

Policies & Regulations for Expanding e-banking to the Poor

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Banking for the Poor

Innovations in Information and Communication Technologies (ICT) have brought tremendous change to the way people work, interact and conduct their daily lives. ICT has transformed the global economy and has heralded a new and dynamic 'information society'. The financial sector as a key component of the global economy has also been set in motion by the ICT revolution. This is resulting in new delivery channels for banking products, and services, which include ATM's, Internet banking, telebanking, PC banking and various others. Electronic banking has changed the way the banking industry does business by forcing the industry to consider non-traditional channels of delivering services to customers. No doubt in the future banking environment will be more paperless and will overcome the traditional barriers of distance and geographic boundaries. Electronic banking promises to be more efficient by providing low cost operations, and access, to financial services

remotely. E-banking can provide services to large populations without much difficulty. Hence e-banking is well suited for microfinance that is intended for the poor segment of the population, who has little or no access to banking services. Despite all of the opportunities and convenience created by e-banking and e-commerce, development of a regulatory framework, for e-banking is a formidable challenge. Electronic transactions cannot remain free of regulations. With the global financial sector becoming heavily dependent on technology, governments are framing policies, procedures, and legal framework, within which business is conducted smoothly in a secure and transparent manner. E-banking has the immense potential to expand the outreach of microfinance services to large segments of the population. This is provided the legal systems and policies regarding electronic transactions are appropriately framed, where e-banking flourishes and technology brings substantial improvement to the business.

Specifications for Electronic Banking & Commerce:

Access to financial services has proved to be an effective tool to bring qualitative change in the lives of the disadvantaged population. Information and Communication Technology (ICT) has a critical role in the quest of making financial services accessible and cost effective. The global financial systems adoption of ICT has resulted in a high level of innovation in products and delivery of financial services. The developing countries, like those in South Asia have yet to arm themselves to receive the benefits of the arising opportunities and the benefits that participation in the global markets provides. E-Banking and e-transactions are the backbone of e-economies which have proved to be a powerful instrument to increase productivity, generate economic growth and which consequently improves the people's quality of living.

The use of e-banking by the microfinance sector has great opportunities in scaling-up the services while keeping the costs at a minimal level. The various factors that are affecting the adoption of e-Banking and e-commerce, particularly in the developing countries can be described in the following three layers:

1. Infrastructure Layer:

The two main types of infrastructure that are important for any type of digital intervention are:

i) Telecommunication and ii) Power

These infrastructures together with buildings, electronic devices and machines make it possible to host a wide range of electronic services such as transmission of voice, data and image. A better infrastructural layer can ensure advance digital services and access to local, regional and global resources in a cost effective manner. Countries can then integrate into the networked economies of the world which provides great opportunities not only to economic and technological fronts but also in social and political areas.

Policies and Regulations:

The setting-up and expansion of a high quality infrastructure can be achieved by a dynamic cooperation between the public and private sector. Large investments need to be attracted from the private sector, while the government provides an investment friendly environment to facilitate private sector investment, while keeping the public interests intact. Governments have to decide on major policy changes that can create opportunities for the private sector to invest and improve the infrastructure. The following are some of the policy steps that have worked in a number of countries, including Pakistan.

- Creation of independent regulatory body with independent financial power

- Deregulation of the sector
- Opening of the telecom market for investment
- Discouraging monopolies (i.e. Anti-Trust) and creating a culture of healthy competition by reducing taxes, royalties, license fees and minimized other entry barriers to the market.
- Minimizing tariffs on import of technologies and related equipments
- Transparent and rational pricing policy

2. Service Layer

The service level includes service structures, business models, systems and standards related to economics, social and transactional activities and a high dependency on infrastructure. Hence standardized and reliable infrastructure can insure efficient and effective services. Similar to other sectors, technology has a vital role in introducing new ways of doing business by the financial sector. An appropriate policy and regulatory environment is of immense importance for introducing and expanding electronic channels such as e-banking. Thus related risks are minimized without inhibiting innovation and competition. Some of the key areas of regulation are:

- Recognition of electronic document and electronic communication
- Regulation on unauthorized access & information breaches
- User identity and authentication policies and digital signature
- Web site certifications
- Information security
- Regulation regarding data fraud, offences and disputes
- Unauthorized access to the bank's central computer system and database.

3. Application Layer

The application level pertains to the system components, software and items that are used by the various service channels to carryout business activities. Software applications, database management systems, MIS tools, data, and text are included within the application level. The e-economy is largely based on the internet with the main channel for e-banking also being internet based. Regulators and policy makers are facing greater challenges on the fronts of e-banking and e-commerce due to the borderless and open architecture of the internet and electronic world. Hence apart from regional interventions, global cooperation is of equal importance. Following are the three main pillars that can facilitate the use of ICT, e-

banking and e-commerce in developing societies:

- i. Creating a favourable environment, fostering innovation in ICT and ensuring their accessibility.
- ii. Developing skilled human resource capable to develop, manage and support ICT tools and applications
- iii. Creating capacity and awareness among the public in general and the user in particular about the use and management of systems and technology.

Policy and regulations at this level should address the following areas:

- Promotion of research & development
- Awareness, accessibility and affordability to information and knowledge
- Creating a culture of transparent and qualitative information
- Fair marketing and contracts
- Capacity building of the public
- Integration of ICT in to mass education
- Promotion of software houses and libraries
- Basic computers and English language literacy for the public

- Creating trust in e-transactions

Pakistan - ICT Developments and its Impact:

During the past couple of year's telecom and IT sectors in Pakistan have shown an unprecedented growth, which has a positive flow on effect on the financial sector which has also flourished. The main catalysts behind these developments have been the various policies introduced by the government from time to time which include the deregulation policy, establishment of the privatization commission, introduction of competition and reductions in tax rates.

The teledensity in the country was 4.3% in 2003 which has now grown to 22%. During 2005 the growth rate for cellular mobile subscribers has been 182% and currently their number has reached 25 million. Similarly this sector has also attracted private and foreign investment. During the year 2004-05, 32% of the direct foreign investment has been in the telecom sector.

The financial sector has benefited from the developments made in the telecom and IT sector. Most of the commercial banks are now on a single switch; this provides convenience to the customers as they are capable of accessing their accounts on any of the banks that are on the link infrastructure. These developments have also enabled the banks to lower their transaction costs and expand their market into new horizons.

Most of the developments in the financial sector have been made in the urban areas. Hence e-banking and other new e-channels have provided choice and convenience to middle and upper income groups. This group are the main target of commercial banks and other commercial institutions. Unlike the rural sector that makes up 65-70% of the population, and who have been largely ignored by the commercial banks and other commercial institutions despite the governments interest in uplifting rural areas. Reaching out to the huge rural population through financial services is a great challenge. To a large extent this challenge can be met through advancements in technology and innovative delivery mechanisms like e-banking and e-commerce. E-banking and e-commerce facilities can be extended to the rural areas if appropriate infrastructure is implemented.

Evolution of e-Banking in Pakistan:

The financial sector in Pakistan comprises of banking and non-banking institutions. The financial sector of the country has mostly been dominated by public sector banks and financial institution till 1991, when the government opened up banking to the private sector. Liberalization and financial reforms created a wave of competition and within a short span of time the banking industry has expanded tremendously.

Pakistan has been among the late entrants into e-banking. The first ATM switch was setup in 1999 and in 2000 Internet Banking was introduced. Focus towards electronic banking in Pakistan started in the year 2002 when the State Bank of Pakistan (SBP) started providing serious attention towards the promotion of e-banking. By directing the banks to provide e-banking services to their customers and interconnecting their switches. Within a year, the majority of the banks have made substantial progress in conducting e-Banking services. For example, ATM cards could be used on most of the Banks ATMs; banks implemented utility bill payments systems as well as the introduction of mobile ATMs. A large portion of the transactions taking place within the banking system has been predominately cash and cheques. However there has been tremendous growth in the electronic transaction during the past year.

Currently there are networks of more than 1000 ATM's all over the country, and the number of electronic transactions has grown to 3 million a month. Banks are providing electronic account management and phone-banking services to their clients. A recent addition in electronic transactions has been allowing clients to access their accounts to do fund transfers and remittances from any ATM from the participating bank. The banking systems in Pakistan are taking advantage of the global

network of service providers and have obtained connectivity to SWIFT.

The banking sector has made substantial progress on the fronts of e-Banking and e-commerce. However microfinance has more or less remained isolated from reaping the benefits of the digital world. NGOs have been the main drivers of microfinance sector in the Pakistan for quite some time. Until 2000, when the Government established the Khushhali Bank and then in 2001 introduced Microfinance Ordinance that paved the way for establishing microfinance banks in the country. The First MicroFinanceBank Ltd (FMFB) was the first microfinance bank established and licensed under the Microfinance Ordinance in the private sector. The number of microfinance banks has risen to 6 (i.e. one in the public sector and 5 in private sector) since the opening of the Microfinance Banking sector, these banks are:

1. The First MicroFinanceBank Ltd
2. Network Microfinance Bank Ltd
3. Rosgar MicroFinace Bak Ltd
4. Tameer Microfinance Bank Ltd
5. Pak Oman Microfinance Bank Lts
6. Khushhali Bank (i.e. in Public sector established under special ordinance)

The use of ICT has also picked up pace in the microfinance sector with the launch of formal microfinance sector in the country. Most of the

microfinance banks have made reasonable investments in implementing technology infrastructure at their end, although it is difficult to make judgements on the efficiency of these systems.

E-banking and e-commerce is very much on the agenda of the microfinance banks. A couple of microfinance banks have already introduced e-channels for delivery of their product and services, though the results are mixed. Constraints being faced by the MFIs include; availability and cost of appropriate ICT infrastructure, particularly in rural areas, policies and regulations by the government and the State Bank of Pakistan (SBP), socio-economic and political environment of the country, and capacity of the organizations as well as the target group in making use of digital technologies. However with all of these difficulties, there still remains a great potential and opportunity for e-microfinance.

Policy and Regulation Models for e-banking & e-Commerce:

The invention of the internet has opened a new paradigm of doing business and communication. This new era where networks comprise of telecommunication, computing, audio visual, text and so many others, creates confusion about where the boundary of one industry ends and the other starts. It presents a great challenge for governments in introducing policy and

regulations. Countries refer to others who have come-up with tangible results to see what best suits their regulatory, economic and political environments. Each country will have to assess their current situations as they decide on how to change ICT and telecommunications regulations to meet their changing needs. A number of states as well as international organizations including WTO, UN and EU have made substantial developments in coming up with policies and regulations on e-commerce, e-banking, e-transactions and other ICT based activities. Following are some of the policies and regulations that can be of great assistance when drafting policies and regulations regarding e-commerce and e-banking:

- WTO Principles on regulatory framework for basic telecommunications regulation
- European Union directives on telecommunication, information & e-com
- The US interconnect Statute
- United Nations Commission on International Trade Law (UNCITRAL)
- UNCITRAL Model law on electronic signatures

Conclusion:

New and innovative channels such as banking and e-commerce have great potential and promise to extend a wide range of financial service to the poor. The “e” has changed the shape of financial services; hence this poses a great challenge to the policy makers and regulators in the financial sector. For the poor to benefit from ICT, there is a need for public private partnership vis-à-vis policy intervention and investment that embraces infrastructure, service, application, technology and human resource.

The other important aspect is about bringing the disadvantaged population into the realm of mainstream economic development by extending the infrastructural and social service facilities to rural and remote areas. The availability of infrastructure and services can act as a catalyst and a change agent in attracting investment as well as technology, enabling the disadvantaged population to access financial as well as other social services.

Policies that can have a great impact in facilitating e-banking and e-com services to the poor should be directed towards

- Attracting private sector investment in ICT
- Facilitate accessibility and cost effectiveness of ICT services and equipment

- Computer literacy and general awareness
- Transaction security and consumer protection and
- Conflict of laws

United Nations Commission on International Trade Law (UNCTRAL)

UNCITRAL Model law on electronic signatures

To keep pace with the advancements in technology and to minimize the digital divide, developing countries need to put ICT on their priorities list, follow policies of creating conducive environment for technological innovation and its effective use in all sectors including the financial sector. A number of countries and organizations have already produced better results in making effective use of e-services hence e-beginners can benefit from their work and experience.

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