



Advancing financial access for the world's poor

**The global enabling environment for microfinance:
*the G20, the Financial Action Task Force, the Basel
Committee and the other standard setting bodies***

UNCITRAL International Colloquium on Microfinance
Vienna, 12-13 January 2011

Agenda

Background – global bodies affecting microfinance/financial inclusion policy

G20 – new global financial architect embraces financial inclusion

Global standard setters embed financial inclusion in their work

Financial inclusion – SMEs, impact and political economy

Discussion

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Background

Global bodies affecting microfinance/financial inclusion policy

- Financial sector policy made at ***national*** and ***sub-national level***
- But in globalized world ***regional*** and ***international bodies*** have increasing impact
- ***Dynamic relationship***: international bodies are country-led
- Which international bodies have ***greatest impact*** on ***national financial sector policy***?
- ***Not a static picture***: e.g., during financial crisis . . .
 - ***Basel Committee expanded*** to encompass G20 membership
 - ***G20*** assumed a ***primary coordinating role***

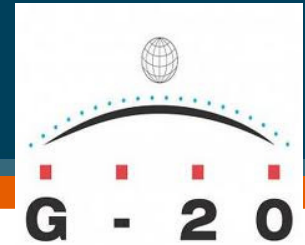
G20 momentum with SSBs



- ***Pittsburgh Summit:*** “Financial Inclusion Experts Group” (**FIEG**) named, focused SME Finance and innovative financial inclusion (sub-group on each; AFI, CGAP & IFC = Implementing Partners)
- ***FIEG outreach to 5 SSBs:*** Financial Action Task Force (**FATF**); Basel Committee (**BCBS**); Committee on Payment and Settlement Systems (**CPSS**); Int’l Assoc. of Insurance Supervisors (**IAIS**); Int’l Assoc. of Deposit Insurers (**IADI**)
- ***Toronto Summit:*** ***G20 Principles on Innovative Financial Inclusion*** approved – very high level, but many closely related to core mandate of SSBs

Culminates in . . .

Global Partnership for Financial Inclusion



- **GPI Sub-Group on G20 Principles & Engagement with SSBs:**
 - *Work stream on implementing G20 Principles on Innovative Financial Inclusion*
 - *Work stream on engagement with SSBs*
 - *Work stream (closely related) in integrating financial inclusion into country level financial assessments (e.g., World Bank/IMF Financial Sector Assessment Program, “mutual evaluations” of the Financial Action Task Force)*

Who are the relevant SSBs?

SSB:

- Basel Committee on Banking Supervision (BCBS)
- Financial Action Task Force (FATF)
- Committee on Payment & Settlement Systems (CPSS)
- International Association of Insurance Supervisors (IAIS)
- International Association of Deposit Insurers (IADI)



Sets standards on:

- Supervision of deposit-taking institutions
- Money laundering & terrorist finance (AML/CFT)
- Supervision of payment systems
- Supervision of insurance and insurers
- Supervision of deposit insurance schemes



Mission: Enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide.

Key financial inclusion issues for BCBS

- Recent BCBS guidance on microfinance calls for specialized knowledge of microfinance when applying Basel Core Principles, but few details provided on some key issues
- BCBS guidance on outsourcing and application of Core Principle 15 (Operational Risk) warrants reflection and possible updating to reflect use of new distribution channels such as mobile phones and retail agents

Main guidance points from BCBS Microfinance Report

4 guidance points for applying BCPs to microfinance

Allocate supervisory resources efficiently

Develop specialized knowledge within the supervisory team



Recognize proven practices that differ from traditional banking

Achieve clarity in regulations regarding microfinance activities

Some Basel Core Principles requiring a tailored approach . . .

. . . in the case of depository microfinance

Principle 6 (Capital adequacy): capital adequacy requirements should relate to (i) the nature of microfinance risks for and (ii) the size and constituents of capital of specialized MFIs. Particular difficulties arise when defining regulatory capital for cooperatives. If risks inherent to microfinance are assessed as higher in a given country, a proportionately higher capital adequacy ratio (CAR) may be warranted.



Some Basel Core Principles requiring a tailored approach . . .

. . . in the case of depository microfinance

To implement **Principle 7 (Risk management process)** effectively, supervisors need specialized knowledge in microfinance to tailor supervisory focus and techniques. Focus should be on credit risk, without losing track of other risks, such as governance weaknesses. In diversified institutions, take into consideration size and importance of MF, so as to use adequate amount of resources in supervision. Remember risk of fast but uncontrolled growth of this sector!



Some Basel Core Principles requiring a tailored approach . . .

. . . in the case of depository microfinance

Supervisors should adjust provisioning and classification requirements **Principle 9 (Problem assets, provisions and reserves)** to the unique risks of microcredit compared to other loan types. The regulation should clearly define microcredit versus other loan types. Past due microfinance loans should be recognized quickly and accurately. Regulatory limitations on exposures dealt with in **Principle 10 (Large exposure limits)** should be tailored to the risks in geographic or sector concentrations often observed in microloan portfolios and across different institutions.



Some Basel Core Principles requiring a tailored approach . . .

. . . in the case of depository microfinance

In applying **Principle 13 (Market risk)** supervisors should pay attention to sources, risks and concentrations in MFI's foreign currency borrowings.

The application of **Principle 14 (Liquidity risk)** and **Principle 16 (Interest rate risk in the banking book)** should take into account the unique features of microfinance assets and funding liabilities, particularly in specialized microfinance institutions.



Inter-governmental policy-making body whose main purpose is to develop and promote national and international standards and policies to combat money laundering and terrorist financing.

Key financial inclusion issues for FATF

- Several FATF recommendations impact financial inclusion:
 - R5: customer identification (CDD) through use of reliable and independent documentation, although FATF does not define “reliable and independent”
 - SRVII requires inclusion of accurate and meaningful originator information on cross-border funds transfers
 - R8 requires “special attention” to new technologies that might favor anonymity
- R9 conditions reliance on CDD undertaken by a third party (but does not cover principal/agent relationships)
- Risk-based approach (RBA) promoted for implementation of several FATF recommendations, but how to adopt RBA rather unclear

Current & recent past financial inclusion-related activities

- Current FATF Chair (Mexico) has stressed importance of financial inclusion, and FATF Working Group on Evaluations and Implementations has put financial inclusion on their agenda
- Several key members (e.g., US) are increasingly vocal on financial inclusion
- *Guidance Paper on Financial Inclusion* (focused on current standards) by June 2011, which will provide high-level guidance on how to bring together AML/CFT policies and financial inclusion (including examples of risk-based approaches, many of which were compiled by WB/CGAP inventory of global practice)
- Updated *Report on New Payment Methods* and related AML/CFT risks (October 2010)



Mission: Strengthen the financial market infrastructure through promoting sound and efficient payment and settlement systems.

Key financial inclusion issues for CPSS

- **Infrastructure development and financial inclusion:** 2007 *National Guidance on Payment System Development* proposes guideline on extending the availability of and improving retail payment infrastructures
- **Infrastructure development and remittances:**
 - CPSS-World Bank *General Principles for International Remittances*
 - Global Working Group for Remittances promotes global implementation of principles and goal of decreasing cost of remittances by 5% in 5 years



Mission: Improve supervision of insurance industry at domestic and international level, maintain efficient, fair, safe and stable insurance markets for the benefit and protection of policyholders; promote the development of well-regulated insurance markets; contribute to global financial stability.

Key financial inclusion issues for IAIS

- IAIS unique among SSBs, as its focus on insurance market development and broad membership (190 members representing almost 140 jurisdictions) make financial inclusion core aspect of its mandate
- Identified financial inclusion as one of its seven points of focus in a recent strategic review



Current and recent past financial inclusion activities

- Joint Working Group with Microinsurance Network generates microinsurance output of IAIS
- Partner in Access to Insurance Initiative (A2II), collaboration of international development agencies and insurance supervisors to:
 - strengthen capacity and understanding of insurance supervisors, regulators and policymakers
 - facilitate role as key drivers expanding access to insurance
 - support implementation of sound policy, regulatory and supervisory frameworks consistent with international standards
- IAIS issues papers on microinsurance currently being developed into IAIS Standards & Guidance

Mission: Enhance the effectiveness of deposit insurance systems by promoting guidance and international cooperation.

Key financial inclusion issues for IADI

- Deposit Insurance Core Principles state membership in deposit insurance schemes should be mandatory for all entities accepting deposits from the public, but . . .
 - in many countries nonbank depository institutions currently fall outside deposit insurance schemes
 - there is no guidance on gray zone between pure payments, stored value instruments and deposits