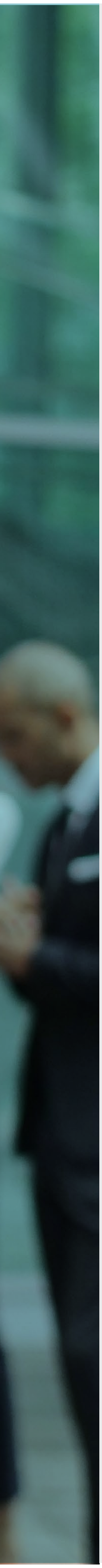
FINANCIAL INCLUSION
STRATEGY

FSCA
Financial Sector
Conduct Authority

FSCA FINANCIAL INCLUSION STRATEGY



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1. INTRODUCTION

1.1 Background

The financial sector in South Africa is a key component of the country's economy. Financial and business services account for close to 20 per cent of the country's overall Gross Domestic Product (GDP)[1] and the sector is a significant contributor to job creation. In addition to its importance at a macroeconomic level, the sector is vital in supporting the participation of ordinary South Africans in the broader economy.

The landscape of financial service provisioning in South Africa has changed significantly over the past two decades. The sector is increasingly sophisticated, well-regulated and stable, weathering events like the financial crisis in 2008 and safely managing the impacts of bank closures. Through a wide physical and digital network, the sector has provided access to a variety of financial products and services, that aim to help South Africans manage their money, plan for the future and cope with financial pressures and stresses.

There have been great strides made in including many previously excluded people into the financial system, and the mainstream economy, including through greater access to bank accounts. The advent of digital channels has contributed to widening access to the sector and improving the efficiency of financial service provisioning.

However, while levels of access have improved in transactional accounts, this is not reflected across many other financial products and services. Regular and sustained use of products and services also remains low. It is acknowledged that the financial needs of many South Africans, in particular the poor and low-income earners, may not be adequately served. For people to be effectively included in the financial sector, focus is needed not only on access to bank accounts, but also on access and the sustainable use of a diverse range of financial products and services that are appropriate to customer needs and economic circumstances.

The 2011 Policy Paper, "A Safer Financial Sector to Serve South Africa Better", set out Government's approach to reforming financial sector regulation to better serve the country and its citizens. Financial inclusion is set out as a key policy priority. To give effect to the proposed reforms, the Financial Sector Regulation Act, 2017 (FSR Act) was introduced. An objective of the FSR Act includes the establishment of a regulatory and supervisory framework that promotes financial inclusion. The FSR Act also established the Financial Sector Conduct Authority (FSCA), with the objectives of protecting customer by ensuring that customers are treated fairly by financial institutions, and providing financial customers with financial education programs. In achieving its objectives, the FSCA is also required to promote financial inclusion.

This document aims to outline the FSCA's strategy and approach to promoting financial inclusion in South Africa.

1 Statistics South Africa, http://www.statssa.gov.za/publications/P0441/GDP%202019%20Q2%20(Media%20presentation).pdf

1.2 What is financial inclusion?

The concept of financial inclusion has deepened and evolved over time and differs across jurisdictions. The Alliance for Financial Inclusion (AFI) notes that countries should "develop a clear and concise definition of what financial inclusion means in their particular national context". [2]AFI also notes that how financial inclusion is defined shapes expectations around what aspects of the market will be emphasised in relation to the provisioning of financial service and products, and who will benefit.

In South Africa, the FSR Act defines financial inclusion to mean that all persons have timely and fair access to appropriate, fair and affordable financial products and services. The National Treasury financial inclusion policy[3] defines financial inclusion as the delivery and use of regulated, affordable and suitable financial services by those segments of society where financial services are needed but not provided or are inadequately provided. From these definitions, it is clear that financial inclusion is broader than simple access but also takes into account the use and appropriateness of products and services.

The assessment and monitoring of financial inclusion can therefore be considered in three dimensions:

Figure 1: Dimensions of financial inclusion

Access	Usage
"Access" refers to the ease with which a consumer can obtain a financial service and includes physical and electronic reach of service provisioning as well as the affordability of financial services	"Usage" refers to both the upake of appropriate and needed products and services as well as how the acquired services are being used after nitial acquisition
Quality	
"Quality" of financial services refers to the experience of the consumer, both when acquiring and during the use of financial services. This includes market conduct, treating customers fairly and equitably, as well as client awareness and financial literacy	

The strategy will focus on the role that the FSCA will play in improving access to, usage and quality of financial services in support of financial inclusion in South Africa. This will be in terms of individuals as well small, micro and medium enterprises (SMMEs).

2 Alliance for Financial Inclusion (2017), "Guideline Note 28: Defining Financial Inclusion"
3 The National Treasury Financial Inclusion policy has not been published yet. The National Treasury is in the process of consulting with intra government stakeholders. According to the National Treasury Budget Review documents the policy will be published in 2019/20 financial year.

2. POLICY CONTEXT

As articulated in the National Development Plan (2013), Government has a vision of a South Africa where every citizen has an equal opportunity to participate in the mainstream economy. The financial sector, being at the heart of the economy, has a vital role to play in the development of such a society. The sector has the potential to contribute towards a greater inclusion of historically marginalised groups by extending access to banking, insurance and by helping to promote and mobilise household savings and easing broader access to credit[4]. A holistic policy approach to financial inclusion is required to effectively leverage the sector's ability to integrate people into the mainstream economy. Government policy responses to this imperative includes the following:

2.1 Financial Sector Regulation Act

Since 2011, Government has embarked on the most significant reform of financial sector regulation since democracy, implementing a Twin Peaks regulatory model. This places equal and dedicated emphasis on market conduct and prudential regulation and aims to ensure better outcomes in the sector, including for customers. Reforms resulted in the enactment of the FSR Act, which, as noted above, has as an objective the establishment of a regulatory and supervisory framework that promotes financial inclusion. The achievement of this objective rest on regulators such as the FSCA and the Prudential Authority (PA), established in terms of the FSR Act. The FSR Act requires the FSCA to amongst others, promote financial inclusion in order to achieve its objective. The diagram below depicts the objectives and functions of the FSCA:

Figure 2: The FSCA's mandate and objectives

FSCA Financial Sector Conduct Authority					
Objectives	Enhance and support the efficiency and integrity of financial markets	Protect financial customers by promoting fair treatment of financial customers	Assist in maintaining financial stability	Provide financial customers and potential financial customers with financial education program	
Functions	Regulate and supervise conduct of financial institutions	Promote sustainable competition in the provision of financial products and financial services	Promote financial inclusion	Monitor delivery of fair outcomes for financial customers	Promote financial consumer education

In recognition of the multiplicity of stakeholders involved in driving financial inclusion, the G20 principles of innovative financial inclusion advocates for co-operation amongst government departments and regulators, and the creation of an institutional environment where financial inclusion efforts are coordinated, and partnerships are encouraged.

4 National Development Plan (2013)

To promote greater intra-governmental coordination and information-sharing in South Africa, the FSR Act establishes a financial inclusion working group within the Financial System Council of Regulators. Members of this Council include the National Treasury, the FSCA, the PA, the Department of Trade and Industry, the National Credit Regulator, the National Consumer Commission, the Department of Health, and the Council for Medical Schemes.

2.2 National Treasury Financial Inclusion Policy

As part of Government's holistic approach to financial inclusion, National Treasury has produced a financial inclusion policy. This policy assesses the current state of financial inclusion in South Africa, puts forward general principles to guide sustainable improvement in financial inclusion and embeds those principles in specific pillars in support of the policy objectives. Taking into account lessons from financial inclusion approaches internationally, a series of specific interventions are proposed in which financial inclusion can be taken forward responsibly and sustainably.

The National Treasury draft policy will serve as a guide to all stakeholders in government, regulators (including the FSCA) and the financial services sector on areas they should focus on to ensure the achievement of the sustainable financial inclusion. The policy focuses on the following three pillars:

- **Pillar One - Deepen financial inclusion for individuals.** Improve the beneficial use of financial services for the newly included, the payment infrastructure for the mass use of new payment methods, and the take-up of savings, insurance and productive credit.
- **Pillar Two - Improve access to financial services for SMMEs.** This includes improving the credit infrastructure for SMMEs, leveraging off a broader payment system and incentivising the provision of asset insurance.
- **Pillar Three – Leverage a more diversified provider and distribution base.** Support competition and diversification of the supply base by strengthening the co-operatives sector, developing a more proportionate regulatory environment to ease compliance costs, allowing for and empowering the use of agents in financial service distribution and leveraging fintech disruptors.

The policy also aims to improve cooperation and coordination amongst stakeholders and has in this regard proposes the establishment of the Financial Inclusion Taskforce (FIT) and the Financial Inclusion Forum (FIF). The FIT is proposed to be the working group established under the Financial System Council of Regulators in terms of the FSR Act. The FIF will be a platform where industry and other non-governmental stakeholders can engage with policymakers and regulators on strategic priorities. The FSCA is expected to play an active role in these coordination structures, as well as in terms of supporting the pillars identified in the policy.

3. DIMENSIONS OF FINANCIAL INCLUSION IN SOUTH AFRICA: CURRENT LANDSCAPE

3.1 Access

The dimension of access reflects the capacity of the financial sector to efficiently serve customers with financial products and services through accessible and convenient distribution channels. It considers the diversification of financial institutions and depth of reach of financial services. It further reflects demand-side barriers that customers may face in accessing financial services, such as cost of acquisition and other socio-economic factors.

The table below summarises issues identified in South Africa relating to access to financial services:

Table 1: Access to financial services in South Africa

Sector	Diversification of providers	Physical and electronic reach	Costs of acquiring a financial service
Banking	• Four big banks dominate the market in terms of total assets and market capitalisation. • Three new bank licenses were granted in 2018/19, the first new banking licenses in almost a decade. Stringent regulatory requirements and the relatively high cost of acquiring licenses could present barriers to entry into the market. • Small banks such as co-operative banks and mutual banks have not effectively penetrated the market. • The economies of scale acquired by the big banks have made it difficult for new entrants to penetrate the market. • The emergence of digital banks offers opportunity to promote access and improve efficiency.	• Number of ATMs and branches are declining as digitisation becomes central to banks' strategies. • Access through mobile phones has not been sufficiently leveraged. • Customers in rural areas face long and/or costly journeys to visit branches.	Cost is not an issue when accessing a bank account – according to Finscope survey (2018), less than 5% of the adult population claims that they do not have a bank account because of costs of acquisition.

Insurance	• The market is dominated by big insurers in both the life and non-life market. • It is difficult for small players to enter and penetrate the market, including due to capital requirements. • The Insurance Act (2017) creates a new category of microinsurance institutions.	• Well-developed intermediary network distributing insurance products. • Access through mobile phone has not been sufficiently leveraged.	Insurance is perceived as expensive by those who do not have it. This does not necessarily imply that cost of acquisition is a barrier to access but may mean that premiums are perceived to be high.
Credit	• The four big banks dominate the credit market. • Non-bank credit providers have low penetration in the market, including in the low-income market. • In terms of SMME credit, there is a small network of development finance institutions providing lending.	• There are over 30 000 credit providers branches. • Access to credit through mobile phones has not been sufficiently leveraged.	The cost of acquiring credit has not been a barrier (although it is noted that credit that is too easily available – or recklessly extended – presents its own costs, including over overindebtedness).
Savings	• Formal provision of savings products is dominated by pension and retirement funds, through mandatory employer arrangements • Products are provided to a lesser extent through banks, insurance companies and collective investment schemes • Informal groups such as stokvels remain prevalent especially in low income market	• Banks savings products are sold through branches and banks digital platforms - no advice is provided • Insurance savings and investment product are mostly distributed by brokers and intermediaries • A few digital platforms have begun emerging	Acquisition costs not an issue when accessing savings. The availability of funds to save is a significant consideration in a low-growth high unemployment economy.

Diversification of financial services providers - the financial sector in South Africa is highly concentrated. Due to the dominance of a few big financial service providers across banking, insurance and credit, competition and innovation may be subdued. Although concentration in the sector does not automatically imply a lack of competition, it has the potential to lead to avoidance of price competition, limited consumer choice and lower levels of innovation[5]. This may change as more digital offerings enter the market, better targeting customer needs. The Insurance Act (2017) provides for a new category of microinsurance providers and aims to put in place a new regulatory framework for the provision of accessible and affordable insurance to low-income South Africans.

5 Competition Commission Banking Inquiry Report (2008)

Physical reach and electronic reach - the South African financial services sector, particularly the banking sector, has a well-developed service network. For the banking sector the automated teller machines (ATMs) and bank branches provide a critical interface between banks and customers. In insurance, distribution happens through a widespread network of intermediaries and other agents.

Technology is redefining transactional banking. This is seen in the entry of digital banks into the South African market, and in traditional banks strengthening and extending the capabilities of their electronic channels. One impact has been major banking groups reducing their physical branch network due to costs of physical infrastructure, the increasing use of alterative channels, and competitor challenges from digital-only branchless banks. While digitisation can support financial inclusion, it is noted that the response of customer in terms of accessing financial services through digital platforms has not matched digitisation efforts by banks. The 2018 Retail Banking Diagnostic noted input from civil society that "some low-income consumers may be reluctant to use online or telephone banking, given the material cost they face in doing so, including the cost of data or airtime to access such electronic services." Another key consideration is that cash is still a dominant means of transacting in South Africa, making traditional physical distribution platforms such as the ATM network necessary.

The insurance sector is well served by a wide range of intermediaries. As at 31 March 2018, there were approximately 10 139[6] category 1 licensed financial service providers (FSPs) with the majority being insurance intermediaries. For both life and non-life insurers, brokers are the dominant distribution channel. Although the broker model is an important interface between customers and insurers, remuneration models that rely on commissions pose a risk of mis-selling of financial products and poor customer outcomes. The Retail Distribution Review (RDR) aims to address these risks in the distribution of insurance products. Other distribution models in the insurance sector are in-house agents, and the bank assurance model where insurance is sold through bank branches.

The retail credit market is the largest segment in financial service sector in terms of the number of participants in the market. However, the market is highly concentrated as it is dominated by the banking sector, in particular the four big banks. The banking sector hold more than 80% of the overall gross debtor's book. With regard to reach, credit is available through over 30 000 credit provider branches. Access through digital platforms is beginning to gain momentum as many providers offer customers the ability to apply for credit and conclude agreements online.

The provision of formal savings is dominated by pension and retirements funds mainly because contribution to the funds is compulsory as a condition of employment. While products are also available through other formal providers such as banks and insurance companies, take up through these institutions is relatively low. The South Africa market is characterised by informal savings groups such as stokvels. These community-based savings clubs are prominent amongst the poor and the low-income earners. Access through digital platforms is nascent, with relatively few fintech player in the savings spaces emerging to provide alternative platforms for savings. Broader socioeconomic considerations must also be taken into account in relation to savings, particularly the low levels of economic growth and high levels of unemployment in South Africa, which translate to low levels of income available for saving.

Costs of acquiring financial services – acquisition costs have not been a major constraint to access. The main barriers to access relate to socioeconomic issues such as lack of employment and income.

6 It should be noted that some FSPs have multiple license categories.

3.2 Usage

Usage and uptake considers the rate of acquisition of financial services and the way in which consumers use financial services. The table below summarises issues identified related to usage and uptake:

Table 2: Usage and uptake of financial services in South Africa

	Transactional bank accounts	Insurance products	Credit products	Savings products
Uptake	80% of the adult population has a transactional bank account According to previous estimates only 46.9% of small businesses use bank products[7]	46% of the adult population has some form of insurance from a licensed insurer 22% of small business owners use formal insurance products[8]	61% of the adult population borrows from a formal credit provider. Only 8% of small business owners have formal credit products[9]	25% of South Africans save with a formal institution and 16% save informally
Usage issues	Lack of trust - 20% of customers indicate that they do not trust banks	High funeral insurance penetration but lower penetration of non-funeral insurance products (e.g only. 8% of adult's population have vehicle insurance and 4% have household content insurance.	High credit usage for consumption purposes and not for productive purposes	High credit usage for consumption purposes and not for productive purposes
	Perceived high banks charges – 67% of the adult population claim that the bank fees are too expensive	Premiums perceived to be too expensive (over 50 % of the adult population who do not have insurance state it is because it is too expensive)	High levels of over-indebtedness	Unemployment remains a major reason why the majority of people do not save
	Inappropriate use of bank account- over 30% of banked population uses the account as a cash distribution mechanism (one deposit one withdrawal)	Poor or non-availability of non-life products appropriate for the lower end of the market (e.g. for informal housing structures; older car insurance)		Limited financial capability
	Inappropriate use of banking channels (e.g. conducting transactions at a branch rather than ATM)	Lack of trust (34% of adult populations claims that they do not trust insurance companies)		

Source: Finscope Survey 2018

Transactional bank accounts - an increasing percentage of the banked population simply use their bank account as a means of cash distribution. This is concerning, given that the effectiveness of financial inclusion depends on continuous and productive usage of the products acquired[10]. This phenomenon is prevalent among SASSA grant recipients[11], with over 40% of banked grant recipients claiming that they withdraw money as soon as it is deposited. This behaviour is not limited to grant recipients however, and behaviour may be attributed to factors such as:

- **Lack of trust in banks** – low income earners have a mistrust of the formal financial services sector which is rooted in fears of exploitation[12]. According to the Finscope Survey (2018) 20% of the adult population in South Africa do

7 The last available data for SMME access to financial services comes from the 'FinScope South Africa Small Business Survey 2010'. It is acknowledged that more recent data is needed and this forms part of the strategy
8 Same comment as above
9 Same comment as above
10 National Treasury Financial Inclusion Policy (2019)
11 Government has recently started paying all social grants directly into bank accounts
12 https://www.weforum.org/agenda/2017/04/financial-inclusion-south-africa/

not trust banks. Incidents of unfair treatment or widespread scams (for example debit order abuse) fuel further distrust and fear toward formal financial institutions[13].

- **Perceived high cost of using an account** - although the monthly fee for entry level basic bank accounts is relatively low, transaction costs such as withdrawal, payment and deposit fees are perceived to be high. The cost burden on low income accountholders can be increased further by the additional costs to customers relating to travel and wait times and transport fares when they need to access the cash in their accounts.
- **Lack of knowledge of the benefits of a transactional account** - people who withdraw money as soon as it is deposited into their account may do so because they lack understanding of the features offered by a bank account. For example, they may not be aware that using a card for purchases and electronic transfers through telephone, internet or mobile app banking is free on basic bank accounts offered by most of the banks.
- **A cash-based economy** – the ability to use bank cards rather than physical cash may not always be possible. The increase in technological innovations allowing for cheaper acceptance of card and other electronic payments may assist in reducing the need to rely on cash.

Despite digitisation efforts, high mobile penetration and lower transaction costs for using digital distribution channels, there is still a considerable number of customers who still prefer transacting face-to-face through branches. This may be due to lack of digital literacy, and the fear of fraud involving ATMs and mobile/internet banking.

It is notable that while many banks offer bank accounts specifically targeted at SMMEs, many owners of small businesses bank in their personal capacity rather than through separate bank accounts.

Insurance products – the main contributing factor to overall levels of insurance penetration is the significant level of uptake of funeral insurance. According to the Finscope Survey (2018), over 50% of all insured people have funeral insurance. The uptake of other insurance products such as vehicle insurance, household content insurance, building insurance and life cover is still low, particularly for low-income earners, exposing consumers to multiple risks.

13 CGAP (2015) 'A Market Systems Approach to Financial Inclusion - Guidelines for Funders'. Available on: https://www.cgap.org/sites/default/files/researches/documents/Consensus-Guidelines-A-Market-Systems-Approach-to-Financial-inclusion-Sept-2015_0.pdf

The low penetration of non-funeral insurance products may be attributed to the perceived

costs of insurance. While insurance is generally a grudge purchase, only 7% of the adult population state that they do not need it while over 50% who do not have insurance state it is because it is too expensive[14]. This demonstrates that while the need for insurance exists in the market, available products may not meet the needs of or be affordable to lower-income people.

SMMEs remain underinsured, with estimates indicating that less than a quarter of SMMEs have any form of insurance.

Credit - access to and uptake of credit in South Africa has significantly increased over the past few years, driven by the introduction of the National Credit Act, which replaced the Usury Act. However (as indicated in the National Treasury Financial Inclusion Policy Paper) credit extended has been predominately unsecured credit, driving short term consumption. Access to productive credit can support the build-up of wealth through the acquisition of a property or means of production.

Access to credit by SMMEs is a complex and multifaceted issue. While providers do exist, a number of factors impede the ability of SMMEs to access lending. There are information asymmetries both on the supply and demand sides – SMMEs don't know which lender to go to for which type of funding and funders don't have enough information about the SMME to make an informed funding decision. Data on SMMEs is scarce, be it credit, payment history, or other relevant metrics. Credit providers may face regulatory limitations in lending to SMMEs. Businesses may not have the necessary financial literacy, financial capability and business management skills to run credible businesses which makes provision of funding risky. 41.8% of small business owners do not use formal or informal products for business purposes, but rely solely on family and friends for borrowing, and saving money at home[15].

Savings – the uptake of formal savings products remains relatively low, particularly among low income earners, and a significant number of people still use informal channels to save. The 2019 Old Mutual Savings and Investment Monitor reflects that 60% of respondents make use of informal savings platforms. The prevalence of these informal saving groups exhibit the financial discipline of individuals, who may require formal products that are more flexible, affordable and suitable to their needs.

14 FinScope Survey 2018
15 FinScope South Africa Small Business Survey 2010

3.3 Quality

Quality indicators describe whether financial products and services match customer needs, the range of options available to customers, and customer awareness and understanding of financial products and services[16]. The table below summarises key issues related to quality measures in the South Africa financial sector.

Table 3:Quality of financial services in South Africa

Indicators	Issues identified
Affordability	• Affordability issues impact all three dimensions of inclusion – access, usage and quality. The costs of using financial products are perceived to be high by many financial consumers, particularly low income consumers. • Some fees, charges and penalties may not be fair or reflective of the value provided.
Transparency	• 47% of the adult population find the language used in financial paperwork confusing.
Consumer protection	• Only 23% of the adult population have heard of an ombudsman. • A total of 100 829 complaints were received across all financial sector ombuds (the ombudsman for banking, short-term insurance, long-term insurance, credit, FAIS and Pension Fund Adjudicator) in the financial year 2017/18. • A consumer protection regulatory framework is in place in the financial sector, however it is fragmented. The regulatory and supervisory framework is being strengthened under the Twin Peaks reform process.
Financial education	• According to the 2016 financial literacy baseline study, South Africa's overall financial literacy score increased from 54 in 2011 to 58 out of 100 in 201617. • These levels are low and may affect the ability of consumer to meaningfully make use of products and services.
Indebtedness	• As at June 2019, out of 25 million credit active consumers, 5.7million are three months late with their account.
Choice	• 65% of the adult population is not sure which bank account is the best one for them. • In the Financial Literacy baseline study, consumer awareness of financial products (product choice) scored 46 out of 100.

Sources: Finscope 2019 & National Credit Regulator Credit Bureau Monitor - Second Quarter 2019 & Human Science Research Council Financial Literacy Baseline Study

The dimension of quality is closely related to the FSCA's overall mandate as a market conduct regulator in South Africa. The FSCA objective of ensuring that customers are treated fairly by their financial institutions covers the full range of product and service provision, from governance and culture to product design, distribution and disclosure, and the ability to make complaints and switch products.

The Financial Services Board (FSB), the predecessor of the FSCA, introduced the Treating Customers Fairly (TCF) initiative in 2011 and has since been entrenching the principles of fair customer treatment throughout the sector. Building on TCF, the FSCA has adopted a set of guiding principles including (among others) being pre-emptive, proactive, risk-based, proportional, intensive, intrusive, transparent, and outcomes-focused. It is embedding TCF outcomes in regulatory and supervisory frameworks, and developing conduct standards that combine principles and rules in a way best designed to achieve desired outcomes – not relying only on rules and "box ticking".

16 The World Bank 'How to measure Financial inclusion'. Available on: https://www.worldbank.org/en/topic/financialinclusion/brief/how-to-measure-financial-inclusion

17 In this study a score of 100 percent indicates complete financial literacy.

Effective dispute resolution further supports financial inclusion, ensuring that customers are empowered to hold institutions to account. The financial sector ombuds system has been instrumental in addressing consumer disputes with financial service providers. However, awareness of the ombuds system remains relatively low, and the fragmentation of the system may be confusing for consumer to navigate. The FSR Act takes steps to improve the efficiency and effectiveness of the ombuds system, including the proposed creation of an Ombud Council to create a single point of entry for customers seeking to resolve disputes.

The financial literacy score shows that efforts to promote financial literacy are bearing fruits. Product awareness relating to transactional bank account is reasonable high. However, there is need to create awareness of other products (e.g. insurance and savings).

4. AN ENABLING ENVIRONMENT FOR FINANCIAL INCLUSION

Promoting financial inclusion requires the participation of different stakeholders in the financial sector and the economy more broadly. The role of the FSCA within this broader ecosystem will leverage its position as regulator of financial institutions to drive targeted initiatives that can improve access, usage and quality of financial products and services. The FSCA will also work closely with other stakeholders to maximise efforts and resources and leverage the respective strengths of various actors.

As a regulator, the FSCA is well-positioned to create an enabling environment for financial inclusion, where financial institutions are better able to provide financial products and services that are accessible, appropriate, and suitable to the needs of customers, with a focus on the underserved. Key levers that the FSCA can use to achieve this are those that address:

- Demand-side issues in the financial sector
- Supply-side issues in the financial sector
- Regulatory environment that affect dimensions of financial inclusion

The powers and tools that the FSCA will use to create this environment will be exercised in terms of the overall mandate given to us in the FSR Act.

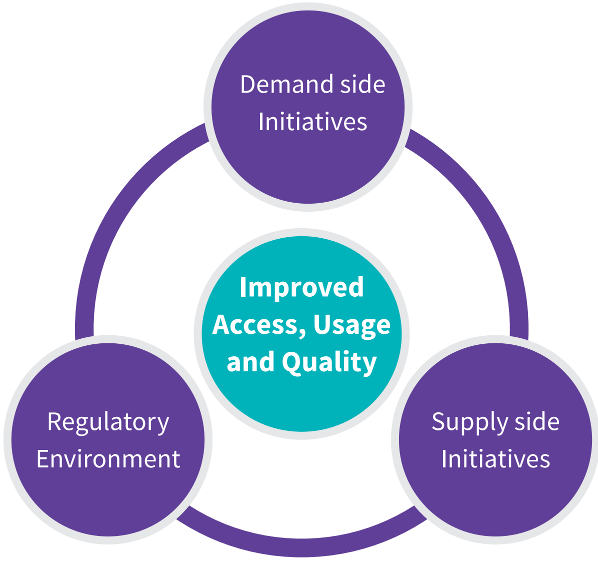
The levers create an enabling environment for financial inclusion as described in the diagrams below:

Figure 3: An enabling environment for financial inclusion.

Demand side	Customers who are informed and use appropriate products the meet their needs	
Supply side	• Diversification of financial services providers • Improved capacity of small financial service providers • Provision of appropriate financial services and products for un-and underreserved Markets	
	Products and Services • Simple products • Affordable, comparable with transparent Pricing • Effective disclosure, branding and Marketing	**Distribution channels** • Accesssible, effective and low cost channels • Positive customer experience at a point of sale • Optimised and digitised channels
Regulatory Environment	• Conducive legal and regulatory environment for retial and SMME • Customer who are protected and treated fairly • Enabled innivation	

Source: SADC Financial Inclusion Strategy/Boston Consulting Group

Figure 4: Levers to improve dimensions of financial inclusion



In line with its function of promoting financial inclusion, the FSCA will therefore lever demand-side, supply-side and regulatory environment initiatives to improve access, usage, and quality of financial products and services, with a focus on un- and underserved markets.

5. FSCA STRATEGIC PILLARS FOR PROMOTING FINANCIAL INCLUSION

The FSCA published its regulatory strategy in 2018, which sets out six strategic priorities for the FSCA, including the creation of an inclusive and transformed financial sector.

Within this framework, we have identified seven strategic pillars toward realisation of this priority. It is anticipated that these strategic pillars will guide the FSCA 's approach to financial inclusion over the next three-year period (2020 – 2023). Through the strategy implementation plan we will set out specific projects that will enable realisation of each strategic pillar. These projects will be reviewed annually, and refined, added to or amended as projects are completed and as the financial sector evolves. The strategic pillars are summarised in the table below and explained more fully thereafter.

Table 4: FSCA strategic pillars for promoting financial inclusion

Strategic pillars to promote financial inclusion		Dimensions of financial inclusion
DEMAND SIDE		
1	Promote financial inclusion through financial education	Usage
2	Collect and monitor data on financial inclusion to monitor progress	Usage Access Quality
	SUPPLY SIDE	
3	Support technological innovation that enables financial inclusion[18]	Access Usage
4	Support small financial services providers who typically serve lower income customers with simple and affordable products	Access Usage
5	Promote the supply of appropriate financial products and services to SMMEs	Usage Access Quality
	REGULATORY ENVIRONMENT	
6	Create a regulatory and supervisory framework that promotes financial inclusion	Usage Access Quality
7	Effectively cooperate with other stakeholders and participate in broader financial inclusion initiatives	Usage Access Quality

18 This pillar also addresses factors relevant to the Regulatory Environment

5.1 Promote financial inclusion through consumer financial education

The FSCA has a statutory mandate to provide financial customers and potential financial customers with financial education programs. It is required to formulate and implement strategies and programs for financial education for the general public. The effective execution of this mandate is vital for promoting financial inclusion, in particular as it can greatly improve usage of financial products and services.

The FSCA's consumer education approach focuses on areas where barriers to effective or optimal financial inclusion exist as result of lack of knowledge and literacy. Our approach aims to ensure that consumers:

- fully understand the nature, risks and benefits of different financial products and services so that they have confidence to choose products that are appropriate to their needs;
- are able to compare financial products and services and make informed choices; and
- fully understand their rights when engaging with financial institutions, including their options for resolving complaints and can take appropriate action when they do encounter problems.

Financial consumer education ensures the sustainability of financial inclusion. The FSCA's consumer education campaigns will create awareness of the benefits and risks of using different financial products, services and distribution channels, to meet specific financial needs. Our consumer financial education campaigns will be informed by research conducted to understand barriers to uptake and usage caused by lack of knowledge and literacy. Where appropriate, we will partner with other stakeholders, including financial institutions, in developing and rolling out consumer education campaigns.

Financial institutions have a statutory obligation, in terms of the Financial Sector Code, to promote consumer financial education[19]. As a result, most financial institutions have over the years designed and implemented financial education programmes aimed at empowering consumers with knowledge to enable them to make more informed decisions about their finances and lifestyles. However, this approach has resulted in a myriad of initiatives, including some that are inappropriate, marketing-focused or duplicative, limiting effectiveness[20]. In exercising its mandate in terms of consumer education, the FSCA will develop standards related to the design, suitability, implementation, monitoring and evaluation of financial education programs, or other initiatives aimed at promoting financial literacy. The standards will ensure that the financial education programmes provided by financial institutions are appropriate, better supporting financial inclusion. The standards will also ensure that there is coordination of industry initiatives to maximise the impact of the sector's resources and efforts and ensure alignment to the National Financial Education Strategy.

5.2 Collect data and monitor progress in promoting financial inclusion

Appropriate, reliable data is needed to support our approach to financial inclusion and to monitor and measure the impact of efforts over time. The data required to effectively monitor progress in promoting financial inclusion focuses on three dimensions of financial inclusion: access, usage and quality of financial services.

To understand demand-side factors that affect dimensions financial inclusion, we will participate in the syndicate arrangement to fund and participate in the design of the Finscope survey. The Finscope Survey is an annual, nationally representative study of consumers' financial behaviour and perceptions of financial services. Through the syndicate arrangement, the FSCA is able to ensure that the questions posed in the survey provide information that may relate to particular areas of concern. For example, questions can be built into the survey to better understand why consumer exhibit a preference for specific types of insurance products over others.

Information regarding supply side data will be built into the statutory conduct of business returns that are completed by entities regulated by the FSCA.

19 Financial Institutions are required in terms of the Financial Sector Code to spend 0.4 % of their after-tax income on financial education programmes.

20 Finmark Trust 2005 'Preliminary Principles for Expanding Consumer Financial Literacy in South Africa', http://www.finmark.org.za/wp-content/uploads/2016/01/Note_fin_Lit_SA_2005.pdf

5.3 Support technological innovation that enables financial inclusion

The rapid penetration of mobile phones in South Africa, together with increasing digital innovation in the era of the Fourth Industrial Revolution, has led to the emergence of new financial services and products and new delivery channels. These have the potential to contribute to the expansion of financial services to serve un- and underserved populations (availability), at low cost (affordability), and in efficient, safe, reliable forms that meet their needs (quality)[21]. Globally, the emergence of fintech (financial technology) firms has required financial regulators to be equally innovative and agile in responding to the benefits that these firms can bring, while also ensuring that potential risks are understood and managed.

In South Africa, barriers to fintech participation include a perceived complex regulatory environment and a lack of clarity or guidance on how fintechs can and should fit into that environment[22]. To address this, the FSCA is participating in the Intergovernmental Fintech Working Group (IFWG) project to establish an Innovation Hub in South Africa[23]. The Innovation Hub aims to include a Regulatory Guidance Unit that will provide an initial point of contact for fintechs to access guidance on regulatory requirements. Qualifying fintechs may also be directed to the Sandbox, where they will be able to test innovative ideas.

A key criterion for entry into the Innovation Hub will be to demonstrate that the innovation will address financial inclusion.

In this way, regulators will ensure that the resources dedicated to the Innovation Hub address supply-side factors by supporting the emergence of businesses that improve access, usage and quality of financial products and services.

To ensure that emerging technology enables business models and products that promote financial inclusion, the FSCA will engage with the fintech sector to create awareness of financial inclusion issues that need to be addressed in South Africa, to encourage the development of appropriate solutions. This can catalyse the development of innovations that address the needs of the un- and underserved population.

21 A CGD Task Force Report (2016) 'Financial Regulations for Improving Financial Inclusion'. Available on: https://www.cgdev.org/sites/default/files/CGD-financial-regulation-task-force-report-2016.pdf

22 Genesis (2019) 'Fintech Scoping in South Africa'

23 The Hub will comprise of three elements namely, Regulatory Guidance Unit, Sandbox and Accelerator.

5.4 Support small financial service providers who typically serve lower income customers with simple and affordable products

The FSCA has a statutory objective to protect financial customers through regulating financial institutions. However, we have acknowledged that regulation can be a barrier to entry and can frustrate efforts to promote financial inclusion through a diversification of financial service providers. Regulations can be complex and difficult for small financial institutions and intermediaries to understand. Many of these smaller financial entities play a vital role in serving lower income and underserved populations.

In this regard, we will roll out regulatory support programmes aimed at ensuring small business wanting to enter the financial services industry understand and comply with licensing requirements. For existing licensed entities, we will also provide guidance and assistance with understanding regulatory requirements and developing a sound compliance culture. This project will assist in supporting better access to and usage of financial products and services.

5.5 Promote the supply of appropriate financial products and services to SMMEs

SMMEs can play an important role in driving economic growth and job creation. Support of SMMEs is identified as a priority of broad government policy. For the FSCA, the participation of SMMEs as financial customers in the financial sector is a key aspect of an inclusive financial sector. It is acknowledged that these businesses may struggle to access appropriate financial products and services, in many instances relying on using products and services in their personal individual capacities as business owners. This can have a negative impact on the long-term sustainability of their business.

To address this, the FSCA will work with stakeholder partners to drive the delivery of appropriate financial products and services specifically designed for SMMEs operating in the country. An initial key focus area will be to collect and analyse recent data regarding SMME access to and use of financial products and services.

5.6 Create a regulatory and supervisory framework that promotes financial inclusion

The FSCA has a statutory objective of protecting customers by ensuring that financial institutions treat customers fairly. In considering what degree of protection may be appropriate for customers, the FSCA must have regard to, amongst others, promoting financial inclusion. This include ensuring that regulatory and supervisory frameworks are proportionate to the risks, nature and scale of financial institutions and allow for progressive realisation of requirements[24].

The principle of proportionality has become an increasingly relevant in promoting diversity of financial service providers and encouraging new entrants into the market. Appropriate frameworks can also support the development and distribution of products and services that better meet the needs of low-income or underserved customers. Appropriately designed regulatory frameworks can address access and usage issues,

but are also crucial for ensuring the high quality of products and services delivered in the market

Regulatory considerations for each of these dimensions is set out below:

Access

- Under a proportional regulatory framework, regulatory requirements should be designed in such that they vary with the benefits and the risks associated with a financial service or provider of financial services. The aim should be for a regulatory framework that enables, rather than inhibits, entrants into the market and appropriate innovation[25]. The Insurance Act for example created a new category of insurance – microinsurance – specifically aimed at driving financial inclusion by promoting a diversity of suppliers to drive access to simple insurance products. This is done through tailoring regulatory requirements such that they are more appropriate for the lower level of risk that simpler products should pose.
- Licensing is a critical component in the regulatory framework and serves a key function in the supervision value chain[26]. It is the first entry point for all applicants into the sector.
- It is therefore essential that licensing processes are not only efficient and robust but promote a diversification of financial institutions. We will ensure that licensing requirements do not pose unnecessary barriers to entry. Applications should be individually assessed to evaluate where it may be appropriate to grant licenses subject to conditions or to allow gradual realisation of requirements.

Usage

- Where there is an identified lack of appropriate products (e.g. savings and investments products) that meet the need of low-income or underserved customers, we may develop product standards to incentivise the development of simple, appropriate or better value products and services.

Quality

- Our supervisory approach, including the exercise of our supervisory powers, should be specific to the financial institutions' risk profile. In deciding how best to develop this approach, we will be guided by primary objectives of protecting customers. The approach must also be cognisant of financial inclusion. The supervisory approach, for example, can assist in ensuring that products that are designed for and marketed to lower-income consumers are appropriate to their needs; ensuring that disclosure requirements ensure better understanding of products and services; and overall that the quality of financial products and services support confidence and trust of financial consumers participating in the sector.

5.7 Cooperation with other stakeholders

As noted earlier in the strategy, the achievement of effective financial inclusion requires a multi-stakeholder effort. For our financial inclusion efforts to be impactful the FSCA must engage, cooperate and partner with other stakeholders. In this regard, we will actively participate in the financial inclusion working group established under the Financial System Council of Regulators.

Through our participation at the Financial Sector Transformation Council, we will advocate for the development of standards that will encourages the financial services sector to design appropriate products for low income earners and distribute these products through channels convenient and affordable to customers.

24 FSCA Regulatory Strategy
25 Principles and report on innovative financial inclusion from the Access through innovation Sub-group of the G20 Financial inclusion Experts Group (2010)
26 FSCA Regulatory Strategy

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