Promoting Equitable Economic Growth through Inclusive Finance

Remarks by
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Distinguished Speakers,

Ladies and Gentlemen!

I am honoured and delighted to address this prestigious conference and I would like to express my gratitude to the Nepal Rastra Bank for inviting me to this event.

In my short remarks, I propose to share my thoughts on the need for promoting equitable economic growth among South Asian countries. Also, I would like to share SBP's vision on promoting inclusive economic growth in Pakistan through financial inclusion.

Ladies and Gentlemen!

In recent years, increasing globalization has enhanced the need for regional economic and financial cooperation among countries due to the cross boarder interdependencies and to take advantage of the emerging opportunities. The global financial crisis has pushed most of the emerging economies into most difficult economic challenges in recent history, in many ways;

First, the export-dependent emerging and developing economies were hit hardest as exports from the advanced economies dwindled due to the financial and economic meltdown causing loss of export revenues and reducing incomes in the South Asia and other emerging economies. Slower growth also translated into job loss, and lowering of wages, consumption, and welfare, therefore severely impacting poverty reduction and increasing social vulnerabilities.

Second, the dwindling export earnings and receding foreign capital inflows translated into foreign exchange market pressures, therefore, most of us were challenged while we endeavored to stabilize our foreign exchange markets due to weakening of exports earnings.

Third*,* the global crisis added to the volatility in international commodity prices thereby raising challenges for monetary management to curtail the inflationary pressures and expectations.

These common challenges must motivate us to strengthen our cooperation at regional level to help our nations sustain and contain future down side risks transmitting from advanced economies.

Ladies and Gentlemen!

The South Asian countries have strong fundamentals to their advantage. Let me highlight some of our strengths: South Asia is home to around 1.7 billion people, with the youth in majority, giving us positive population dynamics for both to grow fast and greater headroom in terms of debt carrying capacity to continue our economic expansion. The combined economy of South Asian region (SAARC) is 3rd largest in the world in the terms of GDP (PPP) after the United States and China and 8th largest in the terms of nominal GDP. Our financial sectors are still underdeveloped and have a low level of financial leverage, yet these are stable and have shown remarkable resilience against the global crisis. Also, low level of financial sector development reflected in low public and private sector debt relative to GDP indicates potential for continued growth in the financial sector.

Ladies and Gentlemen!

Financial sector development is a pre-requisite for promotion of economic growth. Therefore, I would like to share SBP's experience in promoting an inclusive financial sector in Pakistan. Financial access helps the low income households and small businesses better manage their affairs; it spurs local economic activity; and, at a macro-level, the depth of financial intermediation is associated with faster economic growth and less inequality. In the past 15 years, financial access for the low income people has moved from a niche issue pursued by few social entrepreneurs to an important global development agenda. During this time, regional variations notwithstanding, a field focused initially on microcredit broadened first to microfinance, then to access to finance, and most recently to financial inclusion.

Although a late starter in microfinance, Pakistan has kept pace with the changing global trends in policy and practice, and the State Bank of Pakistan's role has been pivotal in steering the sector with a strategic vision and pursuing a systemic approach in developing the microfinance sector on sound footings.

Pakistan was the first country in South Asia to have issued a Microfinance Law (Microfinance Institutions Ordinance 2001) which paved the way for creation of second tier banks catered to serve the low income segments of the society which were excluded from the mainstream commercial banks. This law widely contributed to the development of the sector and provided legislation for NGOs to transform into SBP supervised deposit taking to protect the depositors and to safeguard these institutions against political and other outside interferences.

As a regulator, SBP introduced specialized microfinance policy and regulatory framework pioneering global best practices. These regulations and supervisory mechanism strengthened the enabling environment to help MFBs develop viable business models to realize sustainable growth in microfinance. The success of microfinance regulations and market development in Pakistan is widely acknowledged by the international community. Our microfinance regulatory framework was ranked No. 1 in the world by the Economist Intelligence Unit (EIU) of the Economist Magazine in its reports in 2010 and 2011, and third best in its annual reports for 2012 and 2013.

In 2007, SBP developed a microfinance strategy to provide critical and long-term support to microfinance sector. The strategy implemented initiatives which led to a significant improvement in market infrastructure for microfinance. Today the sector has Microfinance specific CIB to address the problem of multiple borrowings and over indebtedness. A credit guarantee facility has been put in place which helped largely in building the confidence of commercial banks on the microfinance sector and has mobilized around Rs.13 billion from commercial bank and capital markets / retail investors for onward lending to around 650,000 micro borrowers. The facility has helped develop the market and introduced poor borrowers to mainstream financial institutions. This SBP facility changed the way donor funding was previously used to support microfinance institutions.

As the sector evolved, SBP strengthened the regulatory framework with enhanced focus on financial stability; State Bank revised the Minimum Capital Requirement (MCR) for Microfinance Banks (MFBs) in 2011 while allowing the existing MFBs to raise the prescribed minimum paid-up capital in a phased manner over the next three years. This step ensured that only such sponsors venture to establish MFBs which have adequate financial resources to meet the present and future capital requirements in face of the growing demand for investments in technology, intensive infrastructure, and information systems. In another significant development, SBP introduced a microenterprise loan category in the year 2012 to promote enterprise lending and improve asset creation in the country. Under this category, Microfinance Banks were able to lend up to Rs.500,000/- to microenterprises.

To overcome geographical barriers in financial inclusion and reduce costs, SBP issued branchless banking (BB) regulations in the year 2008. This initiative catalyzed important branchless banking deployments in the country and resultantly the retail network of microfinance has arisen overwhelmingly through agents and mobile phone channels.

Now let me share the impact of the aforesaid initiatives, most of which have taken place since 2007.

Seven years down the road, the sector is today catering to more than 3.24 million borrowers (as of Sep 2014) out of which MFBs' share is 1.155 million. Depositors have grown to 5.734 million in Dec 2014, with average yearly growth of 69%. Now average loan size has increased from Rs. 10,000 in Dec 2007 to Rs 32,000 in Dec 2014 promising asset creation whereas previously some critics found the low average loan size meant for supporting consumption smoothening. This growth has led to improved ROE from negative 33.2% in Dec 2007 to positive 7.2% in Dec 2013, fetching both domestic and foreign equity injections in the industry.

In area of branchless banking, eight fully-functional models have emerged. Easypaisa is the third largest branchless banking model in the world. With innovative use of technology and partnerships, these models have started changing the economics of 'banking with the poor'. Pakistan is experiencing phenomenal growth in the number of branchless banking transactions which have been undertaken at thousands of small shops situated in the streets and local markets across the country to serve common people at convenient time. Average monthly volume of such transactions is estimated to be around 24 million. Average size of these transactions is only Rs.5000 which shows that technological solutions are helping to reach out the millions of previously financially excluded segments of our society.

With strong commitment of the Government, SBP's strategic vision, sound legal and regulatory foundations, robust market infrastructure, technological and institutional innovations, and private sector dynamism, the trajectory of microfinance is set for achieving the long term vision of "financial inclusion for all".

In closing, I would like to say that despite very strong economic reasons for enhancing financial cooperation among the South Asian countries, it will not be easy for the many of us to form a consensus on long-term visions requiring common understanding and efforts. This is because our countries differ in their development levels, their cultures and their languages, and suffering from presence of various historical and political conflicts among them. However, we may begin the process towards financial cooperation and integration, which is a longer term goal, by engaging more actively in research and discussions, in order to arrive at a long-term vision of regional financial cooperation that the South Asian countries can share, and to increase our understanding of that vision. I believe this conference is one such effort and we must continue the dialogue in our bilateral forums and similar events in future.

Thank you all!

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