Opening remarks for the 2011 AFI Global Policy Forum "Taking Stock. Setting Goals. Moving Forward." Cancun, September 28, 2011

1. Welcome remarks and introduction

- It is a pleasure to have you here in this beautiful resort in the south east part of México. I welcome all the participants to this Global Policy Forum organized by the Alliance for Financial Inclusion.

- As all of you know, during this year, and in particular the last few weeks, many of us have been deeply involved in discussing issues related to fiscal consolidation, financial stability and low economic growth mostly in advanced economies. These issues are certainly very important and deserve a great part of our time and efforts, since lack of financial stability in the developed countries can represent a serious impediment of growth to the rest of the world.

- However, I am very pleased that we gather here today to devote part of our time to another important topic, which is also part of the G20 agenda. Certainly, financial inclusion does not seem as pressing as crisis management, but it as relevant for its long term implications on economic growth and population wellbeing.

- Looking at this Forum's program it is very gratifying to see that the drive towards financial inclusion around the world have been resilient to the financial crises. Many countries have been working hard and dedicating economic and human resources during this last three years, in spite of the turbulent times in the global financial markets.

- I will focus today's address in three topics. First, I will make some considerations about the importance of financial inclusion. Second, I will describe the efforts that Banco de México has done to promote financial inclusion; and third, I will mention the challenges we face, not only in México but worldwide in this regard. I will end with brief concluding remarks.

2. Importance of financial inclusion

- In recent years there has been an increasing interest in Financial Inclusion. It has been argued that it helps reduce poverty and that it promotes economic development. Recent evidence supports this argument showing that not only does a correlation exist between financial development and economic growth but also that the former causes the latter.

- Reductions in inequality, increased growth rates, and productivity gains are in part the consequence of financial deepening. Furthermore, randomized controlled trials conducted in several countries have shown that financial inclusion leads to wider investment options for small enterprises and better terms for wealth transfers to low-income individuals.

- There is not a universally accepted definition of financial inclusion. Some definitions imply that all people should have access to financial services, while others define a vulnerable group, usually with lower income, as the inclusion target. Some definitions consider inclusion to all types of financial services, others to a subset of them.

- A definition that seems appropriate for the purpose of policy is that used by the World Bank. Financial inclusion is defined as the absence of barriers to access; such barriers may be lack of infrastructure, customers' ineligibility or lack of information, inadequate product design, customers' lack of trust in financial intermediaries, and high prices and interest rates. Inadequate or excessive regulations could also constitute a barrier for financial inclusion.

3. The Mexican case

- Financial inclusion in Mexico has been growing in recent years according to all the merits that are available.

- Nonetheless, a significant number of Mexicans is still excluded from the financial system. In many cases exclusion is not due to the lack of physical infrastructure. Additionally, people with access to the financial system tend to make marginal use of it. To illustrate this, there are more than 80 million debit cards issued in Mexico, but in a given quarter only 38 million of them (less than 48%) are used. Moreover, the number of transactions performed with banking cards at points of sale in Mexico is lower than in Brazil, let alone more developed countries.

- Given the impact that financial deepening has on economic growth, I believe that the limitations on financial inclusion have reduced Mexico´s growth potential.

- The trend for wider financial inclusion in Mexico was not interrupted by the world financial crisis. For instance, the number of deposit accounts did not stop growing during the last years; only credit card accounts dropped but they are already recovering.

- The already existing trend toward wider financial inclusion constitutes a solid base for future developments in this account.

3.1. Banco de Mexico’s mandate and financial inclusion

- Financial inclusion is not explicitly part of Banco de México's mandate; price stability is its first and foremost goal. Nevertheless, other important goals of the Mexican central bank are related to financial inclusion issues.

- Banco de Mexico's law mandates the central bank to promote sound and efficient financial and payment systems. Additionally, the Transparency and Financial System Restructuring Law

(Transparency law) establishes obligations to Banco de México that have a direct and indirect impact on financial inclusion.

- An essential element for financial development is price stability. When there is no price stability, people stop using formal intermediation channels. Price stability allows agents to get into long term financial transactions, like buying a house or saving for retirement. High level of inflation affects severely the wellbeing of the poor because they are not able to hedge against the evasion of purchasing power of their salaries and scout saving. High level of inflation inhibits financial inclusion. Therefore, the main contribution that Banco de México could do to financial inclusion is to promote price stability.

- Wider financial inclusion is consistent with price stability in another way. Inclusion results in better functioning financial markets with fewer informational asymmetries. Also, by incorporating more individuals into the financial sector, more people acquire the means to smooth consumption over time, and to insure against adversity. These may act as automatic stabilizers during crises and recessions.

- Regarding the promotion of a sound financial system, greater financial inclusion allows for a more efficient allocation of resources. In a sense, lending is a matching problem; intermediaries match amounts, terms (plazos) and risks between borrowers and depositors. By including more consumers in the system, banks, and financial intermediaries in general, have a wider pool to solve the mismatch problem.

- Fostering an efficient payment system is an integral part of financial inclusion. Customers with a deposit account, and the payment options usually associated to it, are able to choose the most efficient means of payment available to them. Additionally, access to efficient payments vehicles reduces customers' transaction costs and increases payment security; this impacts productivity positively since customers have more time to dedicate to other activities, at the same time that risks are abated providing an essential element of any entrepreneurial activity: certainty.

3.2. What Banco de Mexico has done regarding financial inclusion

– Banco de México has also participated decisively, within the scope of its authority, in the development of regulation to eliminate the barriers that households, small and medium enterprises, and providers face when interacting in the financial system.

– One of the most relevant recent developments for financial inclusion in Mexico has to do with payments through mobile means. This year, Banco de México issued regulation to contribute to the development of payments through these means by defining several types of bank accounts.

– The logic behind these accounts is that their regulatory treatment should be proportionate to the risks and benefits involved in offering the services; it reflects the international Anti-Money Laundering standards, and it takes advantage of the banking correspondents regulation recently issued. Additionally, it is consistent with the nine principles for innovative financial inclusion endorsed by the G20.

– Four types of bank accounts have been contemplated by regulation by regulation. The documents required to customers to open such accounts and the associated monitoring are negatively related to its transaction capabilities. That is, the least risky accounts have lower information and monitoring requirements.

– Mobile services and banking correspondents hold enormous potential to expand financial inclusion. On the supply side, tside options reduce the cost of service provision, give that there is no need to open branches or deploy ATMs. On the demand side, transaction costs faced to users are significantly diminished. A very powerful side benefit for development purposes is that people in isolated areas will now have a chance to be part of the financial system.

- In addition, this scheme promotes customer confidence in the financial system since their deposits are protected under the deposit insurance system. Also, payments through mobile means are settled through the banking network and are subject to the transparency and protection rules applied to any other payments made through the banking system.

- Banco de México established also the terms and conditions of basic accounts, which banks are obliged to offer accounting to Mexico´s Transparency Law. Basic accounts contemplate restricted services that are not subject to any fees or commissions. Since they are offered by all deposit taking institutions, they are widely available. The offering of basic accounts eliminated some product design and price barriers that used to deter access to the system. These accounts have been rather successful: there are now more than 16 million of them.

- We have also indirectly promoted inclusion by regulating banking fees and commissions. This strategy, implemented since 2010, eliminated charging practices that were not consistent with competitive market behavior. The principles followed in this regulation include: charges have to be related to actual services provided to the consumer; there cannot be two charges for the same service; there must be at least one channel free of charge through which customers may have access to their deposits; fees should not constitute a barrier to customer mobility; and information about fees should be transparent for customers.

- In accordance with the Transparency Law, Banco de México keeps a "Register of Fees and Commissions"; any increase in fees has to be reported and justified to the Central Bank. Banco de México can issue objections if proposed fee increases are deemed unjustified. Objections are made public thereby affecting institutions' reputation.

- Additionally, Banco de Mexico has promoted trust and competition in the banking system by means of publishing reports containing a wide range of indicators of consumer credit. These reports promote competition among providers and customers mobility.

- Also, Banco de Mexico has taken steps to promote the adoption and usage of electronic means of payment, which indirectly favors financial inclusion. Among them, there is a permanent campaign to foster the use of SPEI, our interbank electronic payment system, which is extremely cost effective even for small scale transactions.

4. Challenges ahead

4.1. Challenges for Mexico

- Mexico has made progress in all of the nine principles endorsed by the G20 regarding financial inclusion; however, there are still challenges ahead.

- Reaching isolated, rural areas with low population density is probably the main challenge for the Mexican financial system. Although 95% of the population lives in municipalities in which financial infrastructure is available, there are many small and isolated municipalities that lack physical access to financial services. The recent drive in favor of mobile banking and banking correspondents is designed to face heads on this problem, but it is still too soon to know its impact.

- The promotion of access for people that live in places with financial services availability, i.e. in urban areas, also represents a huge challenge. Many reasons may explain this phenomenon, among them: lack of trust in financial institutions (in a 2009 Banxico survey, 56% of respondents said they had little or no trust in banks); lack of financial education (26% said they were not familiar with checking or savings accounts); poor consumer protection; high prices; and inadequate services.

4.2. Global challenges

- On the international agenda, I firmly believe that the main challenge we face ahead on financial inclusion is to be sure that the overhaul of the financial regulation agreed by the G20, mostly oriented to prevent financial instability, do not affect the efforts and long term process of promoting financial inclusion.
- I do endorse H.R.H Princess Maxima's proposal to include the following text in the foreword of the revised draft of the Basel Core Principles:

  "Recognizing the complementarity among financial stability, integrity and inclusion, as well as the positive effects that financial inclusion has on growth and sustainable development, it is encouraged to implement the principles in ways that do not unnecessarily limit access to finance".

- Other challenge is to promote technological and institutional innovation that lower transactions costs and make financial services readily available. Recent developments in correspondent banking and mobile services seem to be a promising avenue for expanding financial penetration. Regulation should be adapted constantly so that these schemes have a continuous impact on financial inclusion.

- Another challenge is to find a balance between promoting financial inclusion while keeping the adequate Anti-Money Laundering (AML) restrictions.

5. Concluding remarks

- I believe that through financial inclusion, the general population and, above all, the poorest can share the benefits of a stable, efficient and competitive financial system. This is particularly so in today's world in which it is expected that economic growth in advanced economies will slow down, forcing emerging and developing economies to look for opportunities to enhance domestic growth, and an obvious candidate to do so is through financial inclusion.

- Thank you very much.