SECURITIES AND EXCHANGE COMMISSION, NIGERIA

DIGITIZATION, DISRUPTION AND FINANCIAL INCLUSION: Digital Finance as an Essential Tool for enhancing Financial Inclusion

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PROTOCOL - Good morning, distinguished guests, ladies and gentlemen.

It is a great pleasure to be here with you at the 2018 NSE Market Data Day. Let me start-off by thanking the CEO of the NSE, Mr. Oscar Onyema for inviting me to speak before you today, and Mrs. Tinuke Awe and Mr. Bola Adeeko for their warm welcome.

I am delighted to be in the company of distinguished guests and participants from all over the country to discuss such an important topic. I have fixed an addendum to it, however, to read — **DIGITIZATION, DISRUPTION AND FINANCIAL INCLUSION: Digital Finance as an Essential Tool for enhancing Financial Inclusion**.

As the great Mexican writer, Carlos Fuentes once said: "*Culture consists of connections, not separations*." I make bold to add that a great culture also consists of inclusion.

Together, with the CBN and other sister regulatory agencies, SEC has made important contributions to the progress of Financial Inclusion through valuable guidance and active involvement in the National Financial Strategy (NFS) aimed at reducing adult exclusion from financial services to 20% by 2020. Thanks to our collaborative efforts and to strong national commitments, financial inclusion has advanced dramatically in Nigeria. Between 2012 when the NFS was launched and now, various initiatives and sensitization programmes have been and are being implemented.

Yet, about 2 billion individuals and 200 million businesses remain excluded from the financial system—more than 40% of the world's adults *(World Bank's Global Financial Inclusion – Global Findex*). Most of these people live primarily in developing countries and in rural areas. Women, remain under-represented in the financial system with a 9% gender gap in developing countries. For MSMEs who account for more than 90% of global enterprises, and provide close to 50% of all formal jobs in developing economies, approximately 40% of those do not have access to financial services yet they need to grow, succeed and employ more people.

What is also worthy of mention is that financial exclusion is a universal issue. Within the EU alone, 58 million people do not have access to a basic account. In the US, 7% of households are totally unbanked – and that is about 16 million adults. Between 2010-2017, about 1.2 billion people *(Alliance for Financial Inclusion AFI)* gained access to an account for the first time. Much of the progress was related to the impact of financial technology.

Although the challenge of financial inclusion is significant, we have a powerful set of tools to drive progress. Among the most promising is digital finance.

Today I would like to share my thoughts in seven key areas:
(i) Why financial inclusion is important, especially for women and the unserved;
(ii) The dynamics of Digital Finance;

(iii) The intrinsic benefits of digitization in today's Financial Sector;

(iv) The disruptive nature of Digitization of Finance;

(v) The future of FinTech for Financial Inclusion;

(vi) The Bali FinTech Agenda;

(vii) The nexus between digital finance and financial inclusion – the essential role of digital finance in enhancing financial inclusion.

1.0 FINANCIAL INCLUSION: What have we learnt so far? Why is financial inclusion important, especially for women and the unserved?

Financial inclusion (which may be defined as — broad access to and delivery of financial services at an affordable cost to all segments of the society) — is distinctly moving up the reform agenda, both in individual countries and globally. To date, more than 60 governments across the world have set financial inclusion as a formal target and squarely as a key objective. It is also part of the United Nations' Sustainable Development Goals (SDGs).

Financial inclusion helps people become financially independent and economically self-sufficient. Financial inclusion helps underserved populations increase their productivity and incomes. The World Bank, for example, has set a goal of ensuring universal access to financial services by 2020.

Financial inclusion has gained prominence as a global policy agenda as it complements other policy initiatives on reducing poverty, addressing inequality, and promoting financial stability and integrity. As you all know, the **Hamburg Action Plan** sets out the G20's strategy for achieving strong, sustainable, balanced and inclusive growth. Not surprisingly, the third priority action of the Hamburg Action Plan is to "*Promote Financial Inclusion*". This buttresses the critical role financial inclusion plays in global development. A financially included society will provide increased access to finance, especially for women, help support sustainable growth--and will create millions more jobs.

For corporate entities, especially small and new ones, access to finance can encourage investment in new and more productive technologies. It can also help them expand in terms of size and complexity of operations.

There is also an important gender dimension involved. In March 2018, the IMF published a study on Nigeria showing that reducing gender inequality could increase real GDP growth by an average of **1.25%** points annually. Similarly, an IMF's staff research investigated the forces that propel access to financial services for women. The findings show that women who live in countries with stronger protection against harassment are more likely to open a bank account, borrow and save, and make greater use of financial services such as mobile payments. Financial access for the average woman living in an emerging market or developing country is almost 16% deeper – that is, financial inclusion scores are higher – when legal protection is granted. For the average sub-Saharan African woman, the figure is almost 25% higher.

Increased financial access means a greater rate of economic activity among women, especially as entrepreneurs, which translates into more equal income distribution, higher economic growth and productivity.

2.0 THE DYNAMICS OF DIGITAL FINANCE

Digital finance is financial services delivered through mobile phones, personal computers, the internet or cards linked to a reliable digital payment system. A McKinsey report identified digital finance as "*financial services delivered via mobile phones, the internet or cards*". Digital finance encompasses a multitude of new financial products, businesses, software, and innovative forms of customer communication and interaction - delivered by FinTech companies and innovative financial service providers. It allows us to significantly lower costs of financial services for low-income populations and to reach geographically isolated communities in a way that was hitherto unthinkable. The goal of financial services made available via digital platforms is to contribute to poverty reduction and to contribute to the financial inclusion objectives of developing economies. In China, where a traditional and not overly efficient financial system became one of the world's most digitized financial systems, the effect of digital finance led to the *single greatest decrease in poverty in world history.* These developments are part of a global phenomenon known as financial technology or 'FinTech' which is *the interaction between finance and technology.*

3.0 THE INTRINSIC BENEFITS OF DIGITIZATION IN TODAY'S FINANCIAL SECTOR

The influence of FinTech on emerging markets cannot be overemphasized in providing convenient, cheaper, safer and easy-to-use customer centric products and services. Because of the social impact that can be generated through financial technology in terms of ensuring access to financial services and products for the unbanked/unserved, i.e. *democratizing finance*; FinTech can become the engine that enables access to those in need of financial services.

Most emerging market economies have limited financial system infrastructure. Capital markets, to the extent they exist, and banks alike rely on legacy technology, which are not accessible to poor rural populations. It is precisely these dynamics that have enabled new technologies to develop in service of the poor, and FinTech innovators are the main drivers of this revolution, in some cases leapfrogging the traditional industry with new services that provide access to the previously unserved.

FinTech start-ups are flooding the market with **convenient, safe** and **easy-to-use customer centric products and services**. FinTechs are reducing the multi-billion Naira monopolies of Nigerian banks and financial institutions with bespoke financial services and products.

Let us look at some other benefits of Digital Finance. It could lead to expansion of financial services to non-financial sectors, and the expansion of basic services to individuals since nearly 50% of people in the developing world already own a mobile phone *(Alliance for Financial Inclusion AFI)*. The mobile phone is arguably the most powerful instrument of development in history.

Digital finance promises to boost the gross domestic product (GDP) of digitalized economies by providing convenient access to diverse range of financial products and services (and credit facilities) for individuals as well as small, medium and large businesses, which can boost aggregate expenditure thereby improving GDP levels.

Other benefits of digital finance to customers includes greater control of customers' personal finance, quick financial decision-making, and the ability to make and receive payments within seconds. However, the expected benefits of digital finance can only be fully realized if the cost of providing digital financial services is negligible or zero.

4.0 THE DISRUPTIVE NATURE OF DIGITIZATION OF FINANCE

It is however important to understand the risks and disruptions that come with these digital innovations. For example, the technology behind crypto-currencies, including blockchain, offer exciting advancements that are typically built in a decentralized way and without the need for a central bank. This gives crypto-asset transactions an element of anonymity, much like cash transactions. This could result in a potentially major new vehicle which could be used for money laundering and the financing of terrorism.

Questions have been raised from various quarters on whether digital finance triggers disruption in the financial landscape and whether this can raise concerns about financial stability. Central banks and other regulators have been enjoined to carefully monitor this trend so as to contain the risks and reap the benefits of digital innovation.

Disruptive innovations such as blockchain technology, biometric identification, cloud computing, and the use of big data are revolutionizing the collection and processing of financial information, the way we save and borrow, how we intermediate financial resources, the channels we use to pay for goods and services, and how we engage in money transfers between wallets and accounts, domestically and across borders. FinTechs are offering tech-enabled solutions that can better address customer needs and preferences by offering enhanced accessibility, convenience and tailored products. Let us look at some ways in which FinTech is changing the game for the financial services industry:

1. ***Chatbots for customer service*** – Chatbots are bits of software that use natural language processing and machine learning to continuously learn from human interactions. This is becoming a popular tool for banks to streamline customer-facing interactions such as handling queries. The use of these chatbots not only improves customer satisfaction and reduces costs but also frees agents in call centres to focus on value addition.

2. Machine learning and Artificial Intelligence (AI) for fraud detection – Identifying fraudulent transactions is the main goal of anti-money laundering departments. For most market participants, this involves a combination of software and people. Machine learning algorithms can leverage historical records to determine patterns and predict the possibility of fraud/attacks before they occur, reducing manual effort by nearly 50%.

3. Omni-channel banking and obsolescence of bank branches – As banking shifts from being a branch-specific activity to one that permeates all digital channels (mobile, social and online), the importance of having several brick-and-mortar bank offices decreases. In fact, studies show that the adoption of omni-channel banking is driving several banks to reduce the number and size of their branch offices. In the EU alone, nearly 9100 bank branches were shut down by the end of 2016 owing to higher adoption of electronic payments and online/mobile banking.

4. Biometrics for stronger security – There is a lot of interest in finding ways to use biometrics such as vocal patterns, thumbprints, and facial recognition, to add an extra layer of authentication for transactions. Biometrics promotes usability by enabling quick authentication, avoiding the frustration that comes with remembering passwords.

5. Blockchain for digital transactions – Cryptocurrencies are taking the banking world by storm by providing users with faster and cheaper ways to transact. The distributed ledger system of blockchain leverages stringent controls enabling smart contracts and auditable data. By building inherent trust, blockchain provides the perfect trading platform for securities exchanges. It does this by ensuring transparency, thereby minimising risk, human errors and transactional fees.

Disruption can enhance better financial service rendering

Mobility, smartphones and online payment apps coupled with the demand for secure and personalized banking experiences are giving new impetus to the adoption of FinTech within the financial services industry, making it imperative for traditional banks to make strategic investments in innovative technologies. This will help them upgrade their operations and deliver seamless services for higher customer retention.

5.0 THE FUTURE OF FINTECH FOR FINANCIAL INCLUSION

The Future of FinTech in enhancing Financial Inclusion is therefore defined in the following significant areas:

1) Technology is dominating every industry, so there are greater prospects for enhancing financial inclusion. The global FinTech sector is growing at an incredible rate, enjoying 200% year-on-year growth in funding and attracting $12.2 billion in growth capital in 2014 alone.
2) The surface has barely been scratched - While it is clear that FinTech has already made huge inroads into many aspects of the financial industry, what is perhaps even clearer is that the surface has barely been scratched in relation to what FinTech can do in the future. Emerging markets will experience quite rapid growth in financial services provision in substantially less a time than it took developed markets to achieve. **We can probably assume that financial services over the next 10 years will experience a higher degree of change than in the last 100 years.**
3) Regulation - Regulatory compliance is a prerequisite for success for FinTech companies worldwide. Compliance with legal financial regulations is not optimal, but mandatory. RegTech offers many of the same benefits to regulators as it does to financial institutions. Additionally, customers' awareness that their data is prone to cyber-attacks can make customers loose trust in digital channels, or they may avoid using digital channels to perform important financial transactions until strong customer protection frameworks are in place. **The existence of strong consumer protection frameworks which apply to digital financial services will be critical in building the necessary trust and confidence that customers need.**
4) FinTech is targeting Millennials using AI - Several FinTech companies understand how conventional banking and investment avenues are not attractive to many millennials. Millennials will shape the future of asset management: by 2030, Millennials are expected to control as much as $20trillion of wealth globally. To leverage on the gains of financial inclusion for the next generation, specific initiatives should be targeted at educating millennials in Nigeria and catching them young. The SEC in collaboration with the NERDC is already working towards infusing capital market studies into school curriculum.

5) The financial services sector is at the nascent stage of digital disruption. Its main functions remain the same today as yesterday – people use financial services to *exchange money, to save or invest, to finance, or to insure against risk.* All financial services are a response to these four basic needs. New technologies are delivering these financial solutions in convenient, cheaper and faster ways, which will enhance financial inclusion.
6) Many opportunities for FinTech are yet to be explored – By 2020, over 1 million payment transactions will take place every minute in the world. In that same year, investable assets will reach $200 trillion. The potentials are huge.

6.0 THE BALI FINTECH AGENDA

Just last week, we were in Bali, Indonesia for the IMF/World Bank Annual Meeting, where a paper intended to guide policymakers around the world in their handling of the rise of Fintech was released. The paper, called the ***Bali Fintech Agenda***, outlines 12 considerations that the IMF, the World Bank and governments can keep in mind when designing policies and regulations that can maximize the benefits of Fintech while keeping financial systems sound and ensuring inclusive growth.

Those "elements" include Fostering Fintech to Promote Financial Inclusion and Develop Financial Markets; Adapting Regulatory Framework for orderly Development and Stability of the Financial System; and Safeguarding the Integrity of Financial Systems. Let me dwell briefly on these three (3) considerations:

CONSIDERATION IV. Foster Fintech to Promote Financial Inclusion and Develop Financial Markets by overcoming challenges related to reach, customer information, and commercial viability, and by improving infrastructure. Examples include expanding access to finance while reducing costs, providing new ways to raise funding, enabling new information services to assess risks, and spurring new businesses.

CONSIDERATION VI. Adapt Regulatory Framework and Supervisory Practices for Orderly Development and Stability of the Financial System and facilitate the safe entry of new products, activities, and intermediaries; sustain trust and confidence; and respond to risks. Existing regulatory frameworks might address many FinTech risks. Existing regulatory approaches may need to be supplemented to address FinTech driven changes in the financial landscape that may arise from new companies, products, and activities that lie outside the current regulatory perimeter.

At the SEC, we have set up an Assessment Form with a view to developing a Regulatory Sandbox that will offer a 'safe space' in which start-ups and other businesses can test innovative products, services, business models and delivery mechanisms relating to the capital market in a live environment without immediately satisfying all the necessary regulatory requirements. This way, we are ensuring that regulation is made in such a way that it does not stand in the way of innovation and its overarching benefit of developing the Nigerian capital market.

CONSIDERATION VII. Safeguard the Integrity of Financial Systems by identifying, understanding, assessing, and mitigating the risks of criminal misuse of FinTech. Country responses have varied considerably; but, in all cases, it is important to strengthen AML/CFT compliance and monitoring, including by using technology (RegTech and SupTech solutions) to support regulatory compliance and supervision. There is a need to ensure that Pro-Financial Inclusion policies are in line with the traditional mandates of financial regulation: *stability and integrity of the financial system, and consumer protection.*

7.0 THE NEXUS BETWEEN DIGITAL FINANCE AND FINANCIAL INCLUSION – The Essential Role of Digital Finance in enhancing Financial Inclusion.

The use of digital tools creates the potential to make financial services available to a wider range of consumers and enterprises, promoting financial inclusion and the affordability of financial services.

The major setback many experts have cited as the bane of financial inclusion in Nigeria is the apparent distrust for financial services institutions and low literacy levels among Nigerians. Credit must be given to the Federal Ministry of Finance and the Central Bank of Nigeria for measures they have put in place to raise the bar on financial literacy in the country as a panacea to driving financial inclusion.

So what else needs to be done? - One element that readily comes to mind is innovation and technology. This perhaps must be why many commercial banks have been remodeling their operational strategies to deemphasize focus on branch network expansion and steadily moving towards digitization and mobile solutions. According to a 2016 McKinsey Global Institute report, Digital Finance could boost the GDP of emerging economies by $3.7 trillion by 2025 and benefit numerous stakeholders.

Equity crowdfunding portals are disrupting the venture capital (VC) market by enabling investments directly into private company start-ups, and peer-to-peer (P2P) lending platforms are disrupting the banking market by facilitating lending to small and medium-sized enterprises (SMEs). The growth potential is tremendous. Goldman Sachs' 2015 report entitled 'Socialization of Finance' called crowdfunding **"potentially the most disruption of all the new models of finance".** The World Bank estimates that crowdfunding investments in developing countries alone could reach $96billion a year by 2025. According to the World Bank, the market potential in Africa for crowdfunding would reach $2.5billion by 2025.

As conditions for accessing finance are deemed too stringent for many start-ups, the necessity for **equity-based crowdfunding in Nigeria is growing immensely.** It provides a cheaper alternative source of financing which obviates the need to provide collateral security.

Looking ahead, technologies like APIs and Blockchain can enable the development of new modes of recording and sharing data across various business value chains, thereby reducing information asymmetries. Fintech is opening the door to new mechanisms for companies, including MSMEs, to raise funding directly from investors, such as crowdfunding and market-placed lending. In tandem, it is supporting the development of key information services that allow investors to assess the risks of their investments, such as creditscoring or credit rating mechanisms. It is also creating new channels for the distribution of capital markets products—such as mutual-fund supermarkets. At the same time, it is allowing customers to access other support services— such as investment advice (Robo Advisory services)—at a lower cost.

As of 2017, 80% of adults in India had an account. Female bank agents with mobile devices in open-air markets in Nigeria are also scaling up potentials. In this case, women are enabled through a tiered KYC system to setup accounts without documentation or minimum balance requirements, and to make deposits and withdrawals without having to leave their stalls. *Think of a cocoa farming cooperative society in Sikoloba, Ondo State that sells cocoa at the highest price to an industrialist in Amsterdam, Netherlands,* *without any middlemen/intermediaries!* Digital channels deployed by banks, telecom companies, and other providers have enabled millions of people with mobile phones to access digital finance over recent years and have connected them to not just payment services but also to savings, insurance, investment, and credit. Moreover, mobile money has enabled access to essential services like water and electricity (PHCN) through pay-as-you-go services.

Excessive KYC requirements can hinder financial inclusion as providers might find it too onerous to deal with the less-privileged or financial illiterates. The ideal method is to design KYC Due Diligence regime that is adequate to the task of maintaining financial integrity, yet do not create unnecessary barriers to financial inclusion. A carefully implemented Risk-based approach has to be adopted in achieving financial integrity for a fully financially inclusive market.

Partnership is key in promoting Financial Inclusion. This partnership should also include investors, policymakers and FinTechs, if we want to reap the full benefits of FinTech, cooperation is key. No one can do it alone. Some countries are establishing a forum or task force for public- and private-sector players to jointly explore leveraging FinTech for financial inclusion; We are no different in the Nigerian Capital Market – At the second quarterly capital market committee meeting of 2018 in August, we constituted a market-wide FinTech Committee to develop a roadmap for FinTech in the Nigerian Capital Market.

In addition, ensuring a level playing field for FinTech startups (even though they might cause distortion unintentionally) and market operators by ensuring that the regulatory regime does not favour some service providers over others, is key.

So for us to fully harness the power of technology and digital finance to drive financial inclusion in a safe and responsible way, we must adopt a customer-centric approach that puts client needs and wants at the center of our work. Hard-to-reach segments such as women, smallholder farmers, and MSMEs can benefit in particular from digital financial products that are tailored to their mode of operation.

Second, we need to better prepare and empower customers—particularly low-income people who are already living on the edge and may not be digitally literate. We can leverage technology to increase people's financial skills by, for example, designing online programs or developing apps or voice messages that can help poor people manage their money better.

CONCLUSION

Let me conclude. I could not help but notice that the core values of the NSE are captured in the eye-catching acronym *AIF – Ambition, Inclusive and Fair* which help brand amongst others, the many advantages of Nigeria as an investment destination to the world. It suggests that the NSE is poised to *contribute to* and *share even more insights* in the collaborative quest to make the Nigerian economy, a financially inclusive one.

Ladies and gentlemen, despite clear evidence of its benefits to individuals and society as a whole, financial inclusion is often proceeding on an isolated track—more social approach than digitized. It is critical that we avoid such a "*silo mentality*". Financial inclusion is an integral part of inclusive growth strategies and should be closely integrated into macroeconomic and financial policies, using digitized finance mechanisms.

When financial systems become more inclusive, they help broaden financial markets and make policies more effective. By bringing more sections of the population into the formal sector, the effects of market-deepening initiatives are better expanded. We have tried in our efforts, but significant work is needed to assist the almost 2 billion people and over 200 million businesses that remain financially excluded.

At the end of the day, when our economy is more inclusive, the gains are less elusive. The market is deeper, vibrant, more effective, and a better future—for everyone—is more likely. I enjoin us all to be committed to the agenda. It is time to make all the difference and make it a reality.

Thank you.

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