of technical assistance programmes to build up local knowledge and capacity of national supervisors, so that experience in applying proportionality can be shared.

Third, it is timely for financial regulators to engage non-financial regulators such as telecommunication authorities at a global and national level, in order for regulation to keep abreast with the latest developments in financial inclusion solutions. Technology plays a significant role in rapidly scaling up financial inclusion by lowering the cost of delivery as well as increasing convenience and quality of services for the masses. Technology enables us to bypass legacy systems and constraints. For example mobile banking, where banks partner with mobile network operators to offer banking services anywhere, any time and in real time, that has enable reach beyond traditional boundaries without the need for a huge investment in infrastructure.

### Importance of the Global Symposium to galvanise action

This leads on to why we are gathered here at this symposium. The Global Symposium will discuss and highlight the detailed next steps to implement proportionality in practice. This Symposium uniquely brings together the relevant key stakeholders to deliberate the issues of proportionality in practice. The AFI's Working Group members on Digital Financial Services, SME Finance and Global Standards will share their perspectives on regulatory and supervisory matters.

The private sector banks and remittance service providers share practical realities in the market to comply with international standards. In addition, we have international experts from the SEACEN, Toronto Centre and World Bank, who have a pivotal role in implementing effective projects to advance Proportionality in Practice.

Of importance, this Symposium will culminate in an Outcome Statement that captures the actionable recommendations from deliberations among subject matter experts and key stakeholders over the next two days. It is my hope that the Outcome Statement will at least identify 5 practical and easily implementable suggestions and the statement will be adopted by all participants, and provide us with a clear way forward to execute and deliver the recommendations on "Proportionality in Practice" that make it a reality and make a difference for the 2 billion individuals that remain unbanked.

Finally, I would like to also convey my sincere appreciation to our co-host, the Alliance for Financial Inclusion and Toronto Center, for all their contributions to this Symposium.