G 20, International Standard Setting Bodies and Access to Finance

AASC and ADFIAP Joint Regional Symposium

"Best Practice Regulatory Principles Supporting MSME Access to Finance"

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What are we going to cover?

Why G20 and International Standard Setting Bodies (SSBs) are relevant for Access to Finance

G 20 “Principles for Innovative Financial Inclusion” and the “Multi-Year Action Plan on Development”

Bank of International Settlements (Basel) “Microfinance Activities and the Core Principles on Effective Banking Supervision”

And the work of FATF, IAIS, CPSS, IADI and IOSCO (in brief!)

The story so far…

Access to Finance regulation is determined at the country / provincial level and sometimes by regional bodies. But…

2009 Pittsburgh Summit: G20 in effect became the "global financial architect". " **We commit to** improving access to financial services for the poor. … **promote successful regulatory & policy approaches** & elaborate standards on financial access, financial literacy, and consumer protection."

Financial Inclusion Experts Group (**FIEG**) formed with two Sub-Groups: SME Finance Challenge and Access Through Innovation. FIEG approached SSBs

The story continued

2010 Toronto Summit: Principles on Innovative Financial Inclusion approved (**G20 Principles**)

2010 Seoul Summit: Global Partnership on Financial Inclusion formed to: Advance G 20 Principles; Encourage SSBs to take account of Principles; Increase access to private financial services

GPFI came out of Multi-Year Action Plan on Development which included as one of its pillars a commitment to " *increase access to finance for the poor and small and medium enterprises (SMEs)*"

SME Finance Innovation Fund established

G20 Principles

Leadership: Cultivate a broad-based government commitment to financial inclusion to help alleviate poverty.
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.
Innovation: Promote technological and institutional innovation as a means to expand financial system access and usage, including by addressing infrastructure weaknesses.
Protection: Encourage a comprehensive approach to consumer protection that recognises the roles of government, providers and consumers.
Empowerment: Develop financial literacy and financial capability.

G20 Principles cont….

Cooperation: Create an institutional environment with clear lines of accountability and co-ordination within government; and also encourage partnerships and direct consultation across government, business and other stakeholders.
Knowledge: Utilize improved data to make evidence based policy, measure progress, and consider an incremental "test and learn" approach acceptable to both regulator and service provider.
Proportionality: Build a policy and regulatory framework that is proportionate with the risks and benefits involved in such innovative products and services and is based on an understanding of the gaps and barriers in existing regulation.
Framework: Consider the following in the regulatory framework, reflecting international standards, national circumstances and support for a competitive landscape: an appropriate, flexible, risk-based Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) regime; conditions for the use of agents as a customer interface; a clear regulatory regime for electronically stored value; and market-based incentives to achieve the long-term goal of broad interoperability and interconnection.

The SSBs

SSB	Standards
Bank of International Settlements Committee on Banking Supervision (Basel)	Deposit Taking Institutions
Financial Action Task Force (FATF)	Anti-Money Laundering and Counter-Financing of Terrorism
Committee on Payment and Settlement Systems (CPSS)	Payment and Securities Settlement Systems
International Association of Insurance Supervisors (IAIS)	Supervision of insurers and insurers
International Association of Deposit Insurers (IADI)	Supervision of deposit insurance schemes

4 Basel Themes for Regulation of Microfinance Institutions

Define “microfinance” carefully

Allocate supervisory resources efficiently

Supervisors need specialized knowledge

Proven control practices may be different for microfinance

Key Basel Proposals….

CP 2: Permissible activities: the definition on “microfinance” is critical. Consider type and size of activities. Register MFIs. Compulsory savings may be OK with out regulation if balances less than loans. Non financial activities should be in a separate entity

CP 3: Licensing criteria / minimum capital: a tiered licensing approach is contemplated

CP 6: Capital adequacy: focus on (i) nature of microfinance risks and (ii)size and constituents of capital of specialized MFIs. Specific microfinance risks may mean higher capital requirements.

Key Basel Proposals….

CP 7: Risk management process: supervisors need specialized knowledge and to tailor supervisory techniques. Focus on credit risk but there are others e.g. proportionate size of MF portfolio and governance issues

CP 8: Credit risk: these risks are significantly different due to differences in product design, loan methodology, client profile. Again need a clear definition of microcredit

CP 9: Problem assets, provisions and reserves: need different provisioning /classification given risk of rapid deterioration of loans.

Key Basel Proposals….

CP 10: Large exposures: important to manage sector and geographic concentrations

CP 14: Liquidity risk: Limit concentrations from a single funding source. Note risks with use of agents – especially in remote areas. Can be more flexible with start-ups.

CP 15: Operational risk: need deep understanding of distinctive risks / trends – including outsourcing, decentralized lending and use of new technologies, delivery channels and agents.

Key Basel Proposals

CP 16: Interest rate risk: will be higher if have relatively high proportion of fixed rate loans.

CP 19: Supervisory approach: Key is to take into account sector specific risks, costs of supervision (e.g. of large numbers of MFIs) and the capacity and expertise of supervisors

CP 23: Corrective powers of supervisors: tools may be different for microfinance activities e.g. could restrict new members of a co-op if implementing a correction plan. Also – need to be careful re stop lending order as may damage whole portfolio given expectation of future loans

Basel MF Rules: Critical Challenges

Proportionality is King : emphasis should be on the risks of the MFI business (not just the size of the sector)

Focus should be regulations that **make it easier for ODTIs to raise capital** e.g. foreign investors and venture capital (especially favourable tax treatment)

Remember that **MFIs are different from large banks** because MFIs tend to borrow long and lend short (which means liquidity should not be such a concern)

The rules are only relevant to MFIs that take deposits from small investors – if funds are largely sourced from large investment vehicles or banks they are less risky

Basel should have emphasized **information sharing / credit bureaus**

Risks in new channels (CP 15): " risk management standards… should be carefully crafted". What does this mean?

The work of other international bodies

- FATF
- IAIS
- CPSS
- IAD

FATF

FATF Recommendations that might impact access to finance:

- R5: customer due diligence – initial identification and verification and ongoing scrutiny of business relationship and monitoring of transactions
- R8: requires special attention to new or emerging technologies
- R9: restrictions on the use of intermediaries
- R10: 5 year record keeping requirements
- R13: reporting of suspicious transactions

FATF cont….

FATF President said on 10 March 2010: *“ AML/CFT measures should and in my view can be reconciled with financial inclusion and thus contribute to a sustainable development of international financial markets”*

FATF Working Group on Evaluations and Implementations considering financial inclusion

Guidance Paper on Financial Inclusion due June 2011

FATF October 2010 paper on *“Money Laundering Using New Typologies “* is also relevant

IAIS

IAIS represents insurance regulators and supervisors of some 190 jurisdictions in nearly 140 countries, constituting 97% of the world's insurance premiums. It also has more than 120 observers

Access to insurance initiative: IAIS Joint Working Group with Microinsurance Network

IAIS Issues Paper in Regulation and Supervision of Microinsurance (June, 2007)

IAIS Issues Paper on the Regulation and Supervision of Mutuals, Cooperatives and other Community-based Organisations in increasing access to Insurance Markets (October, 2010)

CPSS and others

BIS / CPSS is a standard setting body for payment and securities settlement systems

CPSS recently released for public comment the *Principles for financial market infrastructures* which contain new and more demanding international standards for payment, clearing and settlement systems. It will replace other CPSS/ IOSCO Standards.

Also – note the work of the OECD Task Force on Financial Consumer Protection – aim is to develop common principles on financial consumer protection by G 20 Finance Ministers Meeting in October, 2011. World Bank, FSB and others involved in this work.

IADI

IADI mission is to enhance the effectiveness of deposit insurance systems by promoting guidance and international cooperation.

IADI represents 63 deposit insurers from 62 jurisdictions.

Basel / IADI Core Principles for Effective Deposit Insurance Schemes suggest deposit insurance should be mandatory

Have just held a conference in Africa on ***"Financial Stability in Africa: Role of Deposit Insurance & Financial Inclusion"***

But is there a connection? Is deposit insurance a good idea? Are there other options? What is a deposit anyway?

Take- Aways!

It is important to follow the work of the international standard setters

The trend is to be more flexible in regulatory standards for microfinance – but we need to understand what makes the sector different

There is a cost /benefit trade off to regulatory policy

And good regulations are useless with out appropriate supervisory capacity and implementation…

Everything is context specific – there is not any one right answer

Recommended Reading

http://www.g20.utoronto.ca/summits/2010toronto.html

http://www.bis.org/press/p100830.htm

http://www.fatf-
gafi.org/document/28/0,3746,en 32250379 32236920 33658140 1 1 1 1,00.html

http://www.access-to-insurance.org/the-initiative.html

http://www.iadi.org/

http://www.bis.org/cpss/index.htm