FINANCIAL SERVICES:

Best Practices and the Uniform Application of Standards

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The Flow

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- My approach
- Ihiagwa as a case study:
  - The development of financial goods and services in Ihiagwa
  - Risks, mitigation, market failure and the need for regulation
  - Government Intervention in the local financial services industry
  - Ihiagwa, in the global crucible
- Application of best practices and uniform standards
- Financial services, best practices and fiscal responsibility

FINANCIAL SERVICES: What they are not, what they are

- Items such as loans and insurance are financial **goods**, and not financial **services**. A good is something tangible that lasts (whether for a long or short time), while a service is a task that someone performs for you.
- A financial service is not the financial good itself - say a mortgage loan to buy a house or a car insurance policy – but “something that is best described as the process of acquiring the financial good”(Asmundson, 2011).

My Appproach

- First, it is my intention to use the case of my rural African community of Ihiagwa (in Owerri West Local Government Area of Imo State, Nigeria) to describe the organic development of financial services, and use it to highlight the gaps in best practices and the imperative of the uniform application of standards.
- Secondly, I will use the terms ‘he, him and his’ in a gender-neutral sense to also represent ‘she, her and hers’ respectively.

The development of financial goods and services in Ihiagwa

- As a little boy growing up in Ihiagwa, our community had no commercial bank, no insurance company, no stock brokerage enterprise, no investment funds business, no credit union, no financial technologies (fintech) as we know them today, and none of the other institutions currently associated with the financial sector.
- the principal occupation of our people was farming – producing yam, cassava, cocoyam, pepper, palm wine and other staples for household consumption and for sale to the local market in exchange for money with which other needs of the family were addressed
- Few were involved in MSMEs and the public service

the need for savings (financial goods)

- In the course of their farming activities, our men and women confronted the need to handle the money earned from sales of excess produce
- To preserve their money from being misplaced, stolen or degraded, some people dug secret vaults in the floors or the walls of their sleeping rooms and secured the currency notes and cash therein.

Risks associated with cash holdings

- Many lost their wealth to termites which ate up the currency notes (Because the houses were built with mud, and insecticides were not as commonly accessible as they are these days)
- Also, though housebreaking was not common, some persons still lost their wealth to theft

Risks associated with cash holdings - 2

- Even when the problem of keeping their cash safe was solved, there remained the challenge of how to keep the savings in a form that could earn some returns
- Inflation is not an entirely new phenomenon in my part of the world. Even as at the 1970s, money frozen as cash in the hands of households lost some value over time.

The local loan market

- Savings and loans developed organically in Ihiagwa community from the need to meet local needs
- Successful farmers and traders sometimes found themselves with more liquid funds than they needed at some point in time. At the same time, a spattering of households and small businesses wished for funds in the form of loans to help tide them over one situation or another

The local loan market

- The markets where such idle funds could be loaned out for interest were either missing altogether, or too complicated for most of the village household heads to interrogate, or too far to get to.
- It was through private search efforts, referrals and sheer coincidences that the double coincidence of wants would be met.

Access to commercial banking and other financial facilities

- The earliest branch of a commercial bank close to our Ihiagwa community was the Owerri branch of African Continental Bank (ACB)
- A three-hour walking distance from my village to the bank was a short distance at the time, relative to what many other communities had to go through.
- However, a single transaction at the bank could take the better part of a day; also, the processes appeared complicated to the village man. This made the use of the services of the commercial bank by our smallholders - even just for purposes of depositing their rather little sum - arduous.

‘Esusu’ to the rescue

- The gaps were filled by **ESUSU**, a local contributory savings and capital accumulation exercise
- Members of an age grade, trade or similar groups in a community would agree to make daily, weekly, or monthly contributions to the group from their sales or earnings.
- The total contributions in a period are handed to a member of the group and the practice is repeated until each member takes his turn.
- This model serves the purpose of savings and capital accumulation amongst participants. It is self-organizing, attracts no service charge/fees and self-dissolves at the last cycle.

Variants of ESUSU

- With the passage of time, the village began to see commercially-minded variant(s) of the "Esusu" system that were imported from the city
- In the variants featured itinerant cash deposit collectors whose enterprises are structured as savings/thrift cooperative societies
- Deposits are treated as daily or weekly contributions from members of the cooperative
- The itinerant collectors would return the sum of a person's contributions in bulk at an agreed period, while keeping a small percentage as reward or service charge. The exercise provided a participant the opportunity for savings, loan and capital accumulation, at a small fee.

Financial services are later comers - 1

- Though savings and loans developed organically in Ihiagwa community from the need to meet local needs, the provision of associated financial services was slow to catch up.
- The commercial provision of loan brokerage services, negotiation support, (re)securitization of loans, structuring of terms of agreement, recording and recall of loan agreements, arbitration, enforcement of agreements, etc. are later comers to the local finance sector in Ihiagwa.

Financial services are later comers - 2

- Even where the services existed, they were initially largely on *pro bono* basis and the market for them was missing.
- It was queer, for instance, for someone to ask to be paid in order to help arrange or structure a facility from a money lender or even from a bank. Such a broker would be considered lazy, mean, insensitive, capable of selling his own mother for a mess of porridge, and worth avoiding at all cost
- (“How do you tell someone who needs financial support to pay you simply for helping to link him to a willing lender?” our people would ask)

Financial services are later comers - 3

- With time, certain persons became known in the local and farther communities for money lending.
- The lenders found ways to deepen the financial services space by developing relationships with associates that wrote loan agreements, registered agreements at the courts and enforced agreements using legal and not so legal means.
- In addition, a lenders soon found a need to develop relationships with persons that availed him quick access to loans when required, hence a form of informal subsidiary banking developed out of sheer market need.

RISKS, mitigation, and the need for regulation - 1

- In the case of person-to-person loans, lenders soon they found themselves faced with the challenge of ascertaining if a borrower would meet his obligations as and when due
- Oftentimes, the loan is made based on goodwill – with no collateral involved. At other times, the collateral could be the right to farm on a piece of land until such a time that the facility is repaid.
- In many cases, there was no interest and no clarity over the loan tenor; hence, a lender could find his funds trapped for decades and repaid by the original borrower’s descendants at a time when, in the light of inflation over time, the value of the loan would appear paltry.

RISKS, mitigation, and the need for regulation - 2

- The local 'Esusu' finance model has its own risks:
  - Default by any of the participants,
  - A beneficiary losing his "winnings" to theft or robbery.
- Similarly, the model of itinerant deposit collection entails a risk of an itinerant collector disappearing with people's savings and not being traced. At other times, it is the enterprise for which the itinerant staff works that disappears, leaving depositors bereft of their savings

Risks, MITIGATION, and the need for regulation - 3

- As is normal with businesses at all levels of sophistication, each of the risks has attendant probabilities, impact and mitigants which people of Ihiagwa addressed with unique local methods:
- Where the lending and borrowing parties are from the same community, the *Umunna*, consisting of elders in the clan would be brought in as witnesses to the transaction. This involvement of elders and kinsmen mitigates the risk of default as it places a moral and spiritual burden on the borrower to meet his obligations as agreed

Risks, **MITIGATION**, and the need for regulation - 4

- Furthermore, where the two parties are under an overarching king or traditional jurisdiction, the traditional ruling council consisting of male elders, chiefs and other titled men could be approached to guarantee the transaction and enforce the consequences of default.
- Where, however, there is no co-joint traditional jurisdiction covering the parties, some lenders have had to resort to witchdoctors or priests of traditional religions to administer oath on the borrower. In the event of default, the spiritual order would enforce compliance using spiritual mechanisms that are generally avoided, if not feared, by Africans.

Risks, Mitigation, and THE NEED FOR REGULATION - 5

- Over time, the traditional tools for mitigating the risks associated with lending, borrowing and capital accumulation became increasingly inadequate:
- Our people soon discovered that the *Umunna,* which provided governance and judicial mechanisms for the clan had limited jurisdiction over itinerant deposit collectors whose offices were based in the city
- Some actors began to defy *Umunna*
- Similar limitations applied to local and even state governments

Risks, Mitigation, and **THE NEED FOR REGULATION - 6**

- Soon enough, certain people also began to refuse witchdoctors as guarantors of repayment on the ground that as practising Christians, they had no business ceding regulatory power to supposedly demon-backed systems.
- Moreover, serial defaulters had learnt to ignore the possibility of consequences of default in agreements facilitated by witchdoctors
- The motley risks, confusing nature of terms, variegation in rates and high frequency of backroom manipulations created a need for some **agreed standards of good practice**

Risks, Mitigation, and **THE NEED FOR REGULATION - 7**

- Some service providers relied on peer pressure to achieve compliance; some relied on the judicial system; some relied on the fear of demons. Some service providers were literal sherlocks who administered unfair agreements on poor illiterates and forced them to part with entire family inheritances; some were known for fairness.
- How people paid for financial services varied widely, ditto for how much people paid for the financial services. In addition, the costs were not always transparent.
- In summary, practices varied, thus underlining the need for parameters to determine best practices.

Risks, Mitigation, and **THE NEED FOR REGULATION - 7**

- Moreover, it was clear that in the market for financial goods and services, the suppliers had far more power than the demanders.
- Providers of financial goods and services could fix their rates and terms at murderous levels.
- Many families are known to have lost their entire land holdings after defaulting in repayments of loans of meagre amounts, which agreement document had horrific terms written into them.
- This invites the question: Should the government intervene or fold its hands and let the market be?

Risks, Mitigation, and **THE NEED FOR REGULATION - 8**

- The forces of demand and supply attempted to play some role in stabilizing activities of operators in the local finance sector: If a borrower has good records, lenders would line up to accord his requests; also, a lender or deposit collector would be highly patronized if his services are reliable and kind-hearted.
- **However, the market's capacity to self-regulate was weak and some control was required from an external body, a government**
- Potential lenders began to ask for warrantees, assurances and other confidence-building measures which require a government to enforce

Ihiagwa, in the global crucible

- The Ihiagwa society has since evolved, as has the rest of the world, to the point where diverse types of financial sector transactions in real estate, consumer finance, banking, insurance, investment funding, securities, etc have become both commonplace and part of a global industry.
- With globalization, travel, education, technology, and uptake in transborder businesses, the borders between Ihiagwa and the rest of the world have blurred.
- Diaspora remittances, for instance, are significant.

Ihiagwa, in the global crucible

- Hence the question now is as to whether Ihiagwa - and Nigeria - can have its own standards of good practice as distinct from those of far-flung cities all over the globe where some of its financial services transactions originate, transit or terminate.

Ihiagwa, in the global crucible

- Though the unregulated providers of local financial services in Ihiagwa had the privilege of deciding the terms of their own practices as against what may have held in the rest of the world, they can no longer afford to venture too far from national and international practices.
- The nature and terms of financial services is now influenced, if not exactly determined, by nationally and globally established practices.
- It is no longer easy, or even fashionable, for each provider to structure his own service in his own way. Though witch doctors are still brought in sometimes to guarantee loan repayment, for instance, such occurrences are fringe events.

Ihiagwa, in the global crucible

- It is no longer easy, or even fashionable, for each provider to structure his own service in his own way. Though witch doctors are still brought in sometimes to guarantee loan repayment, for instance, such occurrences are fringe events.
- The question also exists as to how to determine and enforce best practices amongst financial service providers in Ihiagwa who have found themselves unwittingly and inexorably operating in a globalized environment.

Ihiagwa, in the global crucible

- **There is also the question of if, and how, to set and apply uniform standards in the Financial Services Sector across places, and times**
- The truth is that each **community has its peculiarities** which, if it were possible, needs to be recognized in the development and regulation of fit-for-purpose financial services standards.
- However, the large variety of services and confounding complexity in monitoring diverse standards in a plurality of practices across many locations at the same time compel authorities to resort to the adoption of uniform standards for everyone

Best practices and uniform standards

- It has dawned on people of Ihiagwa community that a high authority in the nature of a Government is better placed to determine best practices, establish and enforce standards for even the most local of financial service providers
- Notably, the Federal Government of Nigeria has since enacted laws and established institutions with mandates to set standards in various financial services practices. They also regulate the application of the standards.
- Hence, the Ihiagwa market for financial services has become part and parcel of a single Nigerian financial services market from which it now derives its standards of best practices.

Best practices and uniform standards

- As Nigeria regulates its own standards, so do other nations.
- Similarly, specific practices have their own standards. E.g., insurance, reinsurance, savings, lending, mobile banking, peer-to-peer payments, personal finance, money transfer, transactions in digital currencies, etc.
- The plurality of services and complexity of monitoring diverse standards in a plurality of practices across many locations at the same time make the adoption of uniform standards rather appealing – even where they are not optimal

Application of best practices and uniform standards: Technology to the rescue?

- Technology is a potent tool for both defining and addressing the challenges of the myriad of best practices and uniform application of standards.
- Technology-enabled algorithms and artificial intelligence (AI) deployed through various digital platforms and electronic devices including mobile “smart” phones have made the application of both uniform and non-uniform standards across national boundaries more feasible

Application of best practices and uniform standards: Technology to the rescue?

- However, the same technology also poses peculiar risks to regulators and operators:
  - the easy access to finance (as in personal loans) which technological innovations enable can lead to excessive borrowing and high personal debt
  - the risk of insidious cybercrime which can destabilize and potentially cripple the integrity of the entire financial system.
- The risks are particularly relevant for developing countries given that they generally have very weak cyber-security infrastructure and a lack of capacity to adequately supervise and take the required measures to protect and safeguard the operations and transactions of financial services providers and their consumers.

Application of best practices and uniform standards: Technology to the rescue?

- The risks of inordinate personal debts and cybercrime can be overcome by technology and enhanced regulatory capacity.
- It is important for experts and regulators of financial services across the commonwealth and beyond - including Central Banks, Financial Conduct Authorities, Prudential Regulation Authorities, etc. to work together to forge common best practices and uniform standards, as well as their applications for the efficient delivery of financial services.

Application of best practices and uniform standards: Technology to the rescue?

- Domestic regulatory institutions should be carried along, and also "strengthened" - as in the case of countries with weak or inadequate technological infrastructure - to be able to enforce compliance with standards and best practices in their domains in order to achieve the desirable cooperation that would improve the global financial markets.
- As for the uniformity of standards, regulators of financial services need to give consideration to local peculiarities and strike the right balance between universal practices and the need to engender sustainable growth, create new jobs and enhance productivity in local economies.

Financial services and fiscal responsibility

- In my position as the Executive Chairman of Fiscal Responsibility Commission in Nigeria, I see the benefits and promises of good practices and application of standards in financial services.
- In embracing the open governance initiative, the Federal Government of Nigeria is working with financial services providers for seamless, real-time financial transactions, reporting, monitoring, evaluation and projections.

Financial services and fiscal responsibility

- Financial services have also become big revenue earners for the government through licensing, regulation, and supervision.
- In addition, the application of standards across boundaries have eased the burden of regulations.
- Improvements in the financial services sector have tremendously improved the remittance of taxes and other forms of revenue into the Government treasury.
- Taxpayers now pay their taxes without much stress by using any of the many available payment financial services apps.

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- Taxpayers now pay their taxes without much stress by using any of the many available payment financial services apps. In recent years, the Nigerian government introduced a Treasury Single Account (TSA) policy by which all payments received, or revenues collected on behalf of the government, goes through a single payment portal. This technology-enabled financial service has greatly enhanced accountability and transparency in government’s revenue and expenditure profiles.

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- Accordingly, financial services have advanced the cause of fiscal responsibility which simply means, to ensure prudent, transparent and accountable management of the public treasury and ensure the integrity of the budgeting process while holding down public debts at sustainable levels.

In Conclusion

- The benefits of a uniform application of standards and best practices in the financial services sectors of the communities and States in the Commonwealth and beyond is enormous.
- There is, however, a real need to accommodate local peculiarities in the development of and application of standards
- In order to achieve the goal of a uniform application of minimum standards, therefore, there is a need for more financially and technologically endowed nations to assist the weaker ones in ramping up their regulatory capacities.

Thank you

- As we say in Ihiagwa, Unu emela. Chineke Gozie anyi nile.

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