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# Conduct Supervision in Challenging Times – towards an RDFE approach.

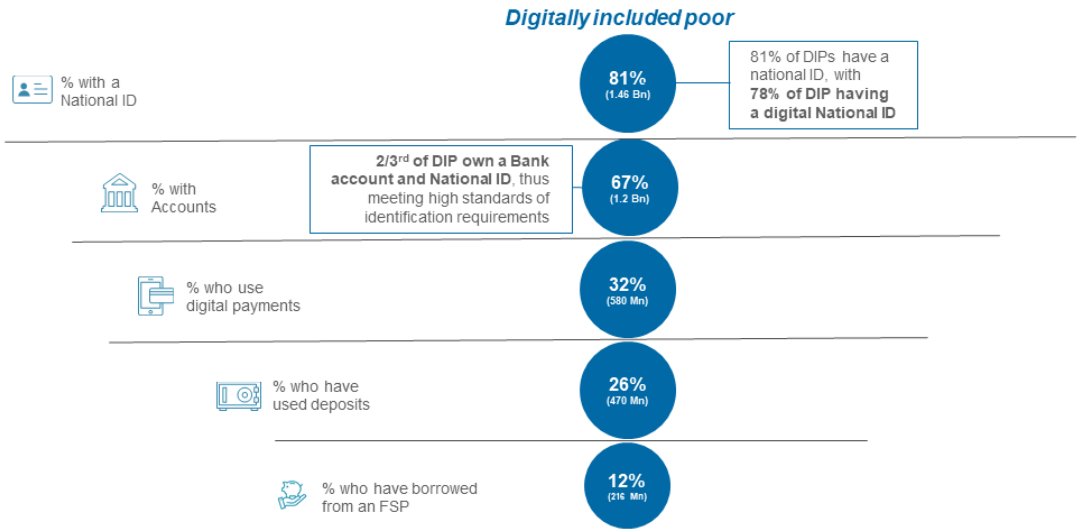
**Gerhard Coetzee – CGAP Policy Lead**

22 November 2023

# Increased digitalization and rapid innovations are fundamentally transforming the financial sector …

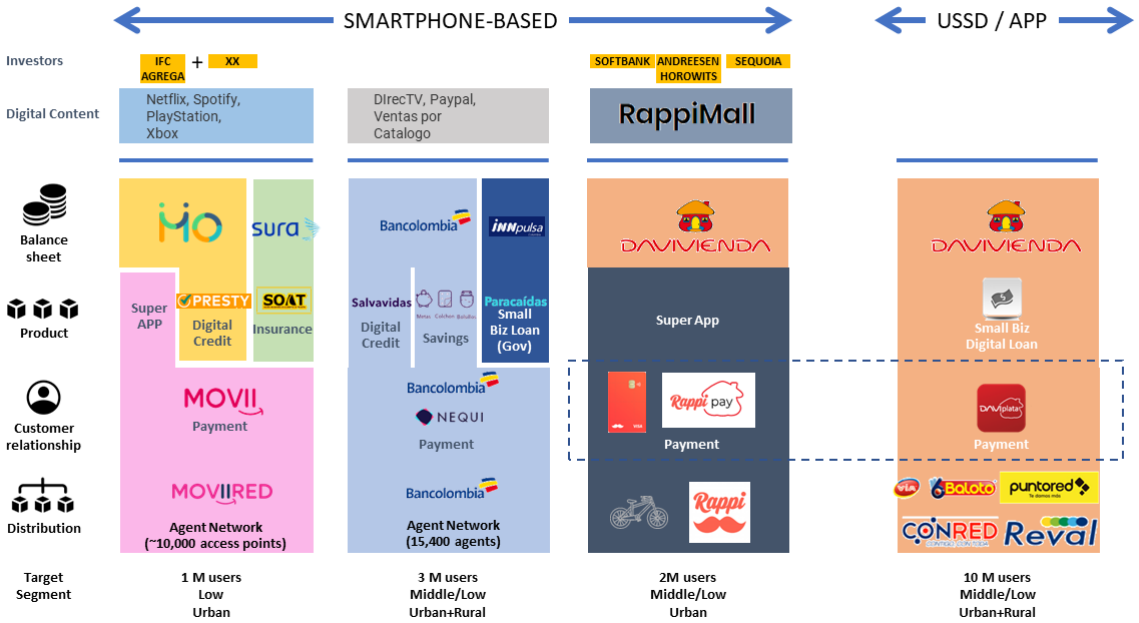
## Rapidly Growing Digital Data Trails

73% of low-income individuals are digitally included




## Modularization of Financial Markets

### Colombia – Customer-facing applications

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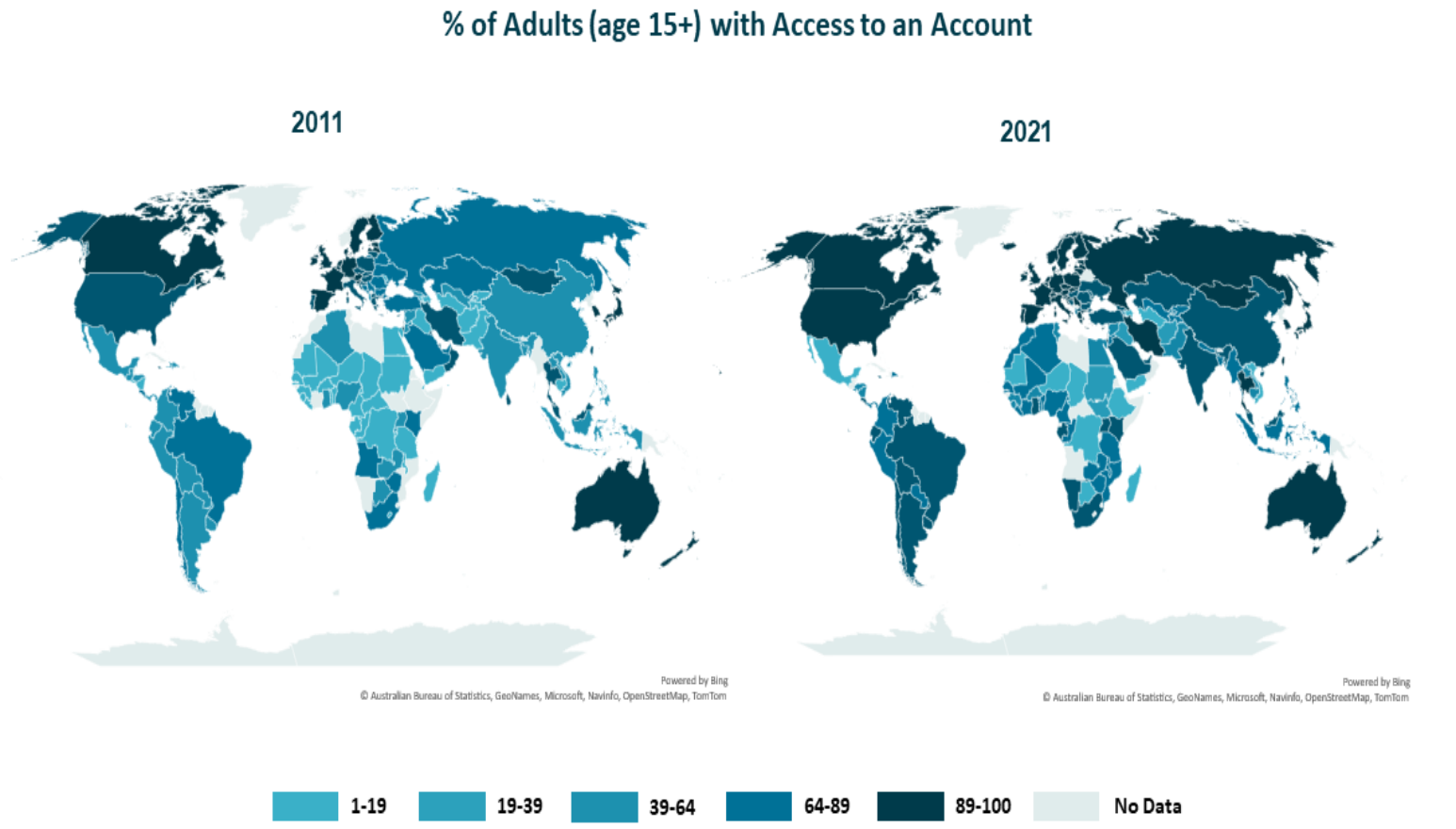
# Combined with investments in Digital Public Ecosystems (DPEs), this should lead to continued progress in financial inclusion (Breadth).




Data source: Global Findex 2021 database

## Key enabler to foster progress: A Digital Public Ecosystem (DPE)

- Digital public infrastructure (connectivity, IDs, payment system, open APIs)
- Enabling policies (sandboxes, agents, consumer protection)
- Data sharing arrangement, such as Open Finance
- Digitization of payments
- Financial and digital literacy

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Source: Global Findex

# This is particularly important considering the climate crisis …

**Inclusive financial markets can help build a greener and more resilient world and contribute to a just transtion**

- Climate-responsive financial services, including for adaptation and resilience
- Inclusive green finance and investments
- Adaptive social safety nets
- Inclusive carbon markets

**However, there is a significant gap between needs (demand) and supply of climate-related inclusive financial services and little financing for scaling**

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# … and increased vulnerability and shocks.

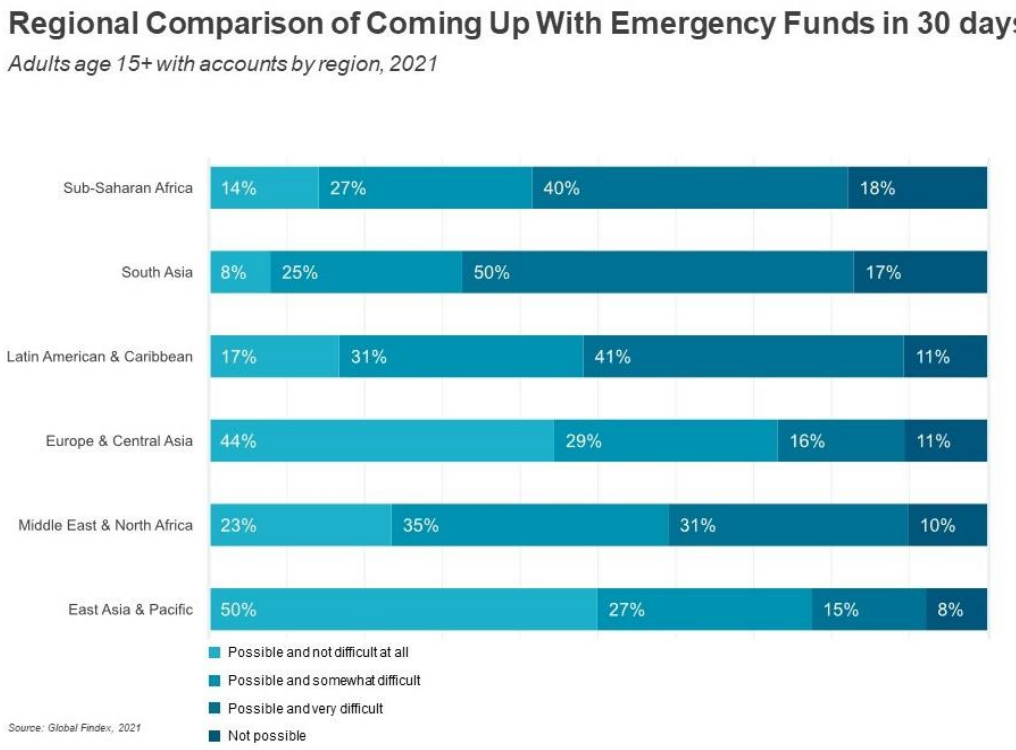
**4 out of 5** of the unbanked globally live in climate vulnerable countries

**In climate vulnerable countries:**

**1 out of 3** adults are unbanked compared to 1 in 10 in other countries

**3 out of 4** adults are not financially resilient

**Resilience to climate impacts**




**Resilience to shocks**

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Source: Analysis by the Office of the UNSGSA based on Findex and Notre Dame Global Adaptation Initiative Index

Sources: Global Findex

## 132 years is too long to close the gender gap. How can we accelerate financial inclusion?

The World Economic Forum's Global Gender Gap Report 2022 reveals that despite progress made towards gender equality in education and health, the gender gap in economic participation and opportunity remains essentially unchanged.

## Central-Bank Digital Currencies Are Coming—Whether Countries Are Ready or Not

The game-changing development could have a profound impact on the banking system. But few people still understand it.

## Fintechs face reckoning over customer service

## Silicon Valley Bank: the multiple warnings that were missed

Ahead of the first official postmortem on its collapse, bankers, regulators and executives admit that it was a crisis hiding in plain sight

## Ghana tackles illegal loan apps over fraud, cyber-bullying

## India's digital lending market likely to grow $515 bn by 2030 : Report

## Crypto has 'amplified financial risks' in emerging markets, central banks warn

Currency's appeal as a low-cost solution for countries with high inflation is 'illusory', says BIS

## CFPB looking at crypto platform hacks

Congratulations, crypto might count as "funds"! Now please report to US consumer-banking regulators

ESG & SUSTAINABILITY

## Looking at financial inclusion through a gender lens

Gender-intelligent design for financial services holds the key to unlocking financial inclusion for women. Joy Macknight reports on some innovative approaches showcased at the recent Women's World Banking summit.

## CBDCs invite risk of global financial fragmentation

## Bank of America to pay $250mn for overdraft and credit card abuse

Lender 'withheld rewards, double-dipped on fees and opened accounts without consent'

## In latest Zelle scam, Wells Fargo customers lose thousands after fraudsters pose as bank employees

Scammers are taking advantage of the platform's instantaneous, irreversible transactions.

## Digital financial inclusion is reshaping payments in Côte d'Ivoire

Government strategies and initiatives are guiding the expansion of financial inclusión

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## India central bank plans to widen use of digital currency

# Innovations are transforming the financial sector landscape …

**EMERGING TECHNOLOGIES**

DLT
APIs
AI/ML
Cloud Computing
Biometric Technologies

**NEW PRODUCTS AND SERVICES**

Cryptoassets
Digital credit
Crowdfunding
CBDC

**NEW BUSINESS MODELS**

Fintechs
Platforms
Digital Banks

**MORE DATA AND USES**

Open Finance
Scoring Systems
Machine Learning
AI

**MORE RISK TYPES AND INCIDENCES**

Fraud
Data Misuse, Privacy and Security
Lack of Transparency
Exclusion, especially women

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# Evolving DFS consumer risks challenge consumers

| | | | | |
|---|---|---|---|---|
| Four broad risk types | **FRAUD**<br>Examples:<br>• SIM swap fraud<br>• Mobile app fraud | **DATA MISUSE**<br>Examples:<br>• Algorithmic bias<br>• Unfair practices e.g., social shaming | **LACK OF TRANSPARENCY**<br>Examples:<br>• Undisclosed fees<br>• Complex user interface | **INADEQUATE REDRESS MECHANISMS**<br>Examples:<br>• Complex redress process<br>• Expensive complaints handling system |
| Two cross-cutting risk types | **AGENT-RELATED RISKS**<br>Examples: Liquidity challenges, agent fraud, discrimination based on social status<br><br>**NETWORK DOWNTIME**<br>Examples: Distributed Denial of Service (DDoS) attacks, insufficiently tested system upgrade, power outage | | | |

Fraud and data misuse are directly linked to **cybersecurity**.

The two cross-cutting risks share some elements with all four broad risk types.

Further info is available in *The Evolution of the Nature and Scale of DFS Consumer Risks*, CGAP 2022

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# The scale of DFS consumer risks has increased in most cases since 2015

Available evidence since 2015 show an increase in scale for most risks

| Risk Type | Global | Regions | Country |
|---|---|---|---|
| Fraud | ↑ | ↑ | ↑ |
| Data Misuse | ↑ | ↑ | ↑ |
| Lack of transparency | ↑ | ↑ | N/A |
| Inadequate redress mechanisms | N/A | N/A | ↑ |

Red arrow: Available data show an **overall** increase in value or volume.

Orange arrow: Literature suggests an increase in value or volume without supporting data.

N/A: Reliable information and data are not available or sufficient to determine increase or decrease of the risk.

Further info is available in *The Evolution of the Nature and Scale of DFS Consumer Risks*, CGAP 2022

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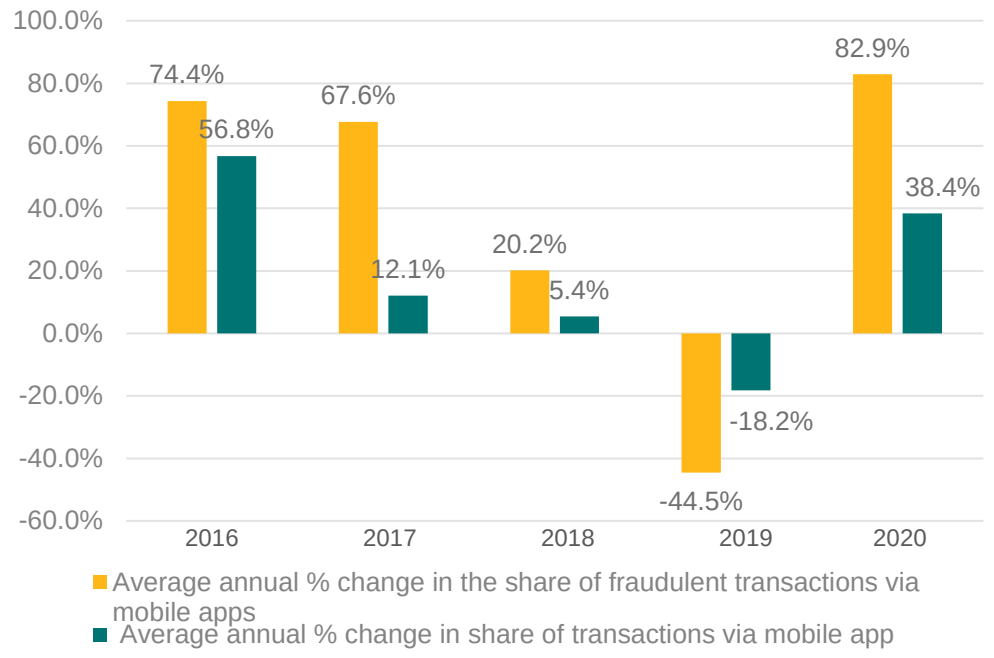
Source: CGAP. "Consumer Risks and Digital Financial Services: A Côte d'Ivoire Study". "
Source: CGAP. "The Evolution of the Nature and Scale of DFS Consumer Risks."

# Globally, mobile app fraud is rising faster than mobile app usage.




Source: Adapted from the Outseer Fraud and Payments Report, Q2 2021, and RSA Quarterly Fraud Reports, Q1 2018 and Q3 2020.

**Percentage change in share of fraudulent mobile app transactions and share of mobile app transactions (globally)**

- 2016/2020 – share of fraudulent transactions via apps +104% vs share of transactions carried out via apps +34%.
- In India and Kenya, fraudulent apps have exposed digital credit customers to abusive lenders.

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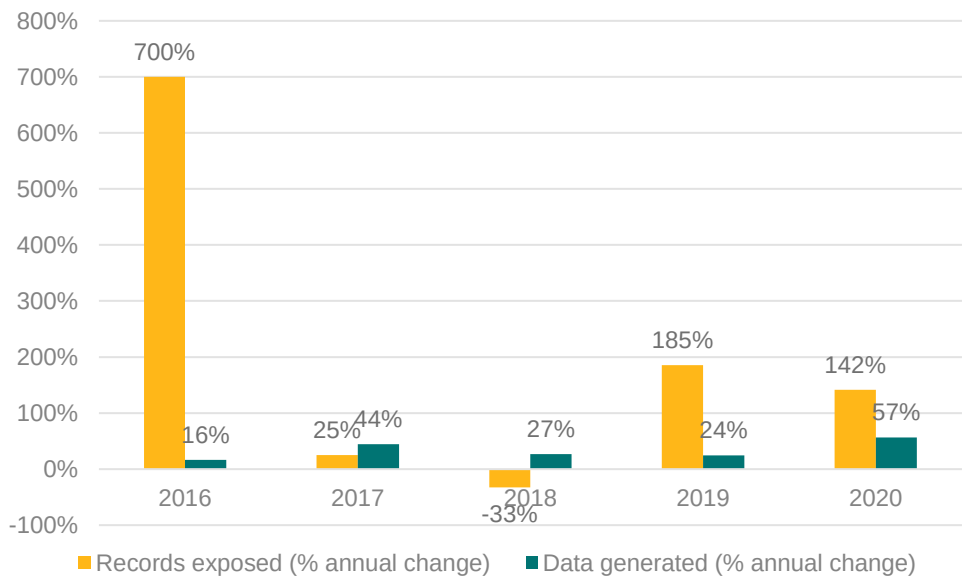
# Globally, the increase in data breaches surpasses the increase in data created.




Source: Data adapted from Risk Based Security 2020 Year End Report (global number of records exposed) and Statista (global data created).

**Global data created and records exposed, annual percentage changes, 2016–2020**

- 2017/2020 – the average annual increase in number of records exposed globally (80%) was much higher than the annual increase in volume of data created (38%).
- The average time to identify and contain a data breach increased from 257 days (2017) to 287 days (2021).

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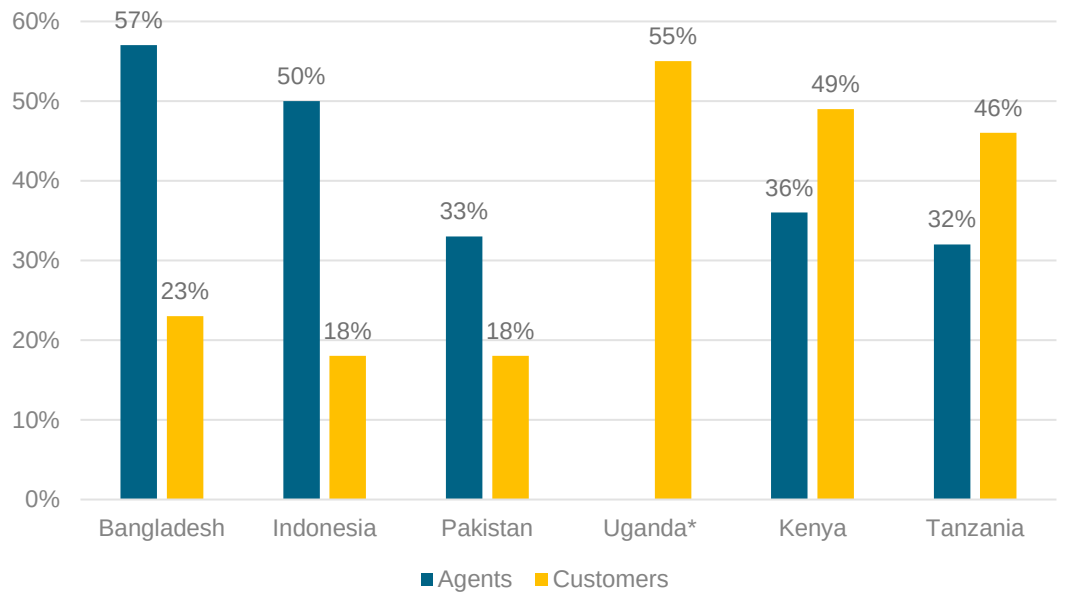
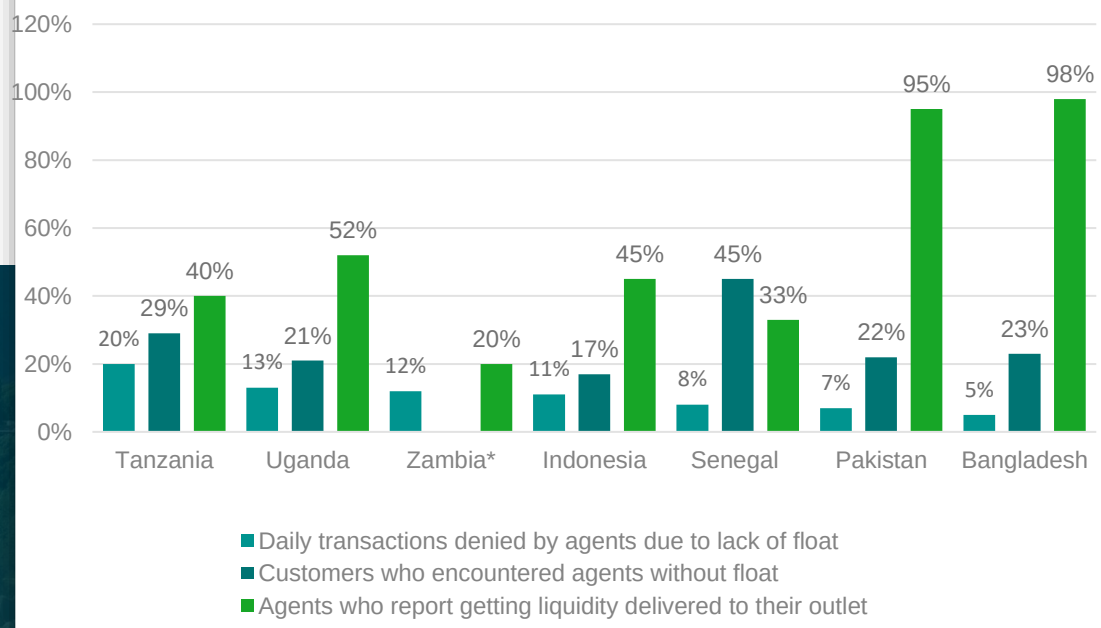
# Network downtime and lack of agent liquidity may lead to risky agent and customer behavior and loss of confidence in formal finance.

Proportion of agents and customers who reported experiencing downtime




Source: Genga et al. 2018, based on data from ANA surveys.

Customer and agent liquidity challenges




Source: Genga et al. 2018 and Kiarie et al 2018, based on data from ANA surveys.

- Customers' day-to-day activities may be interrupted, leading to loss of confidence.

- Customers may leave cash with agent or give their PIN to the agent to transact on their behalf.

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# New opportunities and risks are challenging financial authorities in novel ways…

### FINANCIAL SECTOR REGULATORY PERIMETER

What to regulate, when and how?
How do we prioritize scarce resources?
How do supervisors address technological risks?

### RELATIONSHIPS AMONG DIFFERENT AUTHORITIES

How can regulators (financial and non-financial) collaborate? Nationally and internationally?

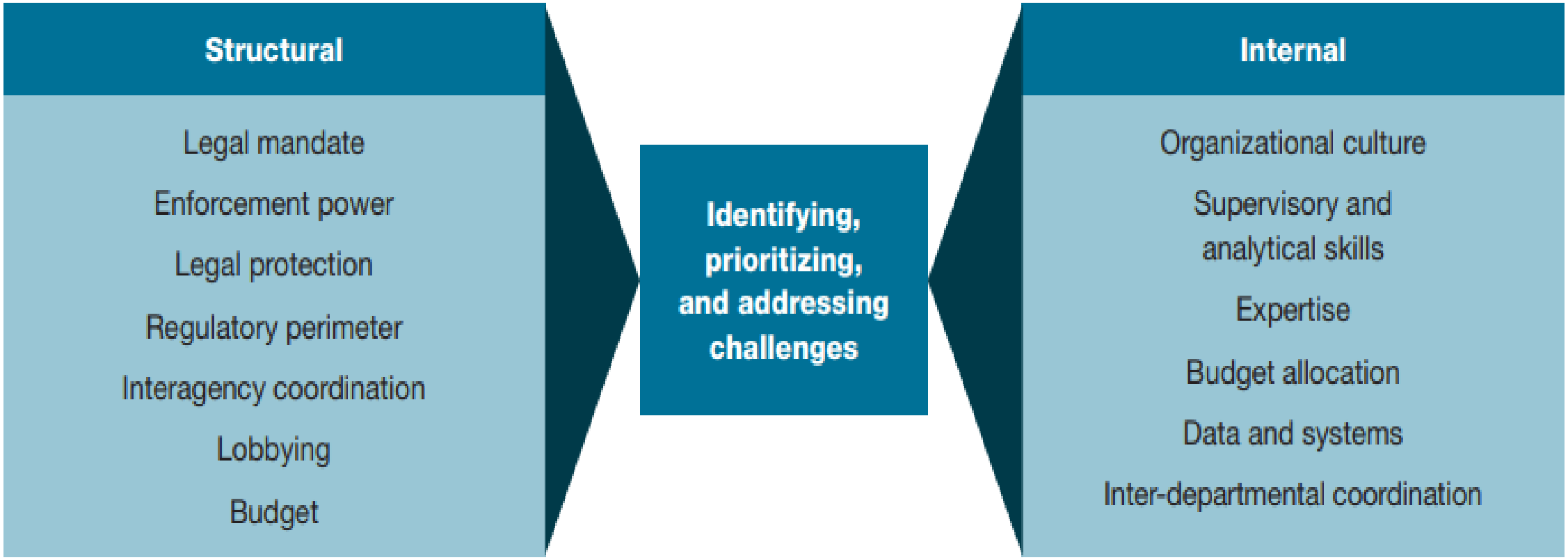
### BALANCING POLICY OBJECTIVES

How do we consider I-SIP and other policy objectives?
Do innovations impact various policy objectives in the same way?

### ENSURING CONSUMER PROTECTION

What is a more holistic and inclusive approach to responsible ecosystems?
How do we achieve positive customer outcomes?
How do we achieve gender equity in financial inclusion?

# …and creates challenges for supervisors in EMDEs.




Further info is available in *Digital Financial Services for Financial Inclusion: Tools for Supervisors*

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# … challenging all of us to consider a responsible DFS ecosystem vision.

Three building blocks (3Cs):

- **Customer-centricity** better protects consumers by putting them at the core of any initiative.
- Key actors have the **capability** to contribute to a responsible ecosystem.
- **Collaboration** involves structured and constructive relationships between actors in the ecosystem.

**Monitoring** collective progress and measuring success through customer outcomes will tie the 3Cs together.

Risk prevention → Risk identification → Risk mitigation

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