**Speaking Notes for Loic Chiquier (Director, World Bank)**

**CGAP-Silatech: Youth Financial Inclusion Workshop**

**12 March 2013**

- Good morning to all of you. It is a pleasure and honor for me to be speaking today to this distinguished audience made of experienced practitioners. I would like to thank Silatech and CGAP for organizing this event and for the opportunity to provide opening remarks on the behalf of the World Bank Group. We are truly delighted to take part in this workshop engaging on the issues of youth financial inclusion in the MENA region, and I am sure we at the World Bank have a lot to learn from all of you over the course of these two days.

- Our base assumption, or even belief, is the **timely importance of this theme** to advance the broader agenda of economic and social participation in the region. Citizens are challenging governments to implement policies that provide renewed economic and social opportunity. Particularly for the young people, many of whom led protest movements since the Arab spring. Financial inclusion is a key component of this broader challenge.

- By financial inclusion we mean the access and usage of quality financial services, provided at affordable prices. A broad range of financial services, not just credit but including as well savings or insurance is critical for a larger part of the population to manage risks, smooth consumption, and invest productively for example into a new business or housing.

- As half (or 88 million) of the region's population is youth (15-24), enhancing financial inclusion must include the needs and behavior of youth. Providing them with quality financial services can help ease the stress associated with major transitions, such as starting secondary school or university, getting married, having children, acquiring a housing, financing consumption goods, starting a small business, or suffering the death of a family member.

- This challenge will require a **strong and coordinated response** from the region's financial sector, and in particular the microfinance sector. We start from a relatively low base here as financial inclusion remains low in the Middle East North Africa (MENA) region compared to other developing country regions. The region has the lowest percentages of adults with a formal account (18%). With regards to youth, only 13% of young people (age 15-24) in MENA had accounts at a formal financial institution, and less than 5% borrowed from a formal financial institution. As highlighted in our financial sector flagship (2011), the microfinance sector is still small, with outstanding microcredit accounting for just 0.2% of GDP. Lending by microfinance providers reaches only 1.8% of the adult population, half the proportion in South Asia or Latin America and the Caribbean. By contrast the number of people living below $1.25 a day is 13 times larger in South Asia than in MENA. Even in Morocco, the country that has made most progress in developing the industry, microcredit loans barely exceed 1% of total bank credit (in amount) compared to 7% in LAC and 5% in Africa.

- We have seen the microfinance industry continue to counter challenges in response to the higher volatile political and economic conditions in the MNA region, which is exposing all financial players to an increased level of risks to manage. In some countries, the microfinance industry faced serious difficulties even before the Arab spring like in Morocco in 2007-08, or through the Arab spring like in Tunisia. In Morocco, NPLs increased, as some overstretched MFIs paid the price of inadequate internal controls, governance and financial infrastructure. The Central Bank took actions to promote consolidation, improve reporting and risk management. Yet NPLs remains relatively high in some areas. A new microfinance law has recently been passed which constitutes a great step forward but there is still some regulatory uncertainty, for example about the capping of commissions. Tunisian and Egyptian markets also remain small, but data suggest a relative recent expansion, correlated with the resiliency of the informal business this industry has been serving, maybe also by contrast by a crowding out of bank lending to the private sector. In Tunisia, the Ministry of Finance took actions to restructure the industry. In most countries, the development and implementation of financial inclusion strategies remains delayed by ongoing political uncertainty.

- These challenges prevent the microfinance sector from expanding, precisely when this development is needed to help the region meet its broader development challenges. **Notably unemployment which is largely a youth phenomenon**. At about 25%, the youth unemployment rate in the MENA exceeds that of any other region in the world – a rate that reaches up to about 30% in Tunisia. The number of young people ages 15 to 24, increased from 44.6 million in 1980 to 88.1 million in 2010—a doubling in 30 years. 2 out of 3 people in the region are under 30 years old and youth make up 1/3 of the working age population. Under such circumstances, our collective challenge is then to transform a demographic reality into a financial and economic opportunity. These calls for additional economic and social opportunity, coupled with the under-developed stage of financial inclusion creates a unique opportunity for governments in this region to take concrete actions to support financial inclusion, including structural changes to the microfinance industry. What the core areas of reform then?

- First, most MFIs in the region are hampered **by limited product offerings and delivery channels**. Apart from Yemen, West Bank and Gaza, MFIs are not legally allowed to take deposits. This is a limitation for these institutions to develop a more sustainable funding base, and to better manage their risks.. Promoting youth savings helps to reduce future portfolio risks, and the regular use of savings has a positive impact on future credit scores and down payments. Notably in a region where the informal sector employs more than half of the labor force. But of course financial regulators remain legitimately concerned about the capacity of non-bank lenders to collect public deposits and professionally manage risks, so the debate is not over. Back to product offerings, we observe quite incomplete markets with hardly developed Islamic micro finance (compared to countries like Indonesia, Bangladesh, or Afghanistan), micro insurance or micro lending for housing.

- Second, the industry suffers from **ineffective or absent regulation that prevents efficient and inclusive growth.** Most financial regulators in MENA do not have a high degree of involvement in promoting financial inclusion. Only few countries in the region have introduced supportive legislation, in most countries there is no clear supervisory responsibility over the microfinance industry. When the majority of microfinance providers are registered as NGOs, some commercial and social investors are reluctant to finance NGOs or associations (or will only do so with short-term debt). Interest rate caps are in place in at least 6 MENA countries, making it more difficult to achieve financial sustainability for MFIs and other institutional providers. Several countries started to draft new micro finance regulatory packages, but most have not been implemented yet.

- Third, operational inefficiencies amongst MFIs are in part the result of **underdeveloped financial infrastructure.** Generally many MFIs are not integrated into the formal credit information system. Credit assessment and risk management techniques of many lenders-– not just MFIs- tend to be outdated, implying that lenders often have to rely on collateral that is expensive to register and may not be readily enforceable. MENA has the lowest score on the Doing Business Legal Rights index of any world region. As a result, financial institutions face higher levels of credit risk, and tend to remain quite conservative. Yet we have seen encouraging progress in that space.

- Fourth, **consumer protection and financial literacy efforts** in the region are relatively nascent. Of 11 MENA countries that responded to the 2010 CGAP and World Bank Financial Access survey, 7 had introduced consumer protection reforms, indicating that MENA is getting in line with global trends. However, many MFIs in the region have developed consumer protection and financial responsibility codes on a voluntary basis, as seen through members of the regional network Sanabel signing a consumer protection and responsible finance document in 2008.

- Addressing the high levels of financial exclusion in MENA will require coordinated and concerted action on behalf of governments, policymakers and researchers, in addition to local communities. The **critical questions we must ask are**: 1) what policies are needed to ensure the microfinance sector develops sustainably and inclusive of important target groups such as youth? And 2) how to implement these policies effectively?

- First, there is a need to improve the legal, regulatory, and institutional environment for microfinance institutions. On the regulatory front, laws must be implemented that provide clear guidelines for MFI operations and balance consumer protection with the ability of the sector to grow and innovate. Amending regulations to allow for a full suite of financial services including deposits and insurance would be an important place to begin.

- Similarly, critical investments in financial infrastructure improve the environment for microfinance. Credit reporting can help manage risks and promote innovation. In particular, developing platforms to track credit information on **mobile phones** can help expand mobile banking, which could grow fast given the number of young people with mobile phones in MENA. Other investments needed include enhancing credit bureaus across the region, expanding payment systems, improving deposit insurance schemes, and upgrading physical infrastructure to access rural clients. Such reforms reduce the cost of delivering financial services to the underserved groups.

- At the institutional level, significant work is needed to enhance the capacity of providers, MFIs, banks and NBFIs, to operate sustainably and offer quality products that meet the financial needs of the youth. Assistance can include developing effective risk management and internal controls systems, training key staff members such as loan officer and senior management, developing effective supervision and reporting systems, and developing products that are in demand. The WBG supports these efforts through a regional approach (MENA MSME TA facility). Access is also a key objective of our new Arab Housing Finance Initiative in partnership with the Arab Monetary Fund

- There is a need to develop the capacity for growth and innovation of micro and small entrepreneurs. We know that MSMEs typically account for 20% to 40% of all employment in MENA. We also know that 10-15% of SMEs create 50-80% of new jobs in the region. These entrepreneurs, however, are largely finance constrained (only 8% of total bank lending is to SMEs; 2% for GCC countries) and often lack the support necessary to manage the red tape around starting and growing a business. An ecosystem most hospitable to micro-entrepreneurs is needed to help **young entrepreneur**s get access to the knowledge, finance, and networks necessary to allow innovative ideas to turn into business success stories. A recent WB project in Lebanon aims to do just this. The project will provide US$2.5 million for Concept Development Grants (CDGs) to microentrepreneurs; andUS$25 million for equity investment in Seed, Early/Venture, and Growth stage firms. We also promote MSMEs in Yemen, where a $4.9 million dollar project will provide 400 firms with matching grants for business development as well as providing up to 400 fresh college graduates internship programs.

- In addition to this operational front, strategic investment in research and data is needed, particularly research that analyzes why the demand, usage, and access to microfinance services remains so low in MENA. The World Bank Group is currently embarking on such a demand-side study of financial exclusion amongst women and youth across North Africa in order to better understand what interventions are needed to bring them into the formal financial sector. We look forward to working with our colleagues across the academic, donor, and NGO community on bridging knowledge and action through research that addresses key market gaps in MENA.

- Financial sector development in the region will increasingly have to move beyond the purview of the microfinance model alone, instead working with a variety of providers, from community-based savings groups to postal banks to promote an integrated vision for financial inclusion.

- The past decade has seen some successful cases where **postal outlets** have been used to provide financial services to the rural poor on an impressive scale. In Brazil, Correios (the postal operator) and Bradesco's (the largest private retail bank) strategic partnership started in the early 2000s and resulted in 11 million new banking accounts opened over 10 years. In Morocco, Al Barid Bank (postal bank) was created in 2010 as a subsidiary of Poste Maroc. Since then, we understand that the postal bank opened close to 500,000 accounts per year and now has more than 6 million accounts. For those customers, the main difference lays in the ability to borrow from Al Barid Bank, something that they could not do before with Poste Maroc. Lower income banking has also started to attract the attention of commercial banks, which have discovered potential of lower-income banking and invested into dedicated units with adapted delivery models. Morocco is an interesting example to watch, with several banks launching targeted product packages for the under-served groups.

- For all key stakeholders involved in financial inclusion in MENA there is a pressing need to learn from peers and best practices in other world regions on practices that have broken cost, technology, and innovation barriers.
    - **On product innovation and youth** currently MFIs in Africa (Uganda, Burundi, and the Democratic Republic of the Congo), Asia (Mongolia), and Latin America (Dominican Republic) have been successful at implementing youth savings accounts on a widespread basis. For example, in Mongolia, XacBank has opened over 7,000 savings accounts for girls aged 14-24 and has over 18,900 girls enrolled in financial literacy trainings. We have one promising example in the region with Al-Amal Bank in Yemen offering loans, savings, and financial education to youth under 30. Much more is needed.

    - **With regards to financial literacy** the Brazil financial education project – which implemented financial education modules in 900 schools coupled with parent financial literacy workshops - has raised students' savings rates by 24% and increased the percentage of parents who track monthly expenses by 17%. The program is set to be rolled out nationally based on the positive results of these pilots. All financial regulators worked actively with the financial industry to improve consumer protection and financial literacy programs. Our MENA counterparts can learn from these examples.

  - Mobile banking is also opening immense opportunities for accessing the rural poor on a cost-sustainable basis. In Kenya, the M-PESA initiative, with over 16 million customers is an iconic story. The MENA region boasts over 250 million mobile subscriptions - 72% of population. Providing the regulatory and market incentives necessary to create a robust mobile-banking sector is an important challenge moving forward.

- Finally, one key success factor of any successful financial inclusion strategy is the capacity to bring together disparate efforts into a coordinated sum. The Moroccan authorities are launching a project that the World Bank will support to develop a comprehensive financial inclusion strategy, bringing together important initiatives under the Banque-Al-Maghrib, the Ministry of Finance, the Ministry of Education, the microcredit industry, banks, insurers, micro lenders and many others to chart a comprehensive roadmap to enhance financial access. The project also works to improve the legal, regulatory and institutional framework for the microfinance industry through building market infrastructure for MFIs and microenterprises and financial literacy trainings.

- In conclusion, the future of the MENA region lies in effectively creating economic and social opportunity for the region’s youth. A robust financial sector that supports innovation, growth, and inclusion is an important part of this process. I wish you the best over the next two days. I am sure that the sessions will provide important insights on how to tackle this challenge. From our end, we look forward leaning a lot from your respective experience, as the collective knowledge in this room is impressive.