

THE ADVISORY GROUP ON APEC FINANCIAL SYSTEM CAPACITY-BUILDING

A Public-Private Sector Initiative

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The Asia-Pacific Financial Inclusion Forum

Summary of Outcomes

Office of the Advisory Group Chair

- PURPOSE** For information.
- ISSUE** Summary of outcomes of the Asia-Pacific Financial Inclusion Forum.
- BACKGROUND** The first APEC Financial Inclusion Forum was convened in 2010 by the APEC Business Advisory Council (ABAC), jointly with the Advisory Group on APEC Financial System Capacity Building and in cooperation with the Ministry of Finance of Japan in their Kyoto Report on Growth Strategy and Finance, APEC Finance Ministers welcomed ABAC's initiative to set up subsequent discussions.
- This year's Forum provided a venue for policy dialogue on expanding new channels to serve the financial needs of the unbanked and under-banked and a platform for capacity building to help relevant policy makers and regulators in the region address two key issues for expanding credit to micro-, small and medium enterprises (MSMEs): credit information and legal frameworks for secured lending. It drew on the combined expertise and experiences of the public and private sectors, international institutions and academe from throughout the region.
- PROPOSAL** N.A.
- DECISION POINT** Note the outcomes of the Forum.



THE ASIA-PACIFIC FINANCIAL INCLUSION FORUM
JOINTLY ORGANIZED BY
THE APEC BUSINESS ADVISORY COUNCIL
THE ASIAN DEVELOPMENT BANK INSTITUTE
EXPANDING FINANCIAL ACCESS THROUGH REGIONAL PUBLIC-PRIVATE
COOPERATION

6-8 September 2011
Asian Development Bank Institute
Tokyo, Japan

SUMMARY OF OUTCOMES

The first APEC Financial Inclusion Forum convened in 2010 by the APEC Business Advisory Council (ABAC), jointly with the Advisory Group on APEC Financial System Capacity Building and in cooperation with the Ministry of Finance of Japan, focused on how to provide enabling environments to extend the reach of microfinance, improve its commercial viability, and increase private investment in MFIs. In their *Kyoto Report on Growth Strategy and Finance*, APEC Finance Ministers welcomed ABAC's initiative to set up subsequent discussions.

This year's Forum¹ provided a venue for policy dialogue on expanding new channels to serve the financial needs of the unbanked and under-banked and a platform for capacity building to help relevant policy makers and regulators in the region address two key issues for expanding credit to micro-, small and medium enterprises (MSMEs): credit information and legal frameworks for secured lending. It drew on the combined expertise and experiences of the public and private sectors, international institutions and academe from throughout the region.

The following are key points arising from the discussions:

- ❑ Currently, an estimated 2.7 billion people in emerging markets do not have access to financial services. With total commitments to microfinance amounting to only US\$21.3 billion at the end of 2009 (68% from the public and 32% from the private sector), it is clear that the needs of the financially underserved are much greater than what the public sector, with increasingly limited resources, can meet. More private sector resources will be needed to meet these needs; mobilizing them through partnerships with multilateral institutions, export credit agencies and other public entities should also be explored.
- ❑ Developing a cohesive financial ecosystem is important for success. This requires comprehensive strategies covering financial service providers, distribution channels, banking products and services, financial literacy and financial infrastructure; concrete measures to address issues; assigning clear and specific roles to agencies and institutions; and strong public-private sector collaboration.
- ❑ Various microfinance crises (including the recent one in Andhra Pradesh) underscore the importance of responsible credit, which requires a strong credit underwriting culture. Addressing the lack of such a culture requires partnership between the public and private sectors, through such initiatives as codes of conduct and regulatory reforms. Development of information sharing systems and promoting consumer protection and financial literacy

¹ The Forum was co-organized by ABAC and the Asian Development Bank Institute (ADBI), in collaboration with the Asia-Pacific Credit Coalition (APCC)/PERC, the Asia-Pacific Finance and Development Center (AFDC), the Banking with the Poor Network (BWTP), the Foundation for Development Cooperation (FDC), the Institute for International Monetary Affairs (IIMA) and the Organisation for Economic Co-operation and Development (OECD), and sponsored by Citi.

are key to promoting sustainable lending operations targeting low-income households and micro- and small enterprises.

- ❑ Convenient and reliable savings services are of prime importance to low-income households. Deposits also provide an inexpensive and stable source of funding for MFIs and help them become resilient to external shocks. Mobilizing small savings involves a number of challenges. On the supply side, these include adapting regulatory frameworks to local contexts, sustainability of business models and designing products appropriate for low-income clients. On the demand side are the prevalence of competing informal savings vehicles among low-income households, lack of trust in the formal banking system and lack of information on banking institutions and services. Addressing these issues requires a comprehensive approach that involves a combination of policies and market-driven initiatives. These should include (a) financial education; (b) consumer protection; (c) proper financial regulation; (d) access to banking products; and (e) information on available financial services.
- ❑ Consumer protection is key to sustainable microfinance. It is a complex issue that requires a local approach and close collaboration among banking supervisors. Key client protection principles include appropriate product design and delivery, prevention of over-indebtedness, transparency, responsible pricing, fair and respectful treatment of members, privacy of member data and mechanisms for complaint resolution.
- ❑ Financial education is a necessary complement to consumer protection.. An important first step is to educate people about the benefits of saving through the formal financial system, i.e., greater security, cost and affordability vis-à-vis informal savings vehicles, and potential access to a wide range of financial services such as lending, payment and remittances. Financial education also needs to focus on inculcating the habit of savings, helping low-income clients understand basic financial concepts, opportunities and options to more efficiently use savings, and how to successfully and safely use new delivery channels such as branchless banking.
- ❑ Market mechanisms are essential to minimizing risks, efficient use of public funds and a healthy financial system. Policies and regulations should facilitate the provision of financial services within a competitive policy framework. Measures that distort the provision of such services have deleterious effects that accumulate over time, and should be replaced with effective market-friendly policies that remove barriers to greater financial access. Where government intervention is needed to address a specific market failure or emergency situation, it should be carefully undertaken only for a limited period. Examples of such government intervention include subsidized funding, credit guarantees and mandated lending programs for specific sectors. Ineffective interventions can be minimized through the undertaking of pilot tests and impact analysis based on adequate measurements.
- ❑ Laws and regulations need to be reviewed with a view to reducing impediments to greater financial access. Priority areas include, among others, discriminatory provisions adversely affecting financial access of certain borrowers, such as women and young people, accounting and reporting requirements, license and permit requirements and fees and charges as applied to small businesses. Taxation policies should encourage more start-ups and enterprises to enter the formal sector, where their ability to access finance can be enhanced.
- ❑ Sound and proportionate regulatory policies and laws are needed to promote access to finance. A light regulatory approach allows innovations that can promote greater financial access. Collaboration among relevant agencies and between regulators and industry are important for the adoption of approaches that can allow regulation to follow, rather than stifle, innovation and the use of new technologies. Regulators should keep abreast of innovation, particularly in payments systems and new forms of delivery of financial services.

- Remittances have great potential for promoting financial inclusion, and are expected to grow in importance in coming years. An estimated US\$450 billion are remitted by migrants to developing economies every year. To the East Asia and Pacific region, about 21 million migrants remitted from all over the world over US\$90 billion in 2010. The region itself is host to around 7 million migrants, which are expected to increase considerably with the region's growing economic integration. Three major issues in the management of remittances are: (a) reducing remittance transfer costs; (b) channeling remittances to the financial system, savings and investment; and (c) macroeconomic management and the investment climate.
 - Reducing costs of remittances is important because remittance flows tend to be highly sensitive to remittance costs. There are wide variations in costs, which can range from 2.5% to 26% of the total amount. Costs are relatively high for the East Asia and Pacific region, compared to South Asia, Latin America and Europe/Central Asia. Costs can decrease with greater competition among RSPs and larger numbers of migrants.
 - Linking remittances more closely to banks and financial institutions such as MFIs or savings cooperatives can promote the mobilization of savings. In the Americas, banks with cross-border branch networks have developed efficient electronic transfer arrangements. However, branch networks are relatively less developed in the East Asia and Pacific region. Connectivity between transfer and deposit points is a key issue. Various means can be considered to harness migrant savings more efficiently. Branchless banking infrastructure based on information technology and telephony using mobile wallets and pre-paid cards can help reduce costs. Such infrastructure is already being deployed in a number of economies, with more being developed. MFIs can play greater roles in money transfer services, cash and management products and lending products that use remittances as guarantees. Collaboration among MFIs can play an important role in linking remittances to other financial products such as savings accounts, micro-loans and mortgage and business loans.
 - A good macroeconomic environment and investment climate are fundamental requirements for attracting remittances and making them more productive.
- Information sharing systems play a key role in promoting sustainable lending operations by reducing risks and costs for lenders and borrowers alike. Such systems reduce information asymmetries and provide disciplinary mechanisms that create incentives for borrowers to make timely payments. They reduce operational costs for lenders. They reduce costs for borrowers through greater competition and lower search costs. The effectiveness of such systems depends on good regulations on data quality, data content and protection of consumers, as well as on adequate consumer understanding and the technical capability of lenders.
- Sound and effective legal frameworks and institutions are fundamental to effective promotion of financial access. Weak legal frameworks and institutions that do not provide adequate protection of security interests and enforcement of contracts discourage lenders from allocating more funds to smaller enterprises that are perceived as riskier than more established firms, and discourage small borrowers with limited resources to protect their legal rights from using financial services as well. Promoting access to finance requires robust laws governing bankruptcy, insolvency and intellectual property rights, courts with appropriate commercial jurisdiction that are accessible to both lenders and small borrowers, qualified and competent judges, case management and judgment enforcement resources and supporting institutions including credit bureaus and security registers. Accessible, independent and cost-effective external dispute resolution mechanisms should also be considered.