Keynote Address by
Dr. Zeti Akhtar Aziz,
Governor, Bank Negara Malaysia
at the Alliance for Financial Inclusion (AFI) 2014 Global Policy Forum

"Advancing Financial Inclusion to its Next Level"

Port of Spain, Trinidad and Tobago
10 September 2014

---

1. It is my very great honour to be invited to speak at this year's AFI Global Policy Forum in beautiful Trinidad and Tobago. First of all, on behalf of Malaysia, let me express how greatly honoured we are to be given this opportunity to host the headquarters of AFI. Malaysia is strongly committed to the financial inclusion cause and will strive to the fullest and best of our ability to provide the necessary support to AFI towards achieving its objectives. This is an exciting time for advancing the global financial inclusion agenda, as the world economic recovery gains further progress and as there is increasing world attention and priority being accorded to achieving financial inclusion and to an economic progress that is more inclusive.

2. While stability and growth has been restored in many parts of the world, all of us recognise that economic growth, no matter how stellar, will begin to fade when inequality sets in, and as income disparities widen. Additionally, experience has shown that financial crisis and economic recession entrenches the cycle of poverty. It has been estimated that during a financial crisis, poor households lose 10 times more of their income compared with the average household.

3. The role of financial inclusion has thus become more magnified as a means to improve the livelihoods and as a means to strengthen the financial resilience of the disadvantaged. It provides the opportunity to save for the future, to invest and generate income and to insure against adverse events. The relative stability and improving global conditions, therefore, provides us with the opportunity to accelerate the financial inclusion agenda as a global imperative.

4. The theme of this year's Forum, "Global Partnerships, National Goals, Empowering People" highlights that financial inclusion is a shared responsibility. The significant progress that has been achieved in advancing financial inclusion, has also provided us with the opportunity for further advancement that would support and facilitate greater scale and sustainability of inclusive finance. Allow me to touch on five potential areas which I believe would cumulatively contribute towards advancing financial inclusion to its next level, both at the national and international level.

Priority 1: Focus on relevant and quality financial services

5. Significant strides have already been made in the area of improving access to financial services. Within a short span of three years, AFI has been instrumental in galvanising commitments from member countries to enhance financial inclusion policies, resulting in 20 million of the unbanked to gain access to financial services. Yet we wish to achieve more than just access. The nature and quality of the financial services and the nature of the participation in the financial system is equally important. The poor are confronted with challenging circumstances, such as low and irregular income that makes monthly debt-servicing difficult, or living in remote rural areas which have no financial services access points, or long working hours that prevent visiting bank branches within the conventional operational hours. As a result, many of the marginalised may have financial services made available to them, but it may not be at the needed conditions or quality that can provide the real promise of upward economic mobility.

6. Access, therefore needs to be complemented by the quality of the financial services. Of importance is the innovation and design of consumer products which have characteristics that are linked to the goal of welfare improvements for the underserved. There is a greater need for features that are responsive to the constraints faced by those that have been marginalised. Flexible microfinance for the agricultural sector for example, addresses the cash flow mismatches between fixed repayments to banks and the irregular income flow of the farmers due to the seasonality of crops. A further innovation has also involved the creation of platforms for matching savers with those that need financing. In Malaysia, the introduction of investment accounts as opposed to deposit accounts in the Islamic financial system is an example, where savings are matched with the funding required by small and medium scale enterprises for financing of specific projects – has resulted in an investment intermediation function by the banking institutions.

7. In addition to innovation, technology is also an agent to deliver quality financial services. Technology can lower cost, increase outreach and expand the range of financial services. The Kenyan mobile payment services, M-PESA, leverages on mobile technology to provide the poor with high frequency, small value transactions and affordable financial services.

Priority 2: Building on the Sasana Accord for measurable goals

8. The second area relates to the identification and adoption of the measureable and time-bound targets as included under the Sasana Accord. Clear and measurable outcomes provide a shared understanding that will align the different stakeholders towards the common goal of delivering results to the financially excluded segments of society.

9. A key aspect of realising the Sasana Accord is to collect and compile the relevant data in a reliable and timely manner. This will also form a basis for better policy formulation and effective monitoring and assessment of the effectiveness of policies. Data coverage needs to involve both the mobilisation of savings and financing activities, including information on the profile of the new entrants into the formal financial system. This is not only to promote effective participation in the financial system but to avoid conditions of over leverage and indebtedness. Access to credit registries to financial service providers would also support the sustainability of the supply of such services. Such financial statistics also needs to evolve with the changing environment including on the range of products and services, the distribution channels and the relative performance of the borrower and the financier. This will allow for early detection of risks and vulnerabilities and thus allow for prompt policy responses to ensure sustainable financial intermediation for the underserved sector.

Priority 3: Strengthening the role of regulation and supervision

10. The third area relates to the role of regulation and supervision in financial inclusion. Today, there is a growing consensus that the policy goals of financial stability, financial integrity, consumer protection and financial inclusion are complementary and mutually reinforcing. There is now a re-thinking of prudential and conduct regulation to reflect a more proportionate approach. The validation by global standard setting bodies that includes the Basel Committee on Banking Supervision, the Insurance Association of Insurance Supervisors, and the Financial Action Task Force that regulation should be commensurate with the risks, benefits and costs is a significant step towards improving the regulatory and supervisory conditions that will be consistent with the conditions for financial inclusion.

11. While the principles of proportionality are widely embraced, there is much less clarity on how they can be applied in practice to reflect risks associated with low-income households and small businesses. The practical issues can be challenging particularly in the context of full service banks. Lending and provisioning standards, reporting requirements, minimum capital adequacy and customer due diligence requirements are among the key areas in which there is still little formal distinction made to address the impact of such regulations on the access to financial services to low income households and small borrowers.

12. Global standard setting bodies therefore have an important role in accelerating the conversion of proportionality principles into practice. This will also be important in the assessment of national financial systems and how it measures up against global standards. For example, under the Financial Sector Assessment Programme (FSAP). Therefore, there are significant benefits to be gained from the provision of guidance to authorities on how regulation can be assessed for its impact on access. Such considerations could also be reflected in the methodologies adopted by international bodies for financial sector assessments and peer reviews.

13. The capacity and capabilities of authorities to provide supervisory oversight financial activities that target the underserved is equally important. Our experience has been that the supervisory skillsets required to evaluate the effectiveness of controls over microfinancing and microinsurance operations differ substantially from those traditionally applied to the retail portfolios of banks and insurance companies. A greater understanding of the product design implications, the relationships that a financial service provider has with its customers and the different motivations that drive consumer behaviour will be important. This is to avoid counterproductive supervisory actions on financial access.

Priority 4: Empowerment through consumer protection and education

14. The fourth area relates to the greater empowerment of consumers through consumer protection and education. Both the financial service industry and the financial consumers have an important respective role for financial inclusion to transition to a higher level. Financial inclusion is best achieved when consumers are assured of fair treatment. In developing financial products by the service providers, of great importance is their professional and ethical conduct. Here, the role of the Board and senior management of such financial service providers need to set the right culture, policies and incentive systems that support fair and responsible

business practices. Policies that promote responsible market conduct that is reinforced by transparent disclosure requirements will be important in advancing responsible financial inclusion.

15. A key aspect of a successful financial inclusion agenda is also building financial capability of consumers so that they can meaningfully participate in the financial system. Financial education, as with other forms of education, is a powerful agent of empowerment. It empowers consumers with the knowledge, skills and tools to build, manage and protect their personal wealth. In Malaysia, efforts to systematically build financial capability among the population began almost twenty years ago, in 1996, when a National Savings Promotion Campaign was launched to enhance awareness on the importance of savings, including among school children. Since then, a more holistic and comprehensive consumer financial education programme for both children and adults has been implemented for more effective participation in the financial in the financial system.

Priority 5: Improving cooperation and partnerships

16. The fifth area relates to that which has been highlighted in the theme for this Forum, the need for greater cooperation and innovative partnerships. The goal of achieving financial inclusion that delivers real and positive impact to the poor is a shared responsibility. The barriers to financial inclusion can only be resolved when different stakeholders, each with different spans of authority and oversight, work together in a coordinated and cohesive manner. It will need to involve the cumulative efforts of the government, regulators, market agents, the financial industry and the consumers.

17. At the national level, improving inter-agency cooperation is vital to ensure that the respective strategies are aligned to achieving the common goals of financial inclusion. This may call for institutional arrangements to bring authorities together to secure a joint commitment towards clearly defined and measurable financial inclusion goals, with well-defined lines of accountability. Brazil, Mexico, Tanzania, Indonesia and Fiji have also established national co-ordination frameworks, which offer AFI members diverse examples of such national collaboration.

18. While we focus on financial inclusion initiatives at the national level, equally important is that adequate attention be accorded at the global level. In this regard, AFI assumes a unique role because it is the only global network that comprises of practising financial inclusion policy makers. Therefore, AFI has an important role in leading the way in gathering

examples of best practices based on specific country experience, in the area of financial inclusion and its relation to financial stability and consumer protection objectives. AFI is therefore also a key platform that brings together policymakers, financial service providers, telecommunication and technology industries to have greater awareness on the trends that can support the advancement of financial inclusion. Additionally, AFI's engagement with international organisations is also key given the implications of their initiatives on financial inclusion.

Conclusion

19. Let me conclude. There is now greater appreciation that the level and quality of financial inclusion will have a significant impact on the prospect for balanced and sustainable growth. AFI has demonstrated its important role in leading the way for greater financial inclusion in the world economy. AFI is unique because its membership covers practitioners from developing and emerging economies, who can share approaches that can be customised to a respective country's unique circumstances. We begin this two day global policy forum, with our vision firmly focussed on our long-term goal of universal access to quality financial services which will provide our communities with the chance to change. This Global Forum and AFI provides an unparalleled opportunity that brings together strategy, knowledge, expertise and best practices from across the AFI membership. This provides us with the real potential to make a difference in financial and economic inclusion and thus with the potential to transform lives.

Thank you.

10 September 2014