CIPF Podcast Series – Innovation
No. 10 - Financial Innovation from a Global Perspective

Transcript[1]

Moderator: Ilana Singer
Speaker: Mahesh Uttamchandani

Ilana Singer:

Hello, and welcome to the CIPF Podcast series on "Innovation". I'm Ilana Singer, Vice-President and Corporate Secretary at the Canadian Investor Protection Fund, or CIPF for short. I am so pleased to have Mahesh Uttamchandani as our guest today. Mahesh works at the World Bank Group where he is the Practice Manager for Financial Inclusion and Infrastructure in the Finance, Competitiveness and Innovation Global Practice. In this role, Mahesh manages the World Bank's global work on payment and market infrastructures and responsible financial access. Among other things, he also oversees the World Bank's insolvency and credit rights task force, and he jointly leads with an international finance corporation co-head, The Universal Financial Access 2020 Initiative. Mahesh, welcome. We're so delighted to have you here with us today.

Mahesh Uttamchandani:

Thanks for having me, Ilana. It's great to see you.

Ilana Singer:

Same here. Our topic for today's podcast is "Innovation". In our discussion, we will delve into some of the work being done by Mahesh and his team at the World Bank, exploring how recent innovations have changed his approach to this work. And we will also hear about recent research undertaken by the World Bank that focuses on technological innovations in financial services from the perspective of consumers. Drawing on articles recently co-authored by Mahesh, we will also discuss insolvency and debt restructuring reforms that have been and continue to be undertaken in response to the current pandemic, as well as past crises.

Ilana Singer:

To begin, let's start with our first question. Mahesh, please describe for our listeners your principal areas of focus at the World Bank.

Mahesh Uttamchandani:

Thanks, Ilana. I should say at the outset that I'll probably be expressing some opinions during our discussion, and those are my own opinions and not those of the World Bank Group, it's senior management or its' shareholder countries.

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[1] This transcript has been edited for clarity and ease of reading. This podcast is for informational purposes only and is not intended to constitute advice of any kind.

Mahesh Uttamchandani:

Essentially, the work that I oversee is our work on what we like to call the ‘plumbing’ for the financial system. It includes all of our work on payment systems, debt enforcement and insolvency, and the broad space of financial inclusion and consumer financial protection. Our work in these areas has global reach and so I oversee all of the technical work we do in these areas across about 150 emerging market and developing countries. Interestingly, particularly in the financial inclusion and payment spaces, innovation has really been at the forefront of this work because FinTech, as you know, has completely transformed the landscape for financial services around the world.

Mahesh Uttamchandani:

If you look at what's going on in developing countries in financial services, there's so much innovation that it's really staggering. We have non-banks playing an increasingly large role in offering mobile wallets and digital payment services to customers who typically haven't had access to these services before. In Kenya, for example, we have this mobile money product called M-Pesa that you may have heard of that has really taken flight, and it has been adopted by such a high percentage of Kenyans that it's used in daily transactions, almost as much as, if not more than, cash. Similarly, in India, there's been a huge proliferation of digital financial products ranging from consumer and SME credit to micro-insurance that have really brought a customer-centered approach to finance.

Mahesh Uttamchandani:

One particular area I'm excited about is micro-insurance that's being provided or sold to very low-income families to protect them against the kinds of calamities that they tend to suffer. So, someone in the family getting their bicycle stolen, for example, which is the primary means of transport, or someone getting malaria or dengue fever. These are all things that can be devastating to the health of a low-income family, and for which there are now micro-insurance products that they can buy to protect against that risk.

Mahesh Uttamchandani:

I think, separate from that, many of your listeners might be surprised at the sheer variety of financial products available to consumers in some emerging markets, and, dare I say, that some of these markets may be more innovative in offering financial services than what we have here in Canada. In many ways, it reminds me of the early days of mobile phones. I know I'm dating myself here, but I know you won't mind since you and I used to study together for our law school admission test back in our days in Kingston together. But if you remember, we have had very good quality affordable landline technology in Canada for a long time. I think, in some ways, this made us slower to take up innovations in cellular technology. For a long period, countries that previously had weak landlines were more incentivized to move faster on taking up the new technology that mobile phones offered. That's why, for so long, Europe seemed so far ahead of us in Canada on mobile phone availability and pricing.

Mahesh Uttamchandani:

I think the same thing is happening in financial services. We've had such a high rate of financial inclusion in Canada for so long. I think it's probably been over 90% for a long time - that basically anyone who wants access to basic financial services can get it. But I think this has made us a bit slower to adopt innovations like person to person micropayments or digitizing government to person payments. I mean, if you look at countries that have recently built the digital rails to move money from governments to individuals electronically and built robust, biometric digital ID frameworks, it's amazing how quickly they were able to get emergency COVID payments to their citizens. For these countries, the idea of sending out cheques to individual postal addresses would have seemed absurd! I mean, the example of India is really interesting to me where they have onboarded about 1.1 billion people over the last few years with a national biometric ID that allows all of the KYC due diligence to be done remotely using a $5 dongle that you'd attach to your computer that can take a biometric measure like a fingerprint. That allows for simple onboarding of customers and it allows for both the government and financial institutions to easily find their customers or recipients of payments.

Mahesh Uttamchandani:

I could talk about this subject for hours but let me just add that some of these innovations are now coming to advanced and developing economies at the same time. I think in the coming months and years, we'll see a lot of activity on things like stablecoins and Central Bank digital currencies, where advanced and emerging markets will be grappling with these issues, at the same time, and without a playbook as to how to regulate or manage these new technologies.

Ilana Singer:

Thank you, Mahesh. I find some of these innovations that you've described, particularly those in emerging economies, to be quite incredible, and particularly in the context of the COVID-19 pandemic and beyond. Are you seeing these types of innovations playing out in the business community as well or is it really just relating to the inclusion from a financial perspective of individuals?

Mahesh Uttamchandani:

Oh, it's definitely for businesses as well, particularly small and microbusinesses. Ilana, one of the things that concerns me most as we hopefully come out of this pandemic, is how disproportionately it's impacted women, both in their capacities as employees and workers, but also as business owners. We know that women-owned businesses have been particularly hit hard by the pandemic, and, in fact, were less likely than male-owned businesses to even access available public support in the countries where it was available. One of the things we're looking at, for example, is how to increase access to finance for women-owned businesses. Credit scoring and underwriting for business is a fertile ground for work on this. We've been working in Ethiopia, for example, where women-owned businesses have typically been constrained in their access to credit, partly because female entrepreneurs often have so-called “thin” credit files, meaning they don't have a long history of financial transactions in their own name which, as we all know, helps establish the ‘breadcrumbs’ or the trail of your credit history, and makes evaluation of your creditworthiness easier for potential lenders.

Mahesh Uttamchandani:

Instead of relying on these traditional methods, we worked with an exciting FinTech partner that helped develop a psychometric scoring tool, which essentially involved lenders loading up these psychological tests on tablets and being able to go out into the field and have potential borrowers complete the test. That test is then used to determine creditworthiness using an algorithm developed by the FinTech and has proven to be as good or better than traditional credit scoring for predicting repayment. By using these, thousands of female entrepreneurs have been able to get access to loans when traditional underwriting models would've left them excluded.

Mahesh Uttamchandani:

Another exciting thing we are seeing is the use of platform data. A lot of large platform businesses in emerging markets - and I'm talking here about companies that, in a local market, might be a competitor to the Amazons of the world – serve as platforms for individual small business vendors. Because the platform can track the payments data to and from individual vendors, they can use an algorithmic scoring model to determine individual vendor's revenue streams and use that as a basis for providing credit to the vendor. They can also use it to track sales and offer products such as receivables factoring.

Mahesh Uttamchandani:

Now, of course, we have to be mindful of monopolistic concerns with these very large platforms and issues such as data privacy and data security. We also need to be aware that algorithmic models of credit scoring can sometimes be ‘black boxes’ that could actually reinforce biases. In other words, algorithms are just code, and code is ultimately written by humans, and humans, as we all know, have inherent biases. I don't want to minimize the risk of any of these challenges, but I do think it's a very exciting time and there's so much opportunity to serve businesses that have traditionally not been well served by finance.

Ilana Singer:

Mahesh, what you have done with your FinTech partner and with these algorithms that you've described in emerging economies is fascinating, and I'm sure that we have a lot to learn from these experiences in Canada and other markets. Now, tying this into what we do here at CIPF, we focus on returning customer property after an investment firm has become insolvent. I understand that the World Bank recently undertook research in the area of innovation with a focus on consumers. Can you elaborate a little on this work, Mahesh, for our listeners?

Mahesh Uttamchandani:

Sure. It's interesting to me that, over the last 30 years or so, we've had some kind of seismic financial shock about every 10 years. So, we had the Asian Financial Crisis in the late 1990s and early 2000s, then the global financial crisis in '09 and 2010, and, of course, now a global pandemic that has hit the real economy very hard and threatens to bring deeper financial shocks.

If we go back to the Asian Financial Crisis, that actually spurred coordinated activity amongst the G8 countries and the G36 - as they were then called - including Canada, of course, to develop an international financial architecture. That's what they called it - an international financial architecture that included developing standards for critical areas of the financial sector, such as, of course, capital markets and insolvency.

Mahesh Uttamchandani:

In the early years of this initiative, a lot of this work naturally focused on corporate insolvency, but in recent years, there's been a recognition that SMEs and microbusinesses have their own unique needs when dealing with debt restructuring and liquidation. We know that globally, micro, small and medium enterprises provide about 60% or 65% of employment globally. Even though individually they're small, in aggregate, they're huge. And we also know that they've been hit particularly hard during this pandemic. They were more likely to shut their businesses down, and less likely to be able to cover their costs during the local shutdowns in the pandemic. So, in 2021, after a wide consultation with practitioners, judges, academics, and policymakers from around the world, including several brilliant minds from Canada, we developed new guidelines for countries to reform their insolvency systems in a way that is conducive to responding to the needs of micro, small and medium enterprises. These guidelines are embodied in the World Bank Insolvency Principles and the UN Commission on International Trade Law's insolvency legislative guide. Now, they don't focus specifically on consumers as consumers, but certainly touch on critical issues affecting individuals in their capacity as sole proprietors and entrepreneurs. As you can imagine, in many small economies, it's often hard to distinguish between the individual in her personal capacity and in her capacity as an entrepreneur.

Ilana Singer:

Mahesh, thank you for all of that. For the benefit of our listeners, we will be adding a link to the World Bank Insolvency Principles into our show notes for reference purposes. These sound very interesting and we look forward to reading them. You have also co-authored several pieces relating to the impact of COVID-19 on a number of areas in financial services. Can you elaborate on a handful of these, including your recent piece about insolvency and debt restructuring reforms that were undertaken in response to the pandemic, as well as past crises?

Mahesh Uttamchandani:

Sure. If you think back to March 2020, which seems like a lifetime ago now, there was a huge concern around the world that there was going to be a wave of business failures, partly due to the shutdowns and the disruption being caused by COVID. So, the language we were using, in terms of COVID cases, was about flattening the curve of hospitalizations, and that language was adopted ultimately by policy makers, looking to flatten the curve of insolvencies and non-performing loans by creating some kind of breathing room for businesses, individuals, and financial institutions to prevent a widespread economic collapse.

Mahesh Uttamchandani:

So, we conducted a pretty comprehensive survey of about 85 countries to try to understand what countries did in this area in response to the pandemic. And over 95% of the countries we surveyed had made some sort of modification to their insolvency and debt restructuring framework in 2020. I would say that the most common types of reforms they undertook fell into three broad buckets. The first and largest was some relaxation of the requirements for debtors to repay their debts. And about 80% of countries surveyed did this in some form, whether through moratoria, extensions to loan timetables, or even the extraordinary measure of closing the courts to prevent enforcement. The second most common type of measure were those designed to block or make it harder for creditors to initiate recovery or bankruptcy proceedings, and slightly under half the countries we surveyed did this. And the third most common type of measure was to change legal duties, in particular, shielding company officers and directors from their obligations to file for insolvency, and about a third of the countries we surveyed did this. Now, as I said, the premise for these emergency measures was that, if no action was taken, there would be a drastic increase in business and personal bankruptcy and rapid wide-spread rises in non-performing loans, which would increase the risk of some sort of financial sector disruption, or in the worst case, even a collapse.

Mahesh Uttamchandani:

What we know now though, is that unusually for a recession, the available data suggests that the COVID-19 pandemic era has seen bankruptcies decline, at least so far. This is true in Canada as well. Now, if we look globally our best estimates tell us that about six months into the pandemic, bankruptcy filing rates were sitting at about 80% of pre-pandemic levels. Now, compare and contrast that with 10 years ago with six months into the global financial crisis, and bankruptcy filings had increased to 150% of pre-financial crisis levels. So, a very stark difference between this crisis and the previous crisis. One interesting data point from Canada, which is aligned with other wealthy countries is that, while the overall number of bankruptcy filings has dropped, there's been an increase in the large volume cases. We know that some very large corporates and some very hard-hit sectors have gone into, as it's known in Canada, the CCAA, and restructured, but overall, the number of cases has gone down. I think our analysis of this suggests that it's possible that the temporary measures and fiscal support that countries brought in has actually worked. I think that's really good news. What we don't quite yet know is, as these temporary measures are withdrawn, and as the financial support recedes, will insolvency filings and non-performing loans increase? I think that is a legitimate open question that policymakers and financial institutions and businesses around the world are starting to grapple with.

Ilana Singer:

Thank you, Mahesh. Similar to the guidelines that you mentioned earlier, we will include your survey piece in the show notes to this podcast. It's fascinating. I think our listeners will be very interested to see the details relating to the survey that you conducted, particularly as it relates to the impact on the financial sector. Well, unfortunately, we're coming to the end of our podcast. Mahesh, it has been a pleasure having you with us today. It's been an inspirational, forward-thinking and thought-provoking discussion.

Mahesh Uttamchandani:

Thank you for having me, Ilana. It's been a real pleasure.

Ilana Singer:

Three key takeaways that I've drawn from the discussion today are as follows:

1. Innovation in financial services in emerging markets is developing at an extraordinary pace since FinTech has been transforming their landscape.
2. Advanced and developing economies are grappling with some of these same innovations and without a playbook on how to regulate or supervise them.
3. And finally, it seems like there is quite a difference between the impact of this pandemic and the impact of past crises on the financial sector. And also, the long-term effects of this pandemic still remain an open question.

Ilana Singer:

I'd like to close by thanking our listeners for their attention. I hope that you have found the discussion as stimulating and interesting as I have. We always welcome your comments, and the best way to reach us is through our website. Finally, we invite you to listen to CIPF's other podcasts available on our website and podcast channels, or feel free to read the transcripts which are available in both English and French. I'm Ilana Singer, and goodbye for now.