
Session 6:

FINANCIAL INCLUSION

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WHY FINANCIAL INCLUSION MATTERS FOR DEPOSIT INSURERS

1. INTRODUCTION

It is estimated that more than two billion adults around the world do not have access to formal or semi-formal financial services. The proportions of the world's adult population that are estimated to be unbanked vary widely among countries across the globe, from less than 10 percent to 75 percent or even higher. In many regions of the world, lack of access to financial services among the poor is being addressed through initiatives and innovations in new channels and technologies, including microfinance institutions (MFIs), branchless banking, and e-money.

While much work has been conducted on the topic of financial inclusion, there is no single universally accepted definition of financial inclusion. The term has been defined in various ways, and most recently, in a white paper prepared by the Consultative Group to Assist the Poor (CGAP) on behalf of the Group of 20 (G-20) Global Partnership for Financial Inclusion, as “a state in which all working age adults have effective access to credit, savings, payments, and insurance from formal service providers”.¹

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¹ Consultative Group to Assist the Poor (CGAP) white paper issued on behalf of the G20's Global Partnership for Financial Inclusion (GPII), “Global Standard-Setting Bodies and Financial Inclusion for the Poor – Toward Proportionate Standards and Guidance”, October 2011.

2. FINANCIAL INCLUSION AND DEPOSIT INSURANCE

Financial inclusion is related to deposit insurance in a number of ways.

First, broad access to safe and affordable small savings accounts can promote financial inclusion and help households prepare for unexpected expenses and plan for a more secure financial future.

Second, deposit insurance, which insures the safety of depositors' savings in the event of bank failure, can play a key role in protecting small, unsophisticated savers.

Third, through public awareness initiatives, deposit insurance systems can play a meaningful role to ensure that poor and low-income depositors are informed about safe methods of storing their money and can help build trust in formal financial institutions.

Finally, by promoting financial stability as a component of the financial safety net and ensuring the safety of depositors' savings in the event of the failure of a bank, explicit deposit insurance systems can promote confidence in formal financial institutions and the banking system and help broaden access to the mainstream financial sector.

In all of these ways, deposit insurance can play a direct or indirect role in promoting financial inclusion.

In recognition of this link, in 2009, as part of its commitment to improving access to financial services for the poor, the G-20 called upon the International Association of Deposit Insurers (IADI) along with other standard-setting bodies, to consider how they can further contribute to encouraging financial inclusion, consistent with their respective mandates".²

In response, during 2010, IADI established a Financial Inclusion and Innovation Subcommittee to engage with other entities, including the World Bank, CGAP, and the standard setting bodies. To date, IADI's subcommittee has been focused on 1) identifying issues that are raised for deposit insurance by the existence of unbanked populations; 2) exploring the implications for deposit insurance due to financial inclusion innovations through technology, new channels, or other means; and 3) conducting research on issues relevant to deposit insurance and financial inclusion, including a recent survey of deposit insurance systems to identify the range of practices related to deposit insurance and financial inclusion.

² See G-20 Communiqué, Meeting of Finance Ministers and Central Bank Governors, Busan, Republic of Korea, June 5, 2010.

3. FINANCIAL INCLUSION ISSUES OF INTEREST TO DEPOSIT INSURERS

Through the work of IADI's subcommittee, a number of financial inclusion issues of interest to deposit insurers have emerged that are being considered.

First, with respect to financial stability, an important consideration for deposit insurers (as well as other regulatory authorities) is the need to strike the right balance between controlling risks and encouraging innovation in the promotion of financial inclusion. Regulators and deposit insurers need to ensure that the institutional framework and regulatory oversight supporting the expansion of financial inclusion promotes and does not undermine financial stability. A deposit insurance system is most effective if a number of external elements or preconditions are in place, including a sound banking system with strong prudential regulation and supervision and a supportive legal framework.

Second, a number of important issues and questions are beginning to arise with the introduction and growth of new products and channels of service delivery that lie outside the scope of the traditional deposit insurance system, including:

- ❖ Whether membership in the deposit insurance system is or should be open to new types of providers and under what terms and conditions;
- ❖ The level and scope of coverage protection and whether it includes or extends to innovations such as e-money and/or depositors with the smallest deposit denominations and if so, under what terms and conditions;
- ❖ The deposit insurance funding systems employed, whether they extend to new providers and under what terms and conditions;
- ❖ The need for adequate consumer protections and public awareness of the availability and/or limitations of deposit insurance, particularly among small saver households that may be the target of financial inclusion initiatives and innovations; and
- ❖ The potential impact of financial inclusion initiatives and innovations on the risk exposure faced by deposit insurance systems, including consideration of emerging issues such as e-money.

IADI recently conducted a survey of deposit insurers to collect data on the range of practices of deposit insurers related to financial inclusion issues. The survey was administered from June – August 2011 and sent to over 100 deposit insurers. It asked a number of questions on a variety of related topics, including: whether the deposit insurers mandate relates to financial inclusion; observed trends in microfinance activity; and deposit insurer response to microfinance activities, including membership, coverage, public awareness, funding, and resolution. Analysis of the survey results is underway and the subcommittee hopes to share the complete survey results during the coming year.