FINANCIAL FLAGSHIP

FINANCIAL INCLUSION IN THE MIDDLE EAST AND NORTH AFRICA:

ANALYSIS AND ROADMAP RECOMMENDATIONS

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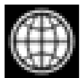

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1 Overview

Financial Inclusion is critical for the competitiveness of the Middle East and North Africa (MENA) region, for employment creation, and for raising incomes and reducing poverty. Financial inclusion is through access to financial services such as credit, bank accounts, deposits, payments services, insurance, and pensions. Firms need access to financial services to be able to invest, innovate, take advantage of market opportunities, manage cash flow and costs, and reduce risks. Microenterprises constitute the vast majority of enterprises in MENA and are a significant employer (92.5 percent of enterprises in the case of Egypt, and 63.6 percent share of private employment[1]). Individuals and households benefit from financial inclusion through a safe place to save, safer and cheaper access to remittances and other payments, loans or insurance payments to cover health or education expenses, and pensions for old age. High levels of financial exclusion hinder efforts to bring enterprises into the formal sector, and to increase investment and trade.

The G20 leaders committed to 'improving access to financial services for the poor' at the Pittsburgh summit in September 2009, and set-up a Financial Inclusion Experts Group with World Bank Group support. The G20 Leadership Summit in Toronto in June 2010 endorsed the "Principles for Innovative Financial Inclusion" that the Group developed. The UN committee on building inclusive financial sectors urged central banks and governments in 2006 to add the goal of universal financial inclusion to the traditional goals of prudential regulation and financial system stability. Universal access to finance has been adopted as a goal by India, Pakistan, South Africa, Mexico, Brazil, Colombia, Malaysia and a number of European countries.

While most MENA countries have taken steps to improve financial inclusion, there has not yet been a comprehensive high level commitment to financial inclusion across much of the region. Financial inclusion is a policy focus for several MENA countries, although it is not yet a priority objective alongside stability for MENA financial regulators and ministries of finance. Five MENA countries now have a financial inclusion strategy, and with three of these adopted since 2006 this seems to be a growing trend for region.

The enabling environment for financial inclusion in MENA has improved in the past two years, but is still weak overall. Deficiencies in financial infrastructure and regulatory frameworks make expanding access to finance costly and risky for banks. Lenders have to rely on collateral that is expensive to register and may not be readily enforceable, and on outdated credit assessment and risk management techniques. Credit information is improving in quality and availability throughout MENA, as credit registries are improved and credit bureaus established, but most microfinance institutions (MFIs) do not yet report to or have access to them. Interest rate caps on micro loans act as a disincentive for banks and investors, and limit

[1] CAPMAS, 2006

their growth. Investment in microfinance providers is constrained by the predominance of an NGO or association model, and by a lack or regulatory and supervisory clarity. Borrowers face higher pricing and many otherwise creditworthy individuals are excluded from access to finance.

The paper provides an assessment of the state of financial inclusion in the MENA region, and identifies constraints, opportunities, and priorities for significantly improving access to finance. The paper first provides an assessment and overview of financial inclusion in the MENA region, including the structure, performance and characteristics of the microfinance sector. The framework for financial inclusion is the focus of the next section, covering regulation and supervision, financial infrastructure, and government policies and programs.

Recommendations for improving Financial Inclusion in the MENA region are outlined in the final section. The priority recommendations are firstly to agree a Financial Inclusion Strategy that is underpinned by improved data, that has both public and private sector commitment, and that scales up financial access on a large scale, principally through bank accounts. Secondly, the paper recommends that regulators should provide a legal and supervisory framework that enables access to finance to be expanded primarily through banks, but with regulatory space for the use of agents, mobile phone technology, and for a finance company model for microcredit and leasing. The paper advocates removing interest rate caps on microloans, and instead strengthening consumer protection and supervisory capacity for microfinance, while stimulating competition between financial service providers. Thirdly, continued improvements to financial infrastructure are encouraged, particularly with regard to credit information and to secured transactions. Finally the paper highlights the need to enable growth in Islamic financial services to meet market demand.

2 Financial Inclusion in MENA

2.1 State of Financial Inclusion in MENA

Financial sector depth is not matched by Access. The MENA region has greater financial depth – as measured by private credit as a proportion of GDP – than all other regions except for OECD countries and East Asia. However, this is not reflected in similarly high levels of access to financial services. MENA lags several regions on the key indicators of bank deposits and loans accounts per population (see regional comparisons in table 1, and country comparisons in Annex A1.1). Just over one fifth (21.3 percent) of adults in MENA have a loan account with a bank, although this does not account for individuals that have more than one loan (the real figure is therefore likely to be lower). Access to bank deposits varies from 10.4 percent for Yemen and 19.2 percent for Syria, to the other end of the spectrum with more than one bank deposit account for each adult in Oman, Lebanon, UAE and Iran (Annex A1.1).[2]

[2] When Tunisia and Morocco's postal banks (and post office, in the case of Morocco) are included, deposit penetration figures improve significantly for those countries.

Table 1. Access Indicators by Region

Region	Banks Deposit Accounts per 1000 adults	Banks Loan Accounts per 1000 adults	Private Credit as % of GDP
Sub-Saharan Africa	315.5	87.5	23.7
South Asia	653.8	54.2	43.9
Middle East & North Africa	**744.0**	**213.3**	**50.6**
Europe & Central Asia	1,395.4	325.2	45.8
East Asia & Pacific	1,116.9	343.9	58.4
Latin America & Caribbean	1,227.5	366.8	44.7
High income: non OECD	1,865.0	851.5	83.4
High income: OECD	2,383.7	702.4	130.8

Source: CGAP and World Bank Financial Access 2010, International Financial Statistics

MENA countries tend to underperform on access to SME lending compared to financial sector depth and relative to countries with similar GDP levels, as illustrated in figures 1 and 2. MENA financial systems are bank-dominated (bank assets were 63.6 percent of GDP in 2008), and banks lend to a narrow set of clients, including the government and larger corporates. MENA countries also tend to have relatively low access to deposits compared to GDP per head.

Figure 1. Bank Loan Accounts per population against Financial Sector Depth and GDP per capita

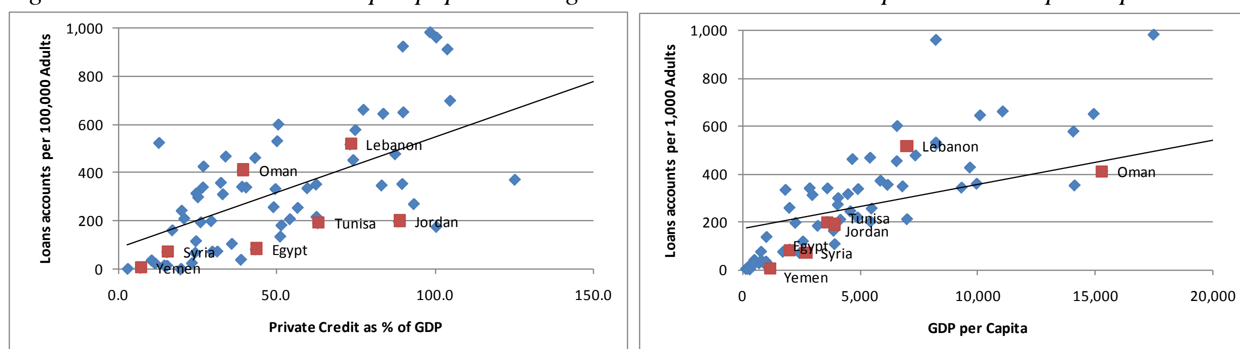
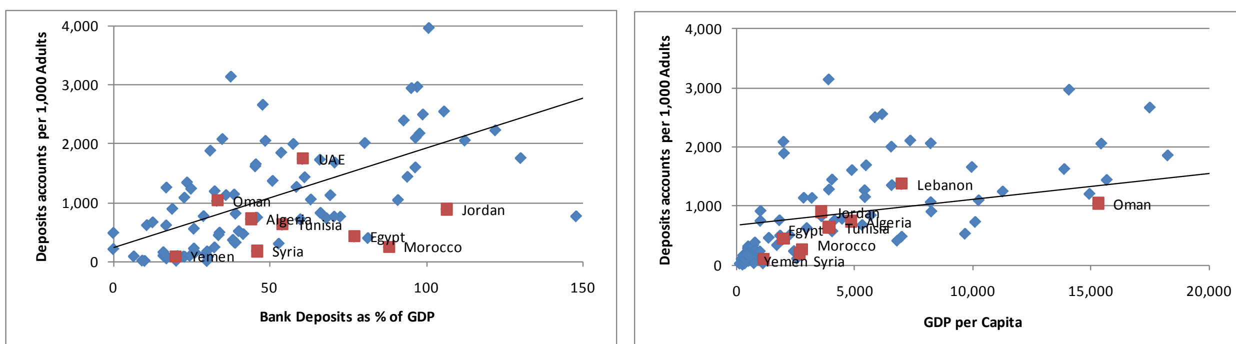


Figure 2. Bank Deposit Accounts per population against Financial Sector Depth and GDP per capita



Sources: CGAP and World Bank Financial Access 2010, International Financial Statistics, World Development Indicators. Iran data for 2008, all other data 2009.

Industry Structure

Financial inclusion in the MENA region is characterized by NGO-dominated microcredit sectors, **postal networks and state banks.** A few countries have introduced legislation that allows for other legal forms of microfinance provider, such as finance companies or banks, but as yet there are few microfinance institutions that are legally allowed to offer (voluntary) deposit services in MENA. Savings and loan cooperatives are not a major source of financial services in much of the MENA region. Table A1.3 (Annex 1) sets out a typology of microfinance providers presented in table form. 'Industry' is defined here as the set of providers of financial services to low income and microenterprise clients.

Banks and Financial Inclusion

Direct commercial bank involvement in microfinance in the MENA region is very limited. Banks prefer to provide wholesale financing through specialized microcredit providers. Bank-microcredit provider linkages build on the relative strengths of both types of entity – banks are able to raise funds from deposits and from the market and often have excess funds looking for returns, while MFIs are closer to clients, have tailored lending methodologies and delivery mechanisms, and lack funds. One of the big three Lebanese MFIs, Ameen, provides financial services in partnership with four Lebanese banks. Moroccan banks have set-up microcredit associations or foundations, rather than provide microloans directly. In Egypt two private sector banks offer microcredit in cooperation with microfinance service companies.

State banks are significant providers of financial services for low income people and microenterprises in some MENA countries. In Algeria, for example, the top 3 providers of loans to micro and small enterprises are public banks, with private banks and NGOs (associations) far behind, although the market share for private banks was growing (IFC survey, 2006). While in Syria, half of MSEs interviewed for the IFC (2008) used banking services from the large public bank, Commercial Bank of Syria. For loans to MSEs, public banks were also the leading providers – Real Estate Bank, Popular Credit Bank, and Commercial Bank of Syria.

State banks hold a significant proportion of financial service outlets in several MENA countries, including Syria, Algeria, Tunisia, Egypt and Iraq. The Principal Bank for Development and Agricultural Credit (PDBAC) is the state agricultural bank in Egypt, and has more than 1200 branches and 23,000 employees throughout the country outside of Cairo, providing deposit services; payments services; foreign currency services and passbooks, machinery and equipment loans and lending for agriculture and other food production enterprises. In Iraq over two thirds (69 percent) of the bank branch network is owned by the two large state banks, Rafidain and Rasheed.

Microfinance banks, or specialized microfinance institutions, are an alternative model where regulations allow. Instead of relying on banks for deposits and commercial borrowing, microfinance banks can intermediate their own funds. AGFUND and the Aga Khan Agency for Microfinance are committed to establishing microfinance 'banks' as specialized financial institutions that provide a broad range of financial services to low income people and microenterprises, on a sustainable basis. AGFUND has set-up MFIs in Jordan, Egypt, Bahrain, Syria and Yemen. For example, Al Amal microfinance bank was established under the Yemen microfinance law, and offers deposit and lending services to low income clients, including micro and small enterprises. Al Amal started operations in 2008, and now has nine branches, 12,000 active clients (half of whom are savers). A money exchange company in Yemen has also reportedly converted to a microfinance bank, Al Kurami. The Aga Khan Foundation has set-up a deposit-taking microfinance institution in Syria, which has some characteristics of a microfinance bank microfinance bank, as a Social Financial Banking Institution. Under Syria's General Microfinance Decree such an institution is allowed to provide microlending, deposit-taking, and micro insurance.

Microcredit in MENA

Microcredit[3] is still limited in scale in much of the region. The market coverage ratio for specialized microfinance providers is only half (1.78 percent) the proportion of the adult population as is the case for South Asia or Latin America.[4] As indicated in Table 2, the number of active borrowers compared to working age adults is much smaller than all regions except sub-Saharan Africa, while microcredit loan portfolios represent a significantly smaller proportion of total credit[5] than any other region.

Table 2. Microfinance Scale by Region

	MFI Providers	Number of active borrowers	Active Borrowers/ Working age population (%)	Gross Loan Portfolio (GLP)	GLP/ Total Credit
MENA		**2,807,116**	**1.99**	**1,505,414,132**	**0.47**
East Asia & Pacific	160	11,294,660	4.74	5,195,228,561	6.12
Europe & Central Asia	263	2,603,513	4.11	9,375,908,169	5.37
Latin America & Caribbean	327	12,781,340	4.93	15,334,944,785	7.14
South Asia	148	39,274,147	5.90	4,293,510,584	4.72
Sub-Saharan Africa	208	6,732,155	1.48	3,162,740,041	4.71

Source: Microfinance Information Exchange Database and Sanabel. Data for MENA is for 2009, other regions 2008.

[3] Defined by the World Bank and CGAP as having an average outstanding loan size less than three times GDP per capita.
[4] Data for Microfinance Institutions that report to the Microfinance International Exchange.
[5] Domestic private credit to the real sector by banks.

There were 2.81 million microcredit borrowers at the end of 2008, with a total loan portfolio of US$1.5 billion. Microcredit is concentrated in two countries: in 2009 47 percent of the region's microcredit borrowers were in Egypt and 33 percent in Morocco (the order was reversed from 2008, when Egypt had 40 percent and Morocco 44 percent).[6] In terms of clients per population and microcredit portfolio as a proportion of total bank lending to the private sector, Morocco still has the highest rates of microcredit access in the region, although this should be viewed in the context of Morocco's low level of access to bank loans. Morocco also stands out in terms of MFI branch networks, comprising 83 percent of the region's reported total. (MIX, CGAP, Sanabel, 2010) Jordan has the highest microcredit coverage of its poor population in the region. Tunisia and West Bank & Gaza have the only other microcredit sectors of any notable size in the region, although microcredit is growing in scale in Yemen, Iraq, and Syria.

Table 3. Microcredit Outreach by Selected MENA Countries

	MFI Providers	Number of active borrowers	Percent of Women Borrowers	Gross loan portfolio	Active Borrowers/ Working age population (%)	Number of clients/ Number of poor (%)	GLP/ Total Credit
Egypt	14	868,315	55.7	165,018,626	1.69	5.8	0.24
Iraq	4	27,708	14.7	16,122,827	0.16		0.45
Jordan	7	134,037	84.1	121,578,626	3.7	65.6	0.68
Lebanon	3	23,678	32.8	20,584,560	0.84		0.1
Morocco	9	1,241,957	46.3	695,647,381	5.96	28.1	1.08
WB/G	8	34,265	43.2	79,727,913	1.68		
Syria	2	22,149	31.4	15,682,015	0.18	7.2	0.04
Tunisia	1	94,959	76.7	33,999,508	1.32		0.14
Yemen	6	24,976	95.8	3,241,486	0.2	0.2	0.16

Sources: MIX database, WDI, IFS 2008 data. 'GLP': gross (microcredit) loan portfolio. Total credit: Domestic private credit to the real sector by banks.

Microcredit is concentrated in a relatively small number of leading institutions. The top 5 MFIs in MENA represent 43 percent of total outreach, and 3 of these are from Morocco (Annex A2.4 has a country breakdown by borrowers and by loan portfolio). 70 percent of microfinance institution (MFI) branches are in Morocco. Microcredit is not well developed in the Gulf Cooperation Council (GCC) countries, where only Bahrain and Saudi Arabia have microfinance institutions that report to the regional microfinance network (Sanabel).

After years of overall slow growth, the rate of growth of the microcredit sector in MENA finally started to catch up with global growth rates between 2006 and 2008. Worldwide growth rates recorded by the Micro Banking Bulletin[7] were 21 percent for borrowers and 35

[6] Sanabel, 2010. These statistics do not include Mauritania and Sudan, which are included in Sanabel regional totals.
[7] The Bulletin has a database of 600 microfinance institutions from 84 countries, including most of the leading institutions by size and performance as recorded by the Microfinance Information Exchange.

percent for portfolio, whereas for the MENA region they were 19 percent and 30 percent respectively. Outreach contracted in 2009 by 3 percent (78,785 borrowers), although total loan portfolio increased marginally, driven primarily by a decline in the size of the Moroccan microfinance sector. This was a consequence of reconsolidation and losses following the microfinance over-indebtedness crisis in Morocco, which is explored in more detail in Annex 5. The total number of microcredit borrowers in Morocco more than doubled from 2005 to 2007, but then fell by almost a third from 2007 to 2009. Growth rates for individual Arab countries varied, with the highest rates in 2009 recorded in Iraq (45 percent) and Lebanon (37 percent). (see Annex tables A2.1, A2.2 for growth rates by country).

Microcredit in MENA reaches relatively poor clients compared to other regions (except Asia), and a reasonably high proportion of women, at 63 percent of total microcredit borrowers (although only 31% employees of Sanabel member MFIs are female). The proportion of women microcredit clients ranges from as low as 18 percent in Iraq, where female workforce participation has declined since the most recent conflict, to as high as 81 percent in Yemen and 83 percent in Jordan where many MFIs target women as part of their mission. Table 4 compares 24 larger and better performing MFIs from across MENA with their counterparts globally, on outreach, gender, efficiency and portfolio quality.

Table 4. Comparative Outreach, Cost and Portfolio Quality Statistics by Region

	Outreach (Income)	Percent of Women clients	Operating Expense/Loan Portfolio	Portfolio at Risk (>30 days)
MENA	**15.8**	**65.4**	**21.4**	**2.4**
Africa	67.8	57.2	32.7	4.7
Asia	17.8	93.8	17.2	1.5
ECA	68.3	43.1	15	2.0
LAC	25.5	59.6	22.3	4.2

Source: 2008 MFI Benchmarks MIX Micro Banking Bulletin. Median values. Outreach is average loan balance per borrower/GNI per capita.

Reported portfolio quality in MENA is generally good, with the exception of Morocco and West Bank/Gaza. Portfolio at risk (measured at 30 days, a relatively conservative measure typical of microfinance) has been broadly stable in recent years, and averaged 3.9 percent for MENA in 2009. (Sanabel 2010) This is despite the decline in the quality of the Moroccan microcredit portfolio. MFIs in MENA are relatively 'profitable', with a higher average return on assets than MFIs in other regions.[8] This is driven by low expenses, high efficiency levels, and initial (zero cost) donor funding. Financial revenues are also low, and this relative profitability does not seem to be a factor of high interest rates (which do not tend to be high by global standards). Annex A2.3 presents efficiency, profitability, and portfolio quality data by country.

[8] Microbanking Bulletin data. It should be noted that MFIs reporting to the Microbanking Bulletin, as to the Microfinance Information Exchange, do so on a voluntary basis. Stronger and larger MFIs are therefore more likely to provide data than small and poor performing MFIs.

Postal Networks

Postal savings banks and post offices continue to be the primary providers of savings and payment services for low income people in the region. There are 6 postal networks providing financial services in MENA, which were all state entities. Egypt Post is the largest provider of savings products to Egyptian micro entrepreneurs and lower income population, serving over 17 million clients through 3,700 outlets nationwide, including with savings, payments and domestic transfer services, although not with microcredit. The largest bank network, PBDAC (the state agricultural bank) has over 1200 branches and outlets, by comparison. While the numbers in Yemen are smaller, the Post and Postal Savings Corporation has 310 branches, which is more than the total number of branches of commercial banks. Tunisian MFIs and the postal service combined have 20 times more branches in rural areas than banks do. (CGAP and World Bank Financial Access 2009; M Khaled, pers. comm.)

Post office branch networks are in many cases among the most extensive delivery channels for financial services in MENA, as noted earlier. The Moroccan post office, for example, provided basic financial services (savings passbooks and checking accounts) to a large customer base (more than 2.5 million people). In recent years, it has successfully leveraged on the large postal network (1,762 branches in 2008) to attract a significant number of unbanked and rural customers (14 percent of the Moroccan population have postal accounts in 2008, up from 10 percent in 2005).

Financial Inclusion and the Global Financial Crisis

Loans to GDP declined in MENA in 2009 as a result of the crisis (with Tunisia a notable exception) for both loans and deposits, due to falls in commercial bank lending. Deposit volumes also fell, with some exceptions, while the number of deposit accounts continued to rise. This phenomenon of continued growth in access to deposits despite falls in overall deposits, was also a feature in other regions, except for those affected most severely by the global financial crisis (such as Eastern Europe and Central Asia), where both fell. (CGAP and World Bank Financial Access, 2010)

Microfinance in MENA was not directly affected by the global financial crisis though. Microfinance markets have not generally reached an equilibrium between demand and supply, as reflected in high unmet levels of demand for microfinance, and the apparent lack of sensitivity to high interest rates (although rates in the MENA region are typically lower than other regions). In most markets microfinance volumes are primarily a function of funding available to microfinance institutions, and of the capacity of MFIs to expand sustainably and manage risks. Funding levels for MFIs were maintained throughout the crisis, with the exception of falls in donor funding to microfinance in Egypt and Morocco that were due to non-crisis factors, so the

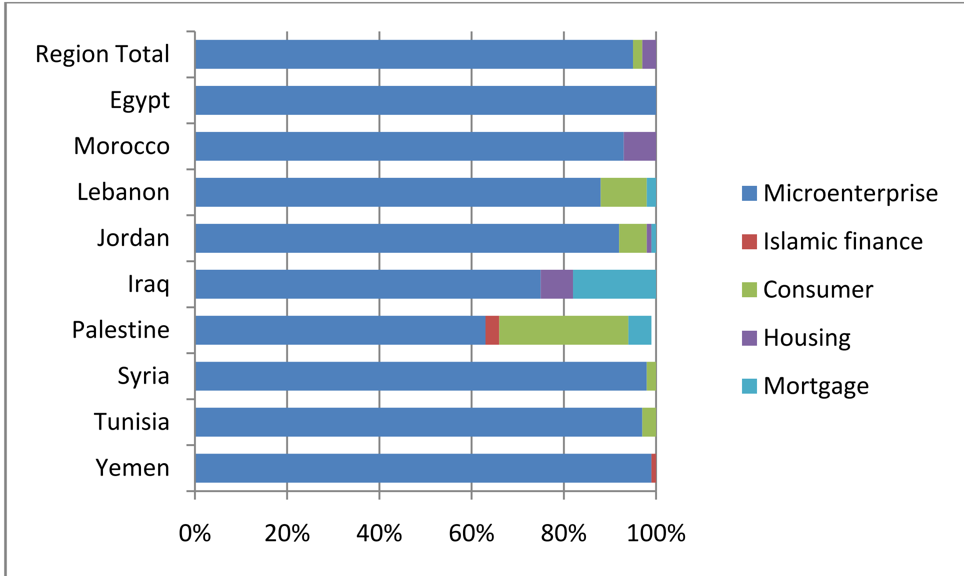
microfinance sector in MENA was fairly well insulated from the global financial crisis. Microcredit NGOs also did not have investment portfolios or direct exposure to complex financial instruments, depending primarily on donor funding and straightforward bank loans.

2.2 Financial Products for low income customers and microenterprises

Access to finance in MENA tends to be narrow, with most microfinance providers not able to offer transaction accounts, payments, housing loans, sight deposits, term deposits, or insurance products. Financial inclusion will continue to be constrained until regulatory reforms and financial infrastructure improvements allow banks and regulated microfinance providers to expand outreach to low income customers and microenterprises at a lower cost and risk.

The vast majority (94 percent) of microloans made by MENA MFIs are intended for microenterprise activities (Sanabel 2010), although given that money is fungible this is a questionable distinction. The majority of microloans are also made through solidarity groups[9] (65 percent of all microfinance borrowers). While most MFIs in MENA are credit-only, and not able to offer a broader range of financial services, there has still been some product innovation, particularly in more mature markets such as Jordan, Yemen, Egypt. Loan products are now offered for housing, agriculture and consumption, as well as for the microenterprise activities that are the primary focus. MFIs in Egypt, Jordan and Lebanon also offer credit life insurance products, as agents or contact points for insurance companies. A third of MFIs also offer training and consulting services. Less than a fifth offer fund transfer services, given restrictions on the range of services. Microleasing is virtually absent.

Figure 3. Microfinance Products offered by MENA MFIs



Source: Sanabel 2010 (2008 data)

[9] Groups of borrowers that co-guarantee each other.

Microsavings are offered on a very limited scale in the region, and are only found in West Bank & Gaza, Syria, and Yemen and only offered by a few institutions. Al Amal Microfinance 'Bank' in Yemen, for example, offers sight deposits, child savings accounts, and also time deposits, as well as Shariah-compliant insurance on loans (Takaful). Micro insurance for health and education (beyond standard death and disability protection offered by many MFIs on microloans) is being introduced by leading microfinance NGOs in Egypt and service companies, as service agents for insurance companies (Allianz and Alico).

Trade credit (credit provided by other firms) is used by many micro and small enterprises in the MENA region. A significant proportion of micro and small enterprises interviewed for IFC microfinance country reports in 2006-2008 reported accessing supplier credit, and most paid little or no interest charges. Half of micro and small enterprises surveyed for the IFC in Yemen (205 out of 405), 39.5 percent of those surveyed by Syria, 40.7 percent of those interviewed in Algeria, and 40.7 percent of those in Lebanon, used some form of supplier credit to acquire supplies, whether as an advance with balance upon receipt, or making a delayed cash payment after delivery.[10]

Islamic financing instruments comprise only a small fraction of microfinance supply. In Syria for example they comprised only 3 percent of outstanding microfinance loans in 2006. Providers of Islamic microfinance also tend to be small in size. Indonesia, Bangladesh, and Afghanistan – none of which are in MENA – account for 80 percent of the global outreach of Islamic microfinance. Leading countries for Islamic microfinance in MENA include Lebanon and Yemen (CGAP, 2008). Yet IFC-commissioned market studies in the MENA region suggest a strong demand for Islamic microfinance products. Between 20 and 60 percent of those interviewed (microenterprises, low income individuals) indicated a preference for Shariah-compliant products. For some the lack of Shariah-compliant products is an absolute constraint to financial access, while for others this is a preference and they continue to use conventional financial services in the absence of competitive Islamic ones.

The range of Islamic finance products offered is narrow - over 70 percent of the Islamic finance products offered are *murabaha* (cost plus), which is a lending product typically used for working capital. Most MFIs in Yemen offer a *murabaha* loan product, for example. However, there are some signs that this limited selection may increase: in Egypt, Bank Misr plans to introduce Islamic microfinance activities to its 33 Islamic branches, and also develop a *mudaraba* (profit sharing agreement) product in addition to the *murabaha* product; in Yemen Tadhamon Islamic Bank opened a MSE division in late 2006; and in the UAE Noor Islamic Bank and Emirates Post Holding Group announced plans to establish a company to offer Sharia-compliant financial services to low income clients.

[10] Sources: IFC, 2007, Assessment of MSE Financial Needs in Yemen; IFC, 2006, Access to Finance Study in Algeria; IFC, 2008, Lebanon: A Diagnostic Study on the Demand for Financial Services by Micro and Small Entrepreneurs.

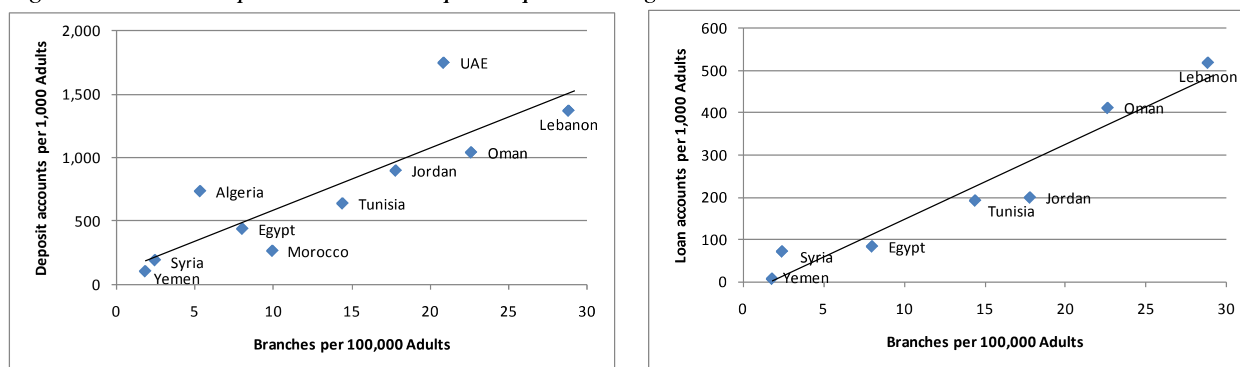
Constraints to Islamic microfinance are mostly related to i) the capacity of microfinance providers to design authorized Islamic finance products that meet the needs of clients, and ii) the need to keep costs low for micro-level transactions. Islamic microfinance providers globally are still in the process of identifying innovations and adaptations to Islamic finance that lower costs and enable them to offer sufficiently attractive pricing to clients. Islamic microfinance can be more reliant on collateral to secure loans, rather than on cash flow-based financing techniques, and as such is more affected by weak collateral registration and enforcement regimes. There can also be a stronger tendency in Islamic jurisprudence to give borrowers more time and opportunity to repay, rather than executing collateral.

2.3 Delivery mechanisms for financial services

Bank branch networks are correlated with access to loans and deposit accounts.

As shown in Figures 4 and 5, the number of deposit and loan accounts relative to the population in MENA is closely linked to the size of branch networks.[11] The number of deposit accounts per population does not seem positively related to the proportion of the branch network held by state banks (Figure 7) though, despite a widespread assumption that state banks have deeper penetration in areas not covered by private banks and therefore can contribute to overall gains in access.

Figures 4 and 5. Deposits and Loans per Population against Branch Networks



[11] As shown in Annex 1.4, the relationship between number of deposits and branches holds even after controlling for per capita income, although it should be noted that the regression results are only suggestive, given the very small sample, and the endogeneity of the branch variables.

Figure 6. Deposits/population vs. Per Capita Income.

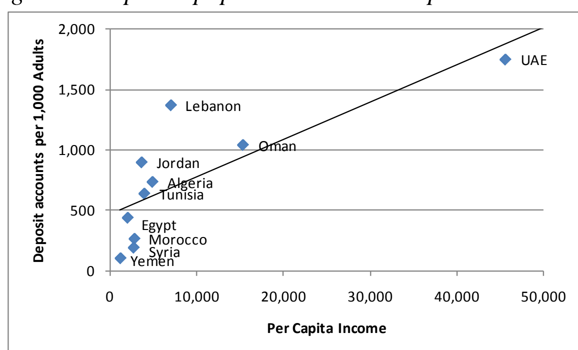
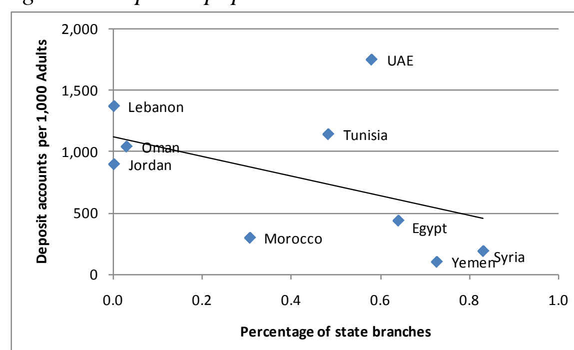


Figure 7. Deposits/population vs. State Bank Networks



Source: CGAP and World Bank Financial Access 2010

While branches facilitate a range of financial services, and can enable a personalized service to clients, 'branchless' outlets such as ATMs and point-of-sale devices also be effective delivery mechanisms not only for withdrawals but also for payments and deposits, at a considerably lower cost than branches. While MENA is typically at or below the averages for ATM access for other developing regions, access through point-of sale (POS) devices is relatively more widespread in MENA. Population densities, income levels, telecommunications networks, banking sector development, and Government policy all influence the density of touch points in the region, as elsewhere. ATM networks in the GCC countries are relatively dense and well developed (tables A3.1 and A3.2 have more ATM and POS detail).

The MENA region reported the second highest increase (24 percent) in ATM networks in 2009 globally, after South Asia (64 percent). MENA's relative density of branches, ATMs and points of sale devices are illustrated in table 5. Iran, UAE, Oman and Lebanon have the highest levels of branch density per population, while Lebanon has (by far) the highest density per geographic area (Annex 1.2).

Table 5. Physical Access by Region

Region	Branches per 100,000 adults	Branches per 1,000 km2	ATMs per 100,000 adults	ATMs per 1,000 km2	POSs per 100,000 adults	POSs per 1,000 km2
SSA	5.1	5.8	11.7	12	5,695.1	1,801.1
SA	6.5	18.1	5.2	11.2	39.6	80.8
EAP	11.8	6.5	25.3	21.3	352.3	185.2
MENA	**14.3**	**11.8**	**31.1**	**21.4**	**641.3**	**774.7**
GCC	17.1	7.6	63.3	28.3	739.3	627.9
non GCC	13.1	13.7	16.8	18.4	608.6	823.6
LAC	15.8	15	44.1	32.6	881.6	871.2
HI: non OECD	19.8	254.4	78.9	511	1,833.2	22,227.1
ECA	21.4	13.8	43.6	24.3	667.6	405.5
HI: OECD	33.4	35.9	103.2	101.5	2,293.9	2,243.3

Source: CGAP and World Bank Financial Access 2010

Mobile Banking

Mobile banking has the potential to be transformational because it: i) uses existing mobile communications infrastructure which already reaches unbanked people, ii) may be driven by new players, such as telecommunications companies, with different target markets from traditional banks, iii) may harness the power of new distribution networks for cash transactions, such as airtime merchants, beyond the conventional merchant POS or ATM networks of banks, and iv) may be cheaper than conventional banking, if the offering is competitive. (Porteous, 2006) CGAP research comparing service provides between banks and branchless banking service providers indicates that mobile banking services can be up to 50 percent cheaper (see Annex 3.4 for cost comparisons).

Mobile banking[12] has been used primarily for payments and transactions so far, and not for loans or savings, although pilots are underway to develop credit and deposit products through mobile phones. Using a mobile phone for more complex transactions than payments and transfers requires a different pricing structure (customers are unlikely to want to pay transfer-level fees to make a loan repayment), and also implies that regulators need to understand any risks that are involved, and to adapt supervisory practices and legal frameworks as appropriate. The functionality of using a small keyboard and screen can also be seen as less convenient than using a branch or computer, even if mobile phones are much more easily accessible.

High potential countries for mobile phone banking in MENA include Egypt, Yemen and Morocco. The table below suggests a characterization of countries in terms of potential to benefit from mobile phone banking, and to support viable mobile phone financial products. Market potential is influenced by the number of unbanked potential customers, wireless penetration rates, and relatively conducive regulatory frameworks that allow private sector activity and innovation. Egypt has the largest population in the Arab world, with very low financial access, but 65 percent of the population (55.4 million) already has a mobile phone. (Michaels, 2010) Mobile and agent-based financial services could also transform access to finance in Yemen. Nearly 70 percent of the population is living in rural areas which are without basic infrastructure. There are close to 8 million mobile phone subscribers in Yemen and less than 1 million bank accounts (CGAP, 2010). While West Bank and Gaza does not have a large population, the difficulties of moving cash in and out of Gaza may provide a business case for the introduction of mobile phone banking. In Iraq, mobile phone banking may help commercial banks overcome constraints of limited branch networks (state banks control the majority of branches) and uncertain security of movement.

[12] Mobile phone payments are financial transactions undertaken using a mobile device such as a cellular phone. Mobile banking includes mobile payments but involves access by mobile device to the broader range of banking services, such as account-based savings or transactions products offered by banks.

Table 6. Which MENA Countries have the Most Potential for Mobile Banking?

LOW POTENTIAL	MEDIUM POTENTIAL	HIGH POTENTIAL
Low rural or unbanked population Low mobile penetration Uncertain regulatory regimes High state ownership of bank and/or telecom assets (can limit innovation)	High state ownership and control of banking and telecoms sectors Uncertain regulatory and business environments	High rural populations Low levels of banked people High mobile penetration Increasingly conducive regulatory regimes
Djibouti, Libya, Saudi Arabia, Syria	Algeria, Iraq	Egypt, Jordan, Morocco, Yemen, Tunisia

Source: Michaels, 2010. Data presented in Annex 3.3.

Mobile phone banking in MENA has not yet taken off, with few mobile phone-based financial services yet launched. Regulators in high potential markets such as Egypt and Morocco are starting to ease regulatory constraints and allow banks to link with MNOs to launch financial services through mobile phones. An emerging example of the use of technology in the MENA region is the use of electronic wallets (e-wallets), linked to cards and mobile phones, that can be used as a form of payment, to withdraw cash, to pay bills, recharge airtime, make deposits, and send or receive money transfers. Emerging mobile phone banking examples in MENA are outlined in the box below.

Box 1. Mobile Phone Banking Products new to MENA

Mobicash is now offered in Morocco by Maroc Telecom with Attijariwafa Bank and Banque Central Populaire. In late 2009, Maroc Telecom (MT), Morocco's largest mobile operator with 16 million subscribers and 61 per cent market share , along with Attijariwafa Bank and Banque Central Populaire, started implementation of Mobicash, Morocco's first mobile payments platform. Over time, this service could introduce access to deposits, withdrawals, bill payments, money transfer and mobile banking, as well as international remittances.

MTN Mobile Money in Yemen is offered by MTN with the Cooperative Agricultural Credit (CAC) Bank. CAC is one of the largest state-owned banks in Yemen, and already has a large portion of the bill payments business. It also has its own POS acquiring network, the largest in the country. The Mobile Money product is a mobile wallet, with customer funds kept in a pooled account at CAC. The service will be accessed at CAC's 85 branches, 92 ATMs and 1,000 POS systems.

M-dinar was launched in February 2010 by Banque International Arabe de Tunisie (BIAT), along with MNO Tunisiana and microfinance institution ENDA, and is a mobile wallet application. Users need to open a BIAT account, and the service will allow for person to person transfers, top-up, loan payment services for MFI clients, and the ability to view account balances, transactions history and request cash from other users. ENDA will also trial mandatory loan repayments via M-dinar to its 150,000 clients.

In Iraq, AsiaCell announced in February 2010 that it would form a strategic partnership with a consortium of private banks, AMWAL, to provide money transfer and other services through mobile phones in Iraq.

Sources: Akhtar & Pearce, 2010; Michaels, 2010; CGAP, 2010.

Agents

Retailers, mobile phone airtime providers, and other non-financial outlets, offer huge potential for expansion of access to finance, if they can be used as 'agents' for financial service delivery. Using banking agents and electronic payments to pay utility bills takes less time than traveling to and queuing in a range of utility offices, thereby bringing very tangible benefits. Similarly, collecting a pension, remittance receipt, and welfare or salary payment is a strong driver for opening accounts. Agents – such as retail stores or airtime sellers – are also key to the viability of mobile banking, as they are able to handle cash transactions. In Brazil, bill payments and the payments of government benefits to individuals comprised 78 percent of the 1.53 billion transactions conducted at the country's more than 95,000 agents in 2006. (CGAP, 2008). Only 10 percent of MENA countries reported allowing banks to use agents in 2008 however, which was well below other regions, for example 60 percent in ECA, 50 percent in high income countries, 41 percent in Latin America and the Caribbean, and 29 percent in sub-Saharan Africa. In 2009 this improved though, with 3 countries reporting reforms to enable the use of agents. (CGAP and World Bank Financial Access 2009, 2010) The use of agents as a delivery mechanism is not yet widespread in the region however.

Opening up the market for agents could lead to a 10 fold increase in access points for financial services in Yemen, according to a recent CGAP market assessment. If small stores could become agents for financial service providers, then MTN and the Cooperative and Agricultural Credit (CAC) Bank, could expand their reach significantly. CAC is already processing bill payments and money transfers through 150 'agent' outlets made up of kiosks and store locations. (CGAP, 2010) If a common switch was also introduced, then a service by any one bank could be accessed through the entire POS and ATM network of the country.

3 Government Policies and Programs, Regulation and Supervision

Deficient financial infrastructure and inappropriate regulatory and supervisory frameworks have hindered financial inclusion in the MENA region, and have resulted in a financial sector that only serves a fraction of otherwise unmet financial service needs. This section explores the policy, regulatory and supervisory framework for financial inclusion in MENA, including financial infrastructure.

3.1 Regulation and Supervision

Financial Inclusion constrained by Regulatory Framework

Improved access to finance in MENA is constrained by inappropriate regulations, a lack of specialist supervisory capacity, and inadequate institutional models. The majority of MFIs in the region are registered as NGOs, and are restricted from offering deposits in addition to loans (by regulators or by their own capacity limitations). Many commercial and social investors

are reluctant to finance NGOs or associations (or will only do so with short-term debt), or are not able to invest in shares. Banks face interest rate caps in several countries that make microloans unattractive, and are in many cases restricted from using agents to extend financial services. Identity ('know your customer') requirements are also relatively high in MENA, and can include requirements that are not appropriate for low income and semi-formal customers, adding a further set of costs and disincentives to banks to extend access. Technologies to improve access, such as point of sale devices and cellphone banking, are held back in MENA by restrictions on the role of agents in financial service delivery, and by extensive customer ID requirements. MENA countries have the highest requirements in terms of documents (government ID, proof of address, legal status, proof of employment, etc) needed to open a deposit account.

Microfinance legislation has been introduced, albeit on a limited scale, in two waves in the region, with the first more than a decade ago in Morocco and Tunisia, and the second more recently in countries further east, such as Egypt, Syria, and Yemen. Government reform priorities have been to ease financing constraints for enterprises, expand microsavings services, attract commercial financing into microfinance, and improve the transparency and strength of microfinance institutions. Morocco and Tunisia first introduced microcredit–specific laws in 1999 with the aim of establishing a new microcredit sector serving low income population segments. Several countries have also introduced institutional and legal reforms to extend access through post offices and state banks. Table 7 illustrates the degree to which enabling regulatory frameworks have been introduced for financial inclusion in the MENA region.

Table 7. Enabling Frameworks for Financial Inclusion

Country	MF Specific Legislation	Investor-friendly MFI legal form?	Deposit-taking allowed?		
			By MFIs	By Post Office/ Post Bank	By Credit Unions
Algeria	-	-	-	-	Yes
Egypt	Yes	Yes	-	Yes	-
Iraq	-	-	-	-	-
Jordan	-	Yes	-	Yes	-
Lebanon	-	Yes	-	-	-
Morocco	Yes	-	-	Yes	-
Syria	Yes	Yes	Yes	-	-
Tunisia	Yes	-	-	Yes	-
West Bank & Gaza	Pending	-	-	-	Yes
Yemen	Yes	Yes	Yes	Yes	-

Sources: M Khaled 2010; Sanabel/CGAP/MIX, 2010

Egypt has introduced regulations for non deposit-taking MFIs, while Syria and Yemen have introduced laws permitting the establishment of deposit–taking MFIs, and Jordan allowed MFIs to register as not-for-profit companies. Egypt has approved a new Non-Bank Financial Institutions Licensing and Regulatory Bill, to be supervised by the Egyptian Financial Services Authority (EFSA), which will set the regulatory framework for microfinance, leasing,

and factoring institutions, as well as standards in accounting, transparency and corporate governance, and lay the foundation for a new category of non-bank microcredit companies. Allowing the creation of supervised microfinance companies can unlock potential investment, while also raising standards for transparency and corporate governance for microfinance institutions. This regulatory reform does not allow for deposit services to low income persons, although Egypt Post does provide fairly extensive access to microsavings services.

Social Financial Banking Institutions (SFBIs) have been allowed in Syria since 2007, with a minimum capital requirement of approximately USD 5 million. SFBIs are allowed to provide various financial services, including microlending, deposit-taking and micro insurance. In Yemen the 2009 Microfinance Banks Law allows these 'banks' to mobilize voluntary microsavings. A microfinance supervisory unit is being established. However, in Syria and Yemen only a few institutions have applied for licenses, which may be related to what are reported to be lengthy registration and licensing procedures as well as lack of clear prudential guidelines. (Khaled, 2010) The business case of such deposit-taking MFIs is also unclear, as they would be competing with well-established postal savings networks. Other countries considering microfinance legislation to allow deposit-taking institutions include Iraq and Morocco.

In an increasing number of MENA countries a financial sector regulatory authority, such as a central bank or non-bank regulator, has supervisory responsibility for microfinance providers. However, in a number of countries there is no clear supervisory responsibility or framework, or the supervisor is a non-financial agency such as a Ministry of Social Affairs or Planning (see Annex A2.6 for detail by country). This makes the development of a sustainable, transparent and efficient microfinance sector that is able to intermediate deposits or borrowing less likely, and dependence on declining or unpredictable donor funding may continue. When compared to developing countries, MENA has a higher proportion of non-regulated institutions and a higher proportion of MFIs that fall under a non-financial regulator (table 8).

Table 8: Microfinance Regulation and Supervision by Region

	MENA (%)	Developing Countries (%)	All (%)
Not regulated	50.0	37.9	47.7
Supervised only by a bank regulator	30.0	42.7	35.4
Supervised only by other regulator	20.0	7.8	7.7
Supervised by both	0.0	11.7	9.2
Number of countries	10	103	130

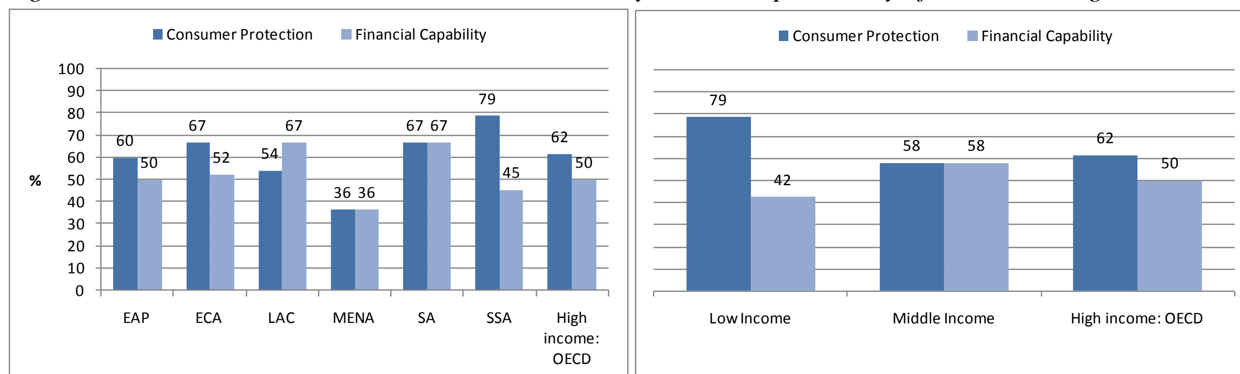
Source: M Khaled, CGAP, 2010

Interest Rate flexibility is constrained. Interest caps are in place in at least 6 MENA countries, whether or not they are actually enforced.[13] Most MENA countries use disclosure requirements (70 percent) rather than usury ceilings in practice, to try and ensure that interest rates are transparent and understood. Currently, most MFIs charge interest rates that are much higher than the interest rate caps, in order for micro-level products to be viable, and in so doing they run a risk of being challenged in court. A more transparent approach would be to remove interest rate caps and instead strengthen consumer protection against abusive practices such as excessive fees on overdrafts, miss-selling of financial products and lack of consumer redress.

Consumer Protection and Financial Inclusion

Consumer protection and financial literacy are increasing priorities worldwide, as financial inclusion increases, with almost two thirds of middle income countries assigning responsibility for these areas to the financial regulator. MENA lags other regions in terms of assigning responsibility for consumer protection or financial literacy to a financial regulator. However a majority of MENA countries introduced consumer protection reforms in 2009. Of 11 MENA countries that responded to the CGAP and World Bank Financial Access survey in 2010 survey, 7 had introduced consumer protection reforms, indicating that MENA is broadly in line with global trends in terms of increasing focus on consumer protection.

Figure 8. Consumer Protection and Financial Literacy under Responsibility of Financial Regulator



Source: CGAP and World Bank Financial Access 2010

Arab microfinance institutions have developed consumer protection and financial responsibility codes on a voluntary basis at a MENA regional level, and also in Jordan. MFI members of the regional microfinance network, Sanabel, signed a consumer protection and responsible finance document in 2008, committing themselves to standards of practice. Jordanian MFIs developed and signed a voluntary Code of Ethics covering disclosure and transparency, service standards, and ethical practices.

[13] To date, however, there have been no known legal challenges to interest rates in this region.

3.2 Financial infrastructure

Financial infrastructure underpins financial inclusion. Moral hazard and adverse selection are reduced as collateral frameworks and credit information systems are improved, and loans can be made - at a lower cost and risk – to clients that previously would have been excluded. Without effective secured transactions laws and judicial (or non-judicial) processes, ideally with unified collateral registries to facilitate lenders' use of collateral as a guarantee, micro entrepreneurs may not be able to leverage current assets into access to finance. Low income individuals and microenterprises also need access to low cost and safe payment mechanisms, whether for salaries, benefits, remittances, or for business transactions.

MENA has the lowest score on the Doing Business Legal Rights index of any region, however. As a result banks face higher costs of overcoming information asymmetries and higher levels of credit and default risk for micro lending, and have not yet directly entered the low income consumer or microenterprise market at any great scale. The Legal Rights index assesses the use of movable assets as collateral, the strength of creditor rights, and the availability of out of court enforcement mechanisms – all key areas for improvement for expanding financial inclusion. No MENA country scores above 4 out of 10 on this index. Banks therefore do not extend lending further into the micro and small enterprise sector. Microfinance providers are forced to rely on solidarity group lending methodologies or on collateral that is expensive to register and may not be readily enforceable, and on outdated credit assessment and risk management techniques. Low income customers and microenterprise clients face higher pricing and more paperwork and delays, and many otherwise creditworthy individuals and entrepreneurs are excluded from access to finance.

The majority of banks in the MENA region accept movable property as collateral. However, loans only secured with movable collateral are not widely used, due to the inability of banks to secure the right over the asset through a collateral registry and due to the difficulties in enforcing security interests in movable property. This is particularly acute for microloans where it may not make economic sense to execute collateral on a very small outstanding amount if the costs of doing so are relatively high. Movable property is usually accepted as a secondary type of collateral and usually taken as a complement to fixed assets (real estate property), which are also not well suited to microloans. Loans secured with assets such as receivables and inventory, are used even less often. None of the MENA countries have a modern law on secured transactions. Intangible movable property, such as accounts receivables, bank accounts and salaries, is only allowed in a few MENA countries. (de la Campa, 2010)

In most countries, MFIs have not been integrated into the formal credit information system, thus creating an information gap that could have direct consequences on the stability of the financial system. In some cases MFIs are prohibited by law from participating in the credit information system. In others, MFIs are reluctant to participate due to the high cost of the

system. The high value thresholds in some credit information systems also constitute a major challenge when compared to the low value of most microloans.

The Moroccan central bank and the Palestinian Monetary Authority have taken a regional lead in requiring microfinance institutions to also upload lending and borrower data and to verify current debts of potential clients into their credit information system. Arrangements to do so are under development in at least 5 MENA countries, but are not yet finalized, and ongoing delays threaten the quality and sustainability of microfinance sector growth, leaving an information gap that could result in similar microfinance crises. MFIs can lack awareness of the benefits of participating in national credit bureaus, and their borrower records and reporting systems may not yet meet the reporting requirements of a credit bureau.

Many Arab countries are undertaking payment system reforms, often supported by the Arab Payment Initiative (World Bank, Arab Monetary Fund, IMF). Countries are working to improve the legal framework, payment system oversight, and introduce real time gross settlement systems (RTGS), well-functioning automated clearing houses (ACH), and switching systems for connectivity between banks and card providers. The process in Egypt, as an example, is ongoing, with an RTGS and ACH established, and with full functionality being introduced in stages, for example to enable direct deposits, direct debits, mobile phone payments and extend financial inclusion.

Box 2. Egypt: Financial Infrastructure Improvements pave the way for G2P-led Financial Inclusion

Egypt is building on its improved payments systems infrastructure to move government payroll and pensions through debit cards, using the automated clearing house (ACH). As a result, 12 million monthly payments are expected to pass through the ACH within three years. Around 350,000 card-based accounts have already been opened under this new initiative, with eight banks participating. The government also plans to conduct a major portion of tax and customs collections through the ACH, and even shift government vendors' payments through the ACH, using government certified digital signatures and the treasury single account.

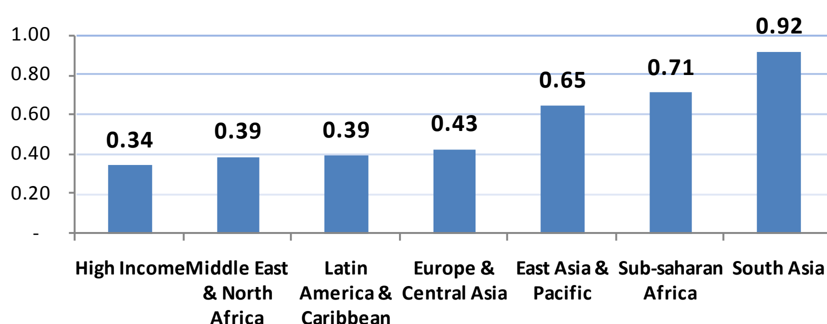
The government makes 30,000-40,000 procurement-related transactions daily, mostly through checks sent to microenterprises and SMEs (for example small tradespersons). These will increasingly instead be made through ATMs and banks accounts. The 'billers hub' that is currently used for bill payment to mobile phone providers, could also be extended to cover payments to government (thus making use of mobile phones), and payment of credit card bills using direct debit arrangements.

Further, a national inter-bank switch system for ATM, Electric Funds Transfer-Point of Sale and inter-bank mobile transactions has been established to support retail payments, and will be extended to cover the remaining four banks not yet included, and to handle local transactions in Egypt rather than abroad. Payment systems regulations would be issued to cover licensing of payment service providers and the oversight of payment services and systems.

3.3 Government Policy and Programs

Financial inclusion is not yet a priority for financial regulators in most MENA countries. Financial regulators in MENA have the second lowest degree of involvement in promoting financial inclusion, ahead only of high income countries where financial exclusion is at much lower levels (figure 9). Almost half of all the countries covered by the CGAP and World Bank Financial Access 2010 report (48 percent) have a strategy document for the promotion of financial inclusion, with 90 percent of those introduced within the last 6 years.

Figure 9. Index of Regulator's involvement in Financial Inclusion



Source: CGAP and World Bank Financial Access 2010

Individual MENA governments have introduced reforms and new initiatives to promote financial inclusion. 'Financially inclusive' bank accounts have been introduced by five MENA countries (Iran, Kuwait, Egypt, Morocco, Oman), two of those in 2009. Over a third of MENA regulators are trying to shift more government-to-person transfers through bank accounts, with five countries having made reforms in 2009 to accelerate this. Only three countries have introduced reforms to enable branchless banking through agent networks. Four out the eleven MENA countries reporting to the CGAP and World Bank Financial Access Survey (2010) reported official household or enterprise surveys that include a focus on access to finance. Tax incentive schemes to stimulate savings are not widely used.

The Moroccan government has prioritized access alongside stability in its ongoing program of financial reforms, and has introduced measures to extend access through microcredit associations, banks, and a new postal bank. In 2008 banks were invited to develop financial inclusion strategies, and the central bank more recently has signaled to banks that it is open to allowing innovations in products and delivery mechanisms. The Central Bank of Egypt has launched a multi-pronged financial inclusion agenda, including a Pensions and Payments Initiative to extend access to basic bank accounts by providing pensions, salaries and procurement payments through the financial system, and a new Licensing and Regulation Law to stimulate the creation of microfinance, leasing, and factoring companies. The Jordanian, Syrian,

Tunisian, Palestinian, Lebanese and Iranian governments, among others, have also implemented notable financial inclusion policies and programs outlined elsewhere in this paper.

State banks and post offices can have extensive branch networks for extending access to financial services. One of the largest branch networks in the region is that of the Principal Bank for Development and Agricultural Credit (PDBAC), the state agricultural bank in Egypt. An initial phase of reforms is showing promising results in terms of improved institutional performance and financials, with an experienced and successful banker as its manager, and non-bank activities (such as agricultural inputs supply) separated from commercial banking. The second phase, with technical assistance from Rabobank, is to better utilize its network of service outlets through improved inter-branch connectivity, product diversification, and investment in improved systems. The PBDAC example is also notable as it represents a more strategic approach of extending financial inclusion through reforms that aim to turnaround institutional performance and improve branch viability, instead of the easier short-term option of closing branches and reducing access.

The creation of a new postal bank in Morocco, building on the strengths of the Post Office as often the only institution serving the low income population - including the rural population, self-employed, and those with irregular incomes – is a promising example of the approach of creating a postal bank.

Box 3. Morocco: new Postal Bank to expand access

The Government is creating a new Postal Bank building on the existing strengths of the Post Office. The post office already provides some basic services (savings passbooks and checking accounts) to a large customer base (4.3 million people).

The new Postal Bank is expected to play a significant access role, by offering a wider range of banking services to underserved categories of the population. The Postal Bank, a subsidiary of the Post Office, will target individuals with a monthly income below 3,000 MAD (357 USD) with an objective of 5.4 million clients by 2015 (a 26 percent increase compared to 2009). These customers are not yet targeted by commercial banks. New services (transfers, payments, debit cards, overdrafts, mortgage loans) will be introduced, although lending would not be offered until a later stage when institutional capacity is more developed.

The Central Bank granted the license to the new Postal Bank in July 2009. As the new institution ventures into new territories, risk management and internal controls will need to be strengthened. In recent years, the Post Office has improved its financial operations with the assistance of consultants (IT systems, branches, back offices, audit), including improvements in internal controls required by the Central Bank during the two year licensing process. The separation of postal and financial activities should improve the quality of services, while outreach should be improved with the specialization of branches and staff, as well as the opening of new branches (550 new branches by 2018) and distribution channels (100 mobile branches and 50 cash points by 2018). The Postal Bank will be subject to the supervision of the Central Bank, like other public commercial banks.

Yemen offers an example of using technology to extend access through a post office network. The Yemen Post Office and Yemen Mobile may launch a mobile banking service, extending access through and beyond the current 300 post office locations. The Yemen Post Office provides savings to 403,000 clients and current accounts to 85,000, and has a significant volume of transfers that would underpin the viability of a mobile banking service, including domestic money transfers, government salary disbursements, retiree pensions, and social welfare fund payments. (CGAP, 2010)

4 Recommendations: a Roadmap for Financial Inclusion in MENA

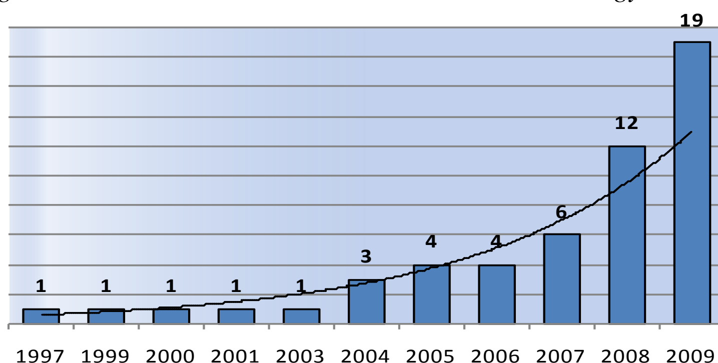
Financial inclusion is an increasing priority for Governments around the world. The 'roadmap' of measures outlined here would i) stimulate private sector investment in serving low income individuals and microenterprises, ii) remove policy, infrastructure and legal barriers to financial service providers to sustainably and prudently expand access to financial services, and iii) encourage product diversification and improved risk management.

The G20 has developed a set of nine Principles for Innovative Financial Inclusion, through a Financial Inclusion Experts Group, which will "form the basis of a concrete and pragmatic action plan for improving access to financial services amongst the poor". These principles were endorsed by the G20 Leadership Summit in Toronto in June 2010, and an action plan will be released at the Seoul Summit in November 2010. The Principles are outlined in Annex 4. The Financial Inclusion priorities outlined in this section are fully consistent with these Principles.

1. Financial Inclusion Strategy backed by data, resources and commitment

Governments and regulators need to take the lead in supporting improvements in access to finance, including in access to microfinance, displaying the *Leadership* called for in the G20 Principles. Financial regulators and governments can add financial inclusion as a goal alongside prudential regulation and financial system stability, and develop financial inclusion strategies. The CGAP and World Bank Financial Access survey (2010) of financial regulators worldwide found that regions that include financial access in their strategies and mandate their financial regulators to carry such agendas are also the countries that reform the most. Regulators with a financial inclusion strategy are more likely to have more financial inclusion topics under their purview and more resources and staff dedicated to working on these matters.

Figure 10. Countries with a Financial Inclusion Strategy Document



Source: CGAP and World Bank Financial Access 2010

Agree Charters and Targets with the Private Sector

Financial inclusion can be promoted through shared public and private sector goals, developed on the basis of improved market data on financial exclusion. *Cooperation* with the private sector and civil society (a G20 Principle) is essential to achieve far-reaching improvements in financial inclusion. Private sector commitments, which may be backed by a threat of regulation or enforcement if the private sector is not sufficiently active in delivering them, can be an effective means of promoting financial inclusion and financial capability. Banks and MFIs can then take a leading role in promoting financial inclusion, spurred on by competition, the threat of regulation, and monitoring, and in line with market opportunities. Commitments by regulators and governments can complement private sector targets.

Charters or codes of practice can be used to agree and set out the financial sector's commitments to expanding access to financial services and to improving the terms of that access. Codes and charters can also encompass consumer education, transparency of information on products, services and tariff structures, complaint handling, and providing secure and reliable banking and payment systems; backed up by regulations and enforcement where necessary. Table 9 synthesizes the key components of what has been effective in several countries.

Table 9: Financial Inclusion Approach and Examples

APPROACH	1. Data underpins Reforms and Innovation	2. Public and private sectors agree financial inclusion goals	3. Public sector removes regulatory barriers and monitors progress on goals	4. Private sector develops new financial services and delivery mechanisms
South Africa:	FinScope Data Survey	Financial Sector Charter	Financial Advisory and Intermediary Services Act, Dedicated Banks Bill	Basic bank accounts and mobile phone banking
UK:	Family Resources Survey	Financial Inclusion Task Force	Progress monitored by Financial Inclusion Indicators	Basic Bank Accounts, Financial services through Post Office
Canada:		Canadian Banking Code	Financial Consumer Agency of Canada	Low cost bank accounts
India:		Banking Codes and Standards Board of India	Reserve Bank of India's guidance on Financial Inclusion	Basic bank accounts, Innovative use of technology to reach customers

Source: Pearce & Bajaj, 2006.

Data availability

Improved data on financial inclusion and unbanked markets/customers is needed to underpin a sustainable expansion in access to finance, as emphasized by the G20 Principle for Financial Inclusion, *Knowledge.* Household and enterprise-level survey questions can provide governments and regulators with the data they need for designing reforms and then monitoring the effectiveness of those reform measures. Financial service providers need market data on financial service demand and needs for new market segments that they have not had previous involvement in, in order to design appropriate financial products and delivery mechanisms. In addition to financial regulator monitoring of progress on financial inclusion, government support may be needed in generating market data for financial service providers, at least initially to address this market failure.

Use Government Payments as a Stimulus for Financial Inclusion

An area that the Government has direct control over is how it pays benefits (social transfers and pension payments) and salaries. By shifting government payments to individuals (G2P, or 'Government to Person') from payments in cash disbursed from post offices or bank tellers, to bank accounts and smart cards (or even mobile phones), significant advances in financial inclusion can be made. Governments make regular payments to at least 170 million poor people worldwide. Yet in most countries, fewer than one-quarter of G2P payments to the poor land in an account that is accessible, in terms of cost and distance. (Porteous, 2006) Delivering G2P payments electronically implies creating for each recipient a store-of-value

account where funds can be held for some period, and connecting that account to an electronic payment system. With these elements in place, it becomes possible to expand the account into a financially inclusive one that the recipient can use to save and to transact outgoing as well as incoming payments.

Promote Financially Inclusive Bank Accounts

MENA governments can encourage banks to launch financially inclusive accounts, shifting G2P payments (increased transaction volume) through such accounts to enhance their viability. Five MENA countries are already promoting financially inclusive bank accounts (according to central bank reporting to CGAP), and five are actively shifting Government payments (salaries, benefits) into the financial system, although only three countries are implementing both – highly inter-related – approaches in parallel. Financial inclusive accounts for low income customers offer basic services such as payments, deposits, and in some cases debit cards, in order to bring unbanked people into the banking system and build a financial history. Encouragement may also be needed by Government through shared financial inclusion targets, and even the threat of regulation if needed, for banks to offer these accounts, as they can be less profitable than full service accounts for higher income customers.

Extend access to a broader range of financial services through existing branch networks

State banks and post offices can offer a unique network of existing outlets as a delivery mechanism for financial services. Postal networks can be restricted to only offering payment and perhaps deposit services though, while access to state banks can be complicated by eligibility criteria, paperwork, inappropriate governance structures, and inefficiencies. Making use of these networks to extend low cost access to a more diverse range of financial services can involve i) institutional reform of a state bank, introducing new financial services and improving governance, portfolio quality, systems and efficiency, ii) the creation of a postal bank, often through a dedicated law, or iii) arrangements with specialized financial service providers, such as banks or MFIs, to provide financial services through the network of outlets.

2. Provide a Regulatory and Supervisory Framework that supports wide Financial Inclusion based on sound risk management and with sufficient consumer protections.

Governments should consider i) allowing banks to expand access through agents, and through use of technology (including mobile phones), ii) providing a finance company model for microcredit and leasing, and iii) removing interest rate caps for microcredit, and instead strengthening consumer protection and stimulating competition between financial service providers. A regulatory and supervisory framework for deposit-taking MFIs such as microfinance banks may not be justified, as these institutions require relatively large up-front investments and can have limited branch networks. Full service commercial and state banks, as well as postal banks and post offices, are better placed to offer deposit services through existing

systems and infrastructure – potentially through financial inclusive accounts - without the need for a new institutional framework such as a deposit-taking MFI.

Stronger, well performing microcredit NGOs should have the option of graduating to regulated financial institutions, such as a finance company model. A finance company legal form can provide the necessary clarity for banks and investors on key questions such as governance, ownership, tax liabilities, and capital base of MFIs, which an NGO license may not. Where regulatory frameworks have been put in place in MENA that allow specialized microfinance institutions – such as finance companies - regulated by financial regulators, the institutions set-up under those frameworks are out-performing microcredit NGOs in terms of growth, and are now a leading driver of growth in MENA microfinance. (Sanabel 2010) A finance company model can tap more effectively into commercial bank and microfinance investor sources of finance – both equity and debt – and potentially do so on more favorable terms (lower cost, less collateral required, longer tenors, currency), than an NGO or association model.

Branchless Banking

For branchless banking innovations to meet their potential to reduce costs and expand outreach, enabling legislation for the use of electronic payments, electronic money, and agents, is needed. Adequate payments infrastructure is also required, and ideally a common switching mechanism. The extent to which mobile banking will be transformational in a country will depend in large measure on whether there is a sufficient degree of openness (there is opportunity to start-up and experiment) and certainty (investors can be confident there will not be arbitrary or negative changes) to the legal and regulatory framework.

Box 4: Principles for an Enabling Environment for Mobile Phone Banking

First tier principles: these are necessary for mobile phone banking to happen at scale:

1. There should be sufficient certainty around electronic contracting.
2. Customers should be adequately protected against fraud and abuse in the mobile banking environment.
3. Inter-operability should be encouraged, through ensuring that providers can access payment platforms and that consumers are able to switch financial providers.

Second tier principles: for transformational models to emerge and succeed, the following additional principles are also necessary:

4. Customer due diligence procedures for account opening should be risk-based, and should not unduly prejudice remote account openings by small customers.
5. Customers should be able at least to make deposits and withdraw cash through agents and remote points outside of bank branches.
6. Adequate provision must be made for the issuance of electronic money by appropriately capitalized and supervised entities which are not necessarily banks.

Source: Porteous, 2006

In countries where mobile banking has taken off, such as Kenya, the Philippines, and Brazil, common characteristics of the interactions between regulators and service providers have been:

- Willingness to consider non-traditional approaches, observe their performance and adjust rules as necessary,
- Continuous dialogue between service providers and regulators,
- Flexible, proportionate approaches to KYC/AML rules via transaction & balance limits, based on understanding of actual risks, and
- Regulator monitoring and reporting mechanisms to keep authorities informed. (Michaels, 2010)

In countries where mobile banking products have been allowed to emerge, financial regulators have tended to focus on whether consumers are making "deposits" when they hand a service provider their money, how to protect consumers, and Anti-Money Laundering rules (in particular Know Your Customer requirements). The training, performance and liability of agents (for example retailers or airtime sellers) are a particular concern to many regulators in this regard. There is also a growing regulator focus on competition, shared infrastructure and/or interoperability, and new business models involving different players.

Use of Agents

A regulatory structure is needed that allows banks to link with MFIs, telecoms providers, and other non-financial actors. Banks and other financial service providers, such as insurance companies, can provide services through agents through wholesale financing, service delivery agreements, fee-based services, agent agreements, and other arrangements. Rules on the use of non-bank retail outlets as agents are needed, that allow outlets (agents) to perform cash-in/cash-out and other customer interface functions. The recent CGAP-led assessment of branchless banking options in Yemen recommended the following enabling framework for branchless banking through agents (Box 5):

Box 5. Enabling Framework recommendations for Agents, the case of Yemen

1. Any legal entity, including MFIs, post office, retail stores, MNO outlets, exchange companies, may be hired by a central bank-licensed institution as an agent to deliver limited financial services
2. Agents may provide most banking services, including bill payments, transfers, deposits, withdrawals, disbursement or repayment of loans, and national wires.
3. The financial institution should remain fully liable for services provided through agents
4. Agents and banks would need to pre-agree customer fees, and communicate those to customers
5. Agents may offer services on behalf of multiple banks, as long as the agent has a separate agreement with each bank.
6. Agents could also be required to implement 'know your customer' requirements, although potentially with lower level requirements for low volume transactions.

Source: CGAP, 2010

Strengthen Consumer Protection

Consumer protection is increasingly important as access increases, so that new customers, and existing customers with access to new services, can take well informed decisions about how best to manage and use financial services. New providers and delivery mechanisms also open up scope for consumer fraud and abuse, as well as to unintentional errors. The G20 Principles call for 'clear and transparent consumer protection regulations that require transparency in pricing and services; identify the parties ultimately responsible for upholding the protections; define supervisory authority; and ensure effective means of dispute resolution and redress are in place.'

Consumer laws and regulations are needed: i) to protect against unfair or deceptive practices, including in advertising and selling financial products, and collecting loan repayments, ii) to improve transparency through disclosure and plain language requirements for products and pricing, in a way that allows consumers to easily compare offers of financial products (for example publication of comparable loan or remittance transfer rates), and iii) to establish a low cost, efficient, and fair mechanism for resolving customer complaints and disputes. (CGAP and World Bank Financial Access 2010) A dedicated agency, or unit within the financial regulator, is needed to ensure a well coordinated and effective approach. Disclosure and redress are at the center of consumer protection, as a primary objective of consumer protection in financial services is to compensate for the imbalance of information, power and resources between consumers and financial institutions. (S Rutledge, pers. comm.)

3. Strengthen Financial Infrastructure for Financial Inclusion

Financial infrastructure improvements reduce the information asymmetry that constrains access to credit and raises the costs and risk of financial intermediation. Reforming secured transactions laws and collateral registries can make the use of collateral more feasible, particularly the kind of lower value movable collateral that is more suited to microenterprise loans. Improving credit information sharing systems, and including microfinance providers, enables microfinance providers to make use of more efficient credit scoring technologies that allow them to lower costs, risks, and loan pricing.

Regulated financial entities should be required to share credit information, ideally through national credit bureaus rather than only through narrow microfinance information-sharing systems. Sharing borrower information is key to lowering costs and overcoming information constraints. By integrating microfinance borrower information into credit bureaus, the coverage and utility of data in the credit bureaus can be improved. Financial institutions of all types can extend access to new customers, while managing risks and costs more effectively. Government intervention or encouragement may be needed to ensure that pricing by monopolistic credit bureaus is accessible for microfinance institutions. Lower pricing for loans below a certain size, may be needed to avoid passing on disproportionately high costs to borrowers. The Moroccan

central bank included differential (lower) pricing for microloans as a condition of awarding the contract for management of new credit bureaus.

4. Ensure a level playing field for Islamic Microfinance

An innovation that is directly linked to financial inclusion is the introduction and adaptation of Islamic banking products for low income consumers and microenterprises. A lack of Shariah-compliant financial services is a constraint on financial inclusion to a proportion of the population. The growth of Islamic microfinance will depend to a large degree on whether financial institutions can develop sufficiently attractive financial products and services, which are competitive with conventional products in terms of pricing, transparency, processing time, and burden on the client. This will be determined in part by their capacity and systems, but regulators can also provide a more level playing field for Islamic microfinance. This extends beyond financial sector regulation to the tax code, as Islamic financing that involves additional transactions such as passing on a property title, has tax implications such as capital gains tax, which are not present in conventional deals.

Practical measures that can be taken by regulators (as has been the case in Indonesia and Pakistan) include: licensing Islamic banks, supporting centers for training and certification on Islamic financial operations to staff and managers of financial service providers, and developing guidelines setting out requirements for licensing and appointment of Sharia advisers to rule on Sharia compliance. The political climate for Islamic finance also affects investor and lender decisions about whether to offer Shariah-compliant products, and acts as an incentive or disincentive to its growth.

ANNEX 1. Access to Finance in MENA: Headline Indicators

A1.1 Access Indicators for Selected MENA Countries

Country	Bank Deposit Accounts per 1000 adults	Bank Loan Accounts per 1000 adults	Private Credit as % GDP
Yemen	103.9	8.3	7.2
Syrian Arab Republic	191.5	72.9	15.7
Morocco	265.3	-	78.4
Egypt, Arab Rep.	439.4	84.9	43.6
Algeria	736.6	-	12.6
Jordan	898.8	200.6	88.8
Oman	1,042.6	412.8	39.4
Tunisia	639.7	193.5	63.2
Lebanon	1,372.0	519.9	73.5
United Arab Emirates	1,750.6	-	73.8
Kuwait	-	-	60.1

Source: CGAP and World Bank Financial Access 2010, International Financial Statistics. Iran data for 2008.

A1.2 Physical Access by selected MENA countries

Country	Branches per 100,000 adults	Branches per 1,000 km2	ATM per 100,000 adults	ATM per 1,000 km2	POS per 100,000 adults	POS per 1,000 km2
Yemen	1.8	0.4	2.8	0.7	17.0	4.1
Syria	2.4	1.8	2.7	2.0	2.2	1.7
Algeria	5.3	0.6	5.7	0.6	-	-
Egypt	8	4.5	8.7	4.9	-	-
Saudi Arabia	8.5	0.7	54.4	4.5	438.5	36.3
Morocco	9.9	4.9	18.6	9.3	89.9	44.8
Tunisia	14.4	7.3	17.3	8.8	121.6	61.7
Kuwait	16.5	19.3	53.4	62.6	1,040.1	1,219.4
Jordan	17.8	7.7	26.3	11.4	-	-
UAE	20.9	9.0	99.3	43.1	-	-
Oman	22.6	1.4	45.9	2.8	-	-
Lebanon	28.8	86.5	39.3	118.0	1,382.8	4,149.1
Iran	29.2	9.7	29.8	9.9	2,038.1	680.4

Source: CGAP and World Bank Financial Access 2010, Egypt Central Bank, Saudi Arabian Monetary Agency

A1.3 Financial Inclusion: Provider Typology

Country	Year	Commercial Banks offering MF	Credit Unions & Mutuals	Government Savings or Development Banks	Microfinance Institutions (*)	Other financial institutions	TOTAL
Algeria	2008	-	No data	4	3[14]	1	29
Bahrain	2009	-	-	-	3	-	3
Egypt	2010	4	-	-	>280 (14)	-	-
Iraq	2010	-	-	-	13 (2)	-	
Iran	2009	-	No data	5	-	-	18
Jordan	2009	1	0	3	200 SHGs, 7 MFIs (7)	-	3
KSA	2010	-	-	-	1	-	-
Kuwait	2008	-	112	1	-	99	227
Lebanon	2009	>3	0	-	(3)	-	53
Morocco	2009	-	11	5	13 (9)	43	84
Oman	2008	-	0	2	0	6	25
Syria	2009	-	0	1	2 (2)	0	21
Tunisia	2009	-	0	1	273 (1)	15	309
WB&G	-	-	-	-	(8)	-	-
Yemen	2009	1	0	2	13 (6)	1	29

Source: Survey on access to financial services CGAP. Figures in parentheses are the number of MFIs reporting to the Microfinance Information Exchange. (*) All MFIs except for those in Syria and Yemen are not deposit-taking. SHGs are 'self help groups'.

A1.4 Regression Analysis: Deposit Accounts

VARIABLES[15]	(1) Dep. Acc	(2) Dep. Acc	(3) Dep. Acc
GDP per capita	0.0171**	0.00644	0.0822*
	[-0.00662]	[0.007]	[0.0365]
Branches per 100,000 adults	38.06***	73.21***	69.84*
	[-9.727]	[-16.93]	[-24.56]
% of State Branches		883.5*	
		[-434]	
ATM per 100,000 adults			-37.8
			[-20.95]
Constant	144.2	-628.8	26.03
	[-135.7]	[-353.2]	[-135]
Observations	10	9	10
R-squared	0.852	0.943	0.904

Standard errors in brackets. *** p<0.01, **p<0.05, *p<0.1

[14] The Agence de Developpement Social (ADS) provides microloans through banks. There are no MFIs of any notable scale.

[15] Source of country data used in the regressions: CGAP and World Bank Financial Access 2010

ANNEX 2. Principal Features of Microcredit in MENA

A2.1 Microcredit Sector Growth (Borrowers)

Country	Active Borrowers				
	2006	2007	2008	2009	Growth Rate 08-09
Bahrain	2,175	2,175	2,175	2,175	0%
Saudi Arabia	7,000	7,012	7,064	7,064	0%
Syria	50,611	54,620	22,660	26,118	15%
WB/G	25,592	23,313	31,633	36,532	15%
Lebanon	16,109	21,284	27,759	38,036	37%
Yemen	33,934	34,062	34,982	41,268	18%
Iraq	15,234	24,597	38,084	55,266	45%
Jordan	77,778	110,202	139,715	161,154	15%
Tunisia	123,504	146,308	177,124	205,206	16%
Morocco	996,482	1,334,147	1,256,084	923,551	-26%
Egypt	751,529	1,093,539	1,148,621	1,310,746	14%
MENA	**2,099,948**	**2,851,259**	**2,885,901**	**2,807,116**	**-3%**

Source: Sanabel Microfinance Regional Network 2010, Microfinance Information Exchange

A2.2 Market Trends: Growth in Outstanding Loan Portfolio

Country	Gross Loans					Growth Rates (%)			
	2005	2006	2007	2008	2009	2006	2007	2008	2009
Morocco	163,683,452	422,546,383	722,756,147	699,063,213	612,432,772	158.1	71	-3.3	-12.4
Saudi Arabia		5,866,041	6,190,234	7,870,346	7,862,514		5.5	27.1	-0.1
Bahrain	775,193	775,193	775,193	775,193	775,193	0	0	0	0
Jordan	65,848,733	83,431,699	87,338,912	128,060,962	133,934,944	26.7	4.7	46.6	4.6
Tunisia	78,262,116	83,614,008	93,436,674	105,012,790	112,407,271	6.8	11.7	12.4	7
Syria	65,556,153	68,151,129	71,271,600	17,917,603	19,871,075	4	4.6	-74.9	10.9
Egypt	190,335,538	245,407,712	271,471,809	328,145,693	372,735,191	28.9	10.6	20.9	13.6
Palestine	36,414,494	40,040,235	53,440,074	80,188,384	97,657,312	10	33.5	50.1	21.8
Lebanon	38,486,265	37,974,542	44,460,215	50,088,416	61,538,963	-1.3	17.1	12.7	22.9
Yemen	4,747,602	5,747,540	4,423,347	6,031,871	7,873,736	21.1	-23	36.4	30.5
Iraq	18,602,228	64,867,831	32,232,442	55,145,177	78,325,160	248.7	-50.3	71.1	42
MENA	**662,711,774**	**1,058,422,313**	**1,387,796,647**	**1,478,299,648**	**1,505,414,131**	**59.7**	**31.1**	**6.5**	**1.8**

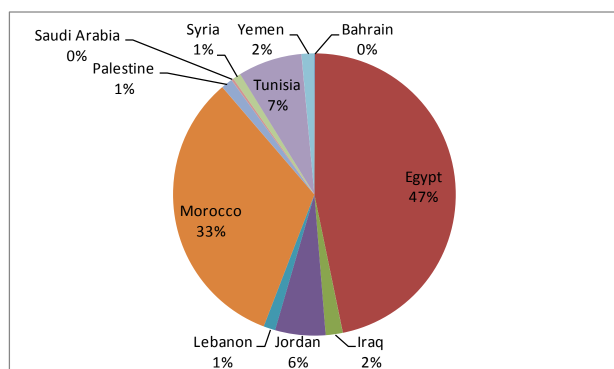
Source: Sanabel

A2.3 MENA Microfinance Sector: Headline Ratios

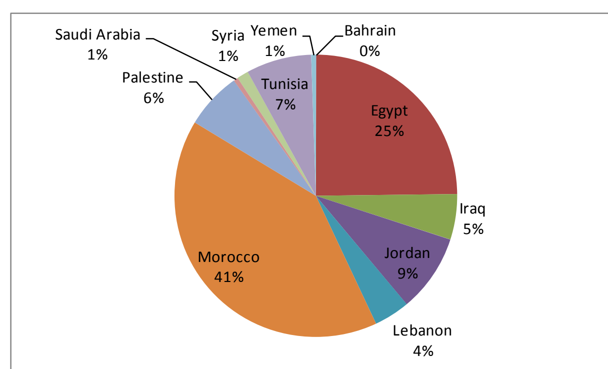
Country	Profitability (ROA)	Operating Expense/ Loan Portfolio	Portfolio Quality (PAR>30 days)
Syria	-2.0	4.5%	3.3%
Morocco	0.3	23.6%	4.8%
Yemen	0.7	43.6%	4%
Jordan	5.4	24.9%	2.1%
Lebanon	5.6	18.3%	2.1%
Palestine	5.7	26.9%	11.3%
Egypt	6.5	20%	1.8%
Tunisia	9.0	17.2%	0.5%
Iraq	20.6	15.4%	0%

Source: MIX database. 2008 data. Profitability ROA (weighted averages). Portfolio Quality (weighted averages by gross loans)

A2.4 Borrowers by Country (2009)



Loan Portfolio Market Share (2009)



Source: Sanabel Industry Survey, 2009 (Microfinance in the Arab Region: An Industry Update)

A2.5 Funding for Microfinance in MENA: Sources of Funding by Lender Type

	Number of MFIs	Total Amount (USD)	Percentage
Development Finance Institution	14	17,019,493	2.6
Financial Institution	24	522,479,127	80.2
Fund	14	29,073,806	4.5
Government	12	69,624,889	10.7
Other	13	13,216,559	2

Source: MIX database

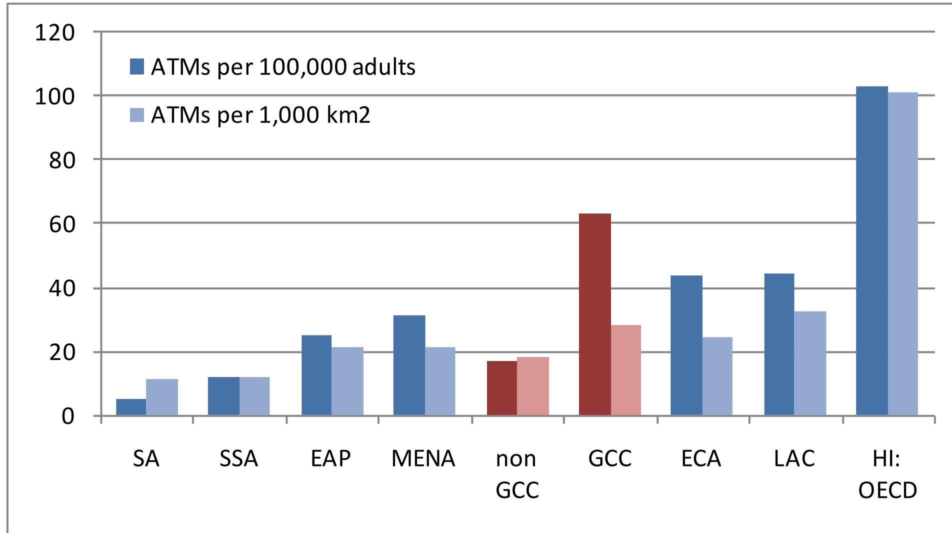
A2.6. Microfinance Regulation and Supervision in MENA

	Not Regulated	Regulated by a financial regulator	Number of regulated institutions	Fall under non-financial regulator
Algeria	X	-	3	X
Egypt	-	X	2	MFI NGOs still overseen by Ministry of Social Solidarity
Iraq	X	-	-	X (Ministry of Trade, NGO Assistance Office)
Jordan	X	-	-	X (Ministries of Industry and Trade, Planning, Social Development)
Kuwait	X	-	0	-
Lebanon	X	-	0	-
Morocco		X	-	-
Oman	X		0	-
Syrian Arab Republic		X	1	-
Tunisia	X	-	-	X
UAE	X	-	0	-
Yemen, Rep.	X	X	14	Most MFIs report to Social Fund for Development

Source: M Khaled, 2010; MIX, Sanabel, CGAP, 2010. Iran also has MFIs regulated by a financial regulator.

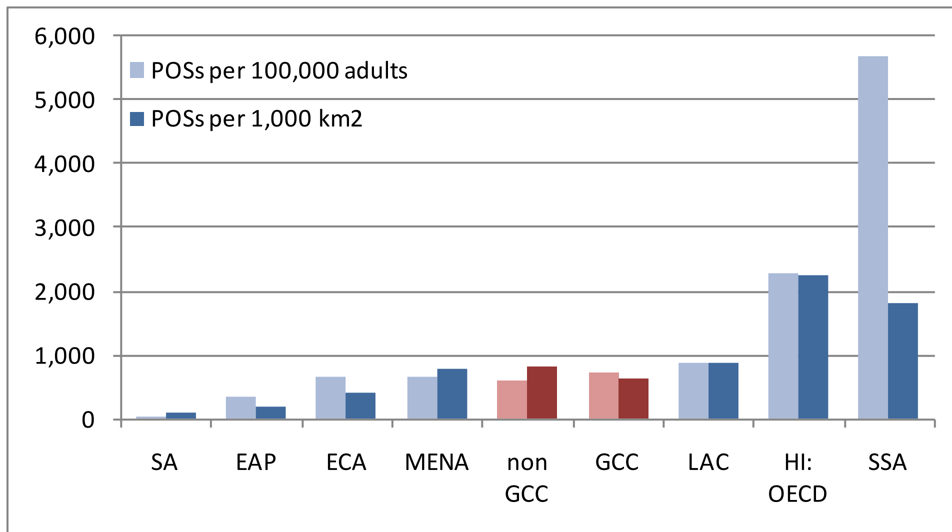
ANNEX 3. Branchless Banking

A3.1 ATM Networks



Source: CGAP and World Bank Financial Access 2010

A3.2 Point of Sale Networks



Source: CGAP and World Bank Financial Access 2010

A3.3 Mobile Penetration, GDP per capita in MENA

Country	Total Population	Rural population (% of total population)	GDP per capita (current US$)	Mobile cellular subscriptions (per 100 people)
Djibouti	849,245	12.7	1,030	13.3
Yemen, Rep.	22,917,485	69.4	1,160	16.1
West Bank and Gaza	3,937,309	28.1	1,123	29.3
Lebanon	4,193,758	13.0	6,978	34.0
Syrian Arab Republic	20,581,290	45.8	2,682	34.3
Egypt, Arab Rep.	81,527,172	57.3	1,991	50.6
Iraq	30,711,152	33.4		57.1
Iran, Islamic Rep.	71,956,322	31.5	4,028	59.8
Morocco	31,605,616	44.0	2,769	72.2
Libya	6,294,181	22.5	14,802	76.7
Tunisia	10,327,800	33.5	3,903	83.3
Jordan	5,906,043	21.6	3,596	90.0
Algeria	34,373,426	34.8	4,845	92.7
Kuwait	2,728,041	1.6	54,260	106.6
Oman	2,785,361	28.4	15,273	115.6
Qatar	1,280,862	4.4	62,451	131.4
Saudi Arabia	24,645,686	17.6	19,022	146.1
Bahrain	775,585	11.5	28,240	185.8
United Arab Emirates	4,484,935	22.1	45,531	208.6

Source: WDI World Bank 2008 data

A3.4 Comparison of Service Prices Between Banks and Branchless Banking Providers

	Bank	Branchless Banking (BB) Provider	% by which BB is Cheaper
Sending	2.8	2.4	12%
Receiving	2.8	2.1	24%
Short-term Safekeeping	3.7	5.4	-48%
Medium-term Savings	3.3	1.6	50%
Bill Payments	6.9	3.4	50%
High Usage	8.4	7.4	12%
M-Pesa Customer	3.3	2.9	12%
Kenya Bank Customer	7.5	6.5	14%
AVERAGE	**4.8**	**3.9**	**19%**
Total Price to send & receive $62 ($160 PPP)	Avg Informal Provider**: $10.7	Avg Branchless Banking Provider: $4.9	**54%**

Source: CGAP, Branchless Banking Pricing Analysis, Claudia McKay, Mark Pickens, May 2010; 2010 data

Note: * Prices based on one month of usage. Figures in US$ PPP adjusted. ** Informal methods analyzed include taxi/courier, money changer, bus service, and post office in 3 countries.

ANNEX 4. G20 Principles for Innovative Financial Inclusion

Innovative financial inclusion means improving access to financial services for poor people through the safe and sound spread of new approaches. The following principles aim to help create an enabling policy and regulatory environment for innovative financial inclusion. The enabling environment will critically determine the speed at which the financial services access gap will close for the more than two billion people currently excluded. These principles for innovative financial inclusion derive from the experiences and lessons learned from policymakers throughout the world, especially leaders from developing countries.

1. **Leadership**: Cultivate a broad-based government commitment to financial inclusion to help alleviate poverty.
2. **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.
3. **Innovation**: Promote technological and institutional innovation as a means to expand financial system access and usage, including by addressing infrastructure weaknesses.
4. **Protection**: Encourage a comprehensive approach to consumer protection that recognizes the roles of government, providers and consumers.
5. **Empowerment**: Develop financial literacy and financial capability.
6. **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.
7. **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.
8. **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.
9. **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.

These principles are a reflection of the conditions conducive to spurring innovation for financial inclusion while protecting financial stability and consumers. They are not a rigid set of requirements but are designed to help guide policymakers in the decision making process. They are flexible enough so they can be adapted to different country contexts.

ANNEX 5. Morocco: Microcredit Portfolio Repayment Crisis and Recovery

Morocco's microfinance sector grew fast, with the total loan portfolio multiplying 11 times between 2004 and 2007. It was seen as a regional leader. However, in 2007 some signs of stress - notably clients' over-indebtedness and loan delinquency - started to emerge. A study conducted by *Planet Finance*[16] highlighted the concentration of microcredit loans and the development of multiple lending in urban areas. Non-performing loans started to rise significantly from one of the lowest levels of the world, 0.42% in 2003, to 1.9% in 2007. The sharp rise in non-performing loans took place in 2008 and affected all MFIs. Portfolio at risk (30 days) increased significantly to 5% in December 2008 and reached an alarming level of 10% in June 2009. In May 2009 *Zakoura*, one of the Moroccan flagship institutions, became insolvent and was forced to merge with another institution. Some MFIs are still facing serious management and portfolio quality challenges.

The roots of the credit crisis can be found in the institutional capacity of microcredit associations. The unprecedented growth overstretched their capacity, translating into lenient credit policies, obsolete Management Information Systems (MIS) systems, lack of internal controls and substandard governance. Multiple lending to the same clients was an aggravating factor. A study conducted by the central bank estimated that 40% of microcredit beneficiaries had more than one loan. The problem is particularly acute in urban areas.

Microcredit associations have put in place recovery plans that include management changes and freezing new disbursements. Associations are tightening their credit processes, putting in place teams focusing on loan recovery, and are taking judicial action with a demonstration effect on delinquent borrowers. They are also exchanging credit information on a weekly basis to control over-indebtedness. Smaller microcredit associations are planning to share resources such as back office systems or to merge. These efforts are slowly paying off. However, some associations have been severely hit and will have to be restructured; others are emerging stronger and well positioned for another phase of growth.

The Ministry of Finance organized the merger acquisition of the worst affected association, *Zakoura*, by the *Fondation des Banques Populaires*, a large microcredit association backed by the *Banque Centrale Populaire*, to restore confidence and avoid further contagion effects on loan delinquency.[17] A directive was prepared to strengthen the governance of the associations and introduce tighter financial reporting requirements. The Moroccan government also secured 46 million USD in donor funding to support the sector, provide new liquidity, and strengthen management information systems and internal control.

A credit bureau was launched in October 2009, with borrower information from the leading microcredit associations included. This was a major step forward that allows microcredit associations and banks to improve credit analysis as well as to control client over–indebtedness.

The Ministry of Finance has launched a survey with funding from the Millennium Challenge Corporation to assess the strengths and weaknesses of the sector and to provide recommendations to improve the regulatory framework for microfinance. The study will also look at the transformation of some of the largest institutions into commercial, prudentially regulated, entities.

Sources: Reille, 2010; MIX, Sanabel, CGAP, 2010; Microfinance Information Exchange.

[16] Planet Finance survey on multiple lending in the microcredit sector in Morocco, unpublished.
[17] While the merger acquisition of Zakoura was announced in May 2009, and Fondation de Banques Populaires (FBP) has taken over management responsibility, there are legal issues remaining to fully complete the merger.

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