Chapter 4

ADVANCING INCLUSIVE FINANCIAL SYSTEM IN THE NEXT DECADE IN MALAYSIA

By
Zarina Abd. Rahman
and
Wan Mohammad Zainuddin Mohammad Zaini[1]

1. Introduction

In 2009, the Malaysian Government introduced the New Economic Model (NEM) which outlines the direction for transforming Malaysia into a high income economy, supported by sustainable growth. Inclusiveness, alongside high income and sustainability, is one of the key desired outcomes of this vision. The participation of the bottom 40% of households based on income stratification in the overall economic and financial sector growth is seen as key to achieving economic prosperity as well as maintaining social cohesion. Although absolute poverty has largely been eradicated in the 57 years since the Independence of Malaysia in 1957, a significant portion of Malaysian households continue to earn less than RM18,000 (US$5,625) annually – significantly lower than the desired annual income goal of RM48,000 (US$15,000) by 2020.

Malaysia acknowledges that an inclusive financial system plays an important part in ensuring sustainable long-term economic growth. Evidence shows the strong positive correlation between the level of financial inclusion and the stage of development of an economy, whereby a higher degree of financial inclusion will contribute to overall economic development[2]. An inclusive financial system provides the more disadvantaged segments of society with access to quality essential financial services and the means to accumulate wealth through savings. It also promotes broader access to financing for investment in economic activities,

1. Authors are respectively Manager and Analyst of Development Finance and Enterprise, Bank Negara Malaysia.
2. Demirguc-Kunt, A.; T. Beck and P. Honohan, (2008), “Finance for All? Policies and Pitfalls in Expanding Access,” Washington, D.C.: The World Bank.

thus creating opportunities for the poor to improve their standard of living. Studies using controlled randomised approaches prove that financial inclusion, especially when designed appropriately, improves the welfare of the poor[3].

2. Supporting Framework for Financial Inclusion in Malaysia

Malaysia's financial sector development policies have facilitated the nation's balanced growth through the realisation of the social and economic benefits of financial inclusion. This includes deliberate measures taken to complement market-oriented development in enhancing and expanding financial services for the broader community and economic sector as well as strengthening the financial infrastructure and institutions to enhance and create an inclusive financial system. Some of the key initiatives are discussed below.

2.1 Strengthened Legal Mandate and Accountability

The Central Bank of Malaysia Act 2009 (CBA 2009) was enacted in July 2009 to replace the Central Bank of Malaysia Act 1958. The CBA 2009 explicitly states that a primary function of Bank Negara Malaysia (BNM, the Central Bank of Malaysia) is to develop and promote an inclusive financial system. Supported by a clear mandate, BNM has been the leading agency responsible for the policies and initiatives aimed at promoting financial inclusion in Malaysia.

2.2 Creating Diverse Institutions to Meet the Needs of the Underserved

Malaysia has created a facilitative business environment that supports the creation of a diverse range of institutions to thrive and compete. In 2006, commercial banks were encouraged to play a key role in expanding access to financing for micro enterprises through the *Pembiayaan Mikro* framework[4]. The framework provided an important platform for the provision of sustainable microfinancing by financial institutions (FIs). Under this framework, micro-enterprises could access uncollateralised business financing in a fast, easy and convenient manner. FIs that participate in *Pembiayaan Mikro* benefit through a shared branding including a common microfinance logo, advertising and promotional platform for their microfinance products. Currently, there are 10

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3. Bauchet, M.; T. Starita and A. Yalouris, (2011) "Latest Findings from Randomized Evaluations of Microfinance," CGAP Access to Finance Forum, No. 2., December 2011.
4. The framework was established following the results of the *2005 Census of Establishments and Enterprises* by the Department of Statistics Malaysia. The Census highlighted that only 13% of micro-enterprises obtained financing from formal FIs.

participating financial institutions (PFIs) providing sustainable micro financing under this framework, with more than 2,400 access points nationwide[5]. The products under this scheme offer financing of up to RM50,000 (US$15,236) with a median approval and disbursement time of 5 working days. Business financing provided by the financial institutions under this scheme is augmented by the Micro Enterprise Fund (MEF) that provides funds at favourable rates for FIs to on-lend to micro-enterprises. The Fund allows the FIs to manage the cost which would have otherwise been high due to the small financing size. Through the MEF, commercial incentives are maintained to drive the provision of microfinancing in a sustainable way. As at end-2013, outstanding micro financing of the PFIs stood at RM857.0 million (US$267.8 million) involving 68,360 micro financing accounts. Supportive financial infrastructures such as credit bureaus have also allowed the commercial banking institutions (BIs) to thrive with differentiated strategies based on their strengths to deliver a broader range of products and services to meet the diverse needs of consumers and businesses.

BNM has also encouraged the growth of Islamic banks in parallel with conventional banks to ensure that all segments of society are served. Islamic financing products and services provide financing options which are aligned with the principles and economic requirements of the underserved. The Islamic banking sector has recorded a significant growth over the last decade and currently accounts for 25.7% of total banking assets[6].

At the same time, development finance institutions (DFIs), cooperatives and micro finance institutions (MFIs) also have an important role in serving niche groups of customers in Malaysia. With a wide distribution of networks across the nation including the rural areas, DFIs and cooperatives complement the other financial institutions[7] in providing businesses and consumers with alternative sources of accessing financial services. There are more than 10,000 cooperatives nationwide with financing disbursed amounting to RM25.2 billion (US$7.9 billion) in 2013. Of this amount, RM20.10 billion (US$6.13 billion) were approved by the two co-operative banks in Malaysia[8].

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5. These financial institutions adopt various sustainable business models such as a mass market model which leverages on existing branches, dedicated micro-finance branches, co-operative model and partnership with strategic distributors.

6. Bank Negara Malaysia, (2013), "Malaysia as an International Islamic Financial Center," Financial Stability and Payment Systems Report.

7. Bank Negara Malaysia, (2007), Financial Stability and Payment Systems Report.

8. Bank Kerjasama Rakyat Malaysia Berhad (Bank Rakyat) and Koperasi Bank Persatuan Malaysia Berhad.

In addition, MFIs such as Amanah Ikhtiar Malaysia (AIM) and TEKUN were established to further the micro finance agenda. AIM is a private trust that was established in 1987 with the objective of assisting the hard core poor to come out of the poverty trap. This is done through the provision of micro financing for various income generating activities through its 123 branches nationwide[9]. AIM adopts the Grameen Bank model where financing is given to groups of borrowers, primarily women. These types of financing do not require collateral or guarantors, and the recovery of the impaired debt involves engagements with self-help groups without necessary recourse through legal action[10]. As at end-2013, AIM has more than 404,000 micro financing accounts with loans outstanding of RM1.5 billion (US$0.47 billion). Similarly, TEKUN provides micro financing especially to the rural communities for income generating activities as well as to support entrepreneurs, mainly in agriculture and agricultural-based sectors. Established in 1994, it now has loans outstanding totaling RM1.7 billion (US$0.53 billion) as at end-2013. AIM provides financing up to RM20,000 (US$6,095) with tenures of up to 150 weeks, while TEKUN provide financing up to RM100,000 (US$30,473) with tenures of up to 10 years. As at end-2013, these MFIs have cumulatively approved RM12.7 billion (US$3.9 billion) in loans to 3.1 million micro entrepreneurs.

The Credit Guarantee Corporation (CGC) is another key institutional arrangement facilitating greater access to financing by the small- and medium-enterprises (SMEs). By providing credit guarantees to business loans, CGC addresses the issue of lack of collaterals, which is one of the main constraints faced by small businesses. Since its inception up to end-2013, the Corporation has guaranteed RM50.3 billion (US$15.7 billion) in financing involving 417,149 accounts.

2.3 Enhancing Oversight Arrangements for Non-banks

The Development Finance Institution Act (DFIA), enacted in 2002, gives BNM the oversight responsibility to ensure the six DFIs perform their mandated roles in an effective and prudent manner, supported by strong corporate governance and sound financial and business practices. In particular, the National Savings Bank (Bank Simpanan Nasional, BSN) was mandated to mobilise savings in the underserved areas and promote microcredit. The Agricultural Bank

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9. As at-end 2013.
10. Amanah Ikhtiar Malaysia, "Sejarah," Available at: <www.aim.gov.my/~cms/KenaliAIM/Sejarah.htm>.

(Agrobank) was corporatised to enhance its capacity to serve the agricultural sector in a sustainable way, while the SME Bank was established to serve the SME sector. The DFIA also gave BNM oversight responsibility over Bank Kerjasama Rakyat Malaysia Berhad (Bank Rakyat), the largest of the cooperative banks.

BNM has accorded special attention to supporting DFIs which play an important role in serving strategic sectors. Amendments to the DFI Act are being proposed to further strengthen the regulatory and supervisory framework supporting the ability of DFIs to serve their respective mandates effectively. The amendments are scheduled to be tabled to the Malaysian Parliament in March 2015.

In January 2008, the Cooperatives Commission of Malaysia (Suruhanjaya Koperasi Malaysia, SKM) was set up to regulate the development of cooperatives. Apart from exercising a supervisory role over all cooperatives in Malaysia, SKM also aims to create an ecosystem that is conducive to the development of competitive cooperatives through the provision of grants and financing.

2.4 Promoting Basic Banking Products

Increasing access to basic banking services and products such as financing and savings accounts is essential to bring more businesses and households into the formal financial system. Greater participation in the formal financial system in turn, will contribute towards increasing business investments and personal incomes[11]. In 2005, BNM issued a Guideline for Basic Banking Services which required all commercial banks to provide basic banking services. This is to ensure that all segments of society have access to basic deposit and transaction services at a reasonable cost. This Guideline outlines the features of basic savings and current accounts which have low minimum initial deposit requirements, offer reasonable savings rates and provide free over-the-counter and ATM transaction services. As at end-2013, 18.4% of all savings accounts in the financial system are basic savings accounts.

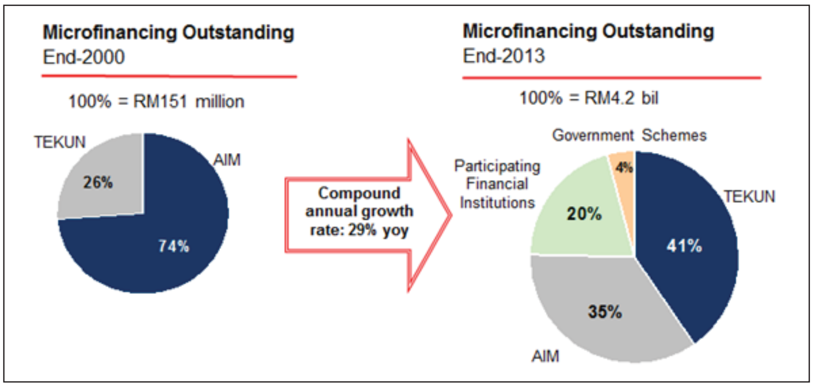
11. Dupos and Robinson, (2011), "Savings Constraints and Micro Enterprise Development: Evidence of Field Experiment in Kenya," *NBER Working Paper*, No. 14693.

Table 1
Features of Malaysian Basic Savings Accounts

Type	Nature of transaction	Number of transactions per month provided by the FIs without charge
Over the counter visit (OTC)	Account enquiries, deposits, withdrawals, funds transfer within the same bank and bill payments	6*
ATMs	Balance enquiries Withdrawal Funds transfer within the same bank	No limit 8* No limit
Deposit Machines**	Cheques deposits Cash deposits	No limit No limit
Interbank GIRO	Interbank funds transfer	2
Internet Banking	Account enquiries Bill payments Funds transfer	No limit No limit No limit

* Additional transactions may incur a charge as determined by the financial institution.
** If deposit machine facilities are not available at the branch, deposit transactions can be made at the counter without charge, These transactions will not be counted in determining the total number of OTC services performed.
Source: www.bankinginfo.com.my.

Illustration 1
Significant Growth of Microfinance in Malaysia[12]



Source: Bank Negara Malaysia, AIM, TEKUN.

12. Government Schemes consists of the Micro Economy Stimulus Package (Micro ESP-i), Special Loan Scheme for Chinese New Villages (Skim Pinjaman Khas Penduduk Kampung Baru Cina), and Micro Credit Scheme for Hawkers and Petty Traders.

2.5 Developing a Comprehensive Supporting Financial Infrastructure

A common barrier to financing access is the lack of reliable credit history on borrowers. Recognising this, BNM has led several important initiatives to promote the development of a comprehensive credit bureau ecosystem. In 2001, the Central Credit Reference Information System (CCRIS) was established to collect credit information from all regulated financial institutions. In addition to supporting BNM's assessment of credit risk in the financial system, the database provides important information on a borrower's credit history to FIs to enable them to perform better credit assessments. At the same time, consumers as the borrowers can build a positive credit history which leads to better access of financing at reasonable costs. As at end-2013, CCRIS captured credit information on about 8.29 million borrowers, including information from major non-bank credit providers.

The Credit Bureau Malaysia (CBM) was established in 2008 to assist SMEs to build credible and comprehensive credit records. CBM credit records include transactions from outside the regulated financial system such as transactions with suppliers, landlords and utility companies. This more comprehensive credit record improves access to finance for businesses that are utilising the formal financial system for the first time. CBM also has incorporated a credit scoring methodology which facilitates financial institutions to assess the credit worthiness of potential customers. Further, CBM plays an important role in educating entrepreneurs on how credit scores are calculated and how they can improve their credit score and provides online credit reports to its clients to facilitate the latter in assessing financing applications. As at end-2013, CBM has 28,435 SME members and had produced 1.4 million credit reports since inception.

2.6 Consumer Education and Protection

A holistic consumer education and protection framework represents an important component of BNM's strategies to promote financial inclusion. Such a framework aims to ensure fair dealings by FIs, informed participation by consumers and sustained public trust in the financial system. These conditions are necessary to ensure that all segments of society are able to use financial products and services responsibly to improve their livelihoods.

In Malaysia, due attention is given on promoting effective disclosures by FIs. FIs in Malaysia are required to comply with general and specific disclosure requirements that aim to ensure that information disseminated to consumers is timely, easy to understand, accurate, and comparable. This will reduce the information asymmetry between financial institutions and consumers. Significant focus is also given to ensuring responsible conduct by financial intermediaries in the provision of financial advice and in carrying out suitability assessments when offering products to consumers.

The Consumer and Market Conduct Department was established at BNM in 2006 to formulate and implement policies that promote fair and responsible treatment of consumers and to supervise and enforce compliance with such policies. These policies cover, among other things, obligations of financial intermediaries to observe fair practices in complaints handling, debt collection, responsible financing, imposition of fees and charges, and provision of credit cards.

In ensuring that consumers have access to advisory and resolution facilities, BNMLINK was established as a centralised point of contact for members of the public and businesses including small- and medium-enterprises (SMEs) to address their inquiries and complaints in relation to the financial sector. The public can interact directly with the FIs or BNM to obtain information and financial advisory services, or resolve any complaints against FIs. TELELINK allows the public to access these services by telephone while MobileLINK extends BNMLINK's advisory services nationwide using a custom made coach equipped with the supporting facilities and technologies.

For dispute resolutions, the Financial Mediation Bureau was established in 2005 to ensure that consumers of all FIs have recourse to an independent, fair and impartial dispute resolution mechanism. Meanwhile, the Credit Counseling and Debt Management Agency (Agensi Kaunseling dan Pengurusan Kredit, AKPK) was established in 2006 to provide counseling on financial matters and assist over-indebted individuals to work out loan repayments with FIs.

At the same time, consumers are empowered with the knowledge and skills to make good financial decisions through financial education (FE) programmes developed by BNM in collboration with AKPK and the industry. This includes the POWER! Programme which was introduced in 2011 and conducted by AKPK, targeted specifically at young individuals and new borrowers with the aim of empowering them to effectively manage their finances. The FE programme helps to enhance the financial literacy of consumers on various financial products and understand the risks and obligations involved in using them. Information web portals have been developed to provide up to date information and knowledge on a wide range of banking and insurance products and services.

Malaysia also established the Malaysia Deposit Insurance Corporation (Perbadanan Insurans Deposit Malaysia, PIDM) in 2005 as a key component of the financial safety net with the mandate of insuring deposits and benefit payments under insurance and takaful (shariah-compliant insurance) policies against the failure of banks or insurance and takaful providers. PIDM protects deposits up to RM250,000 (US$78,125) per depositor per bank and up to RM500,000 (US$156,250) per policyholder in insurance and takaful benefits. The protection is provided automatically at no charge to the consumers.

2.7 Driving a Strategic Focus on SME Development

The development of a strong and dynamic SME sector is a high priority on the national development agenda as SMEs account for 97% of the total business establishments in Malaysia. This sector accounts for 59% of total employment and contributes about 32% to gross domestic product and 17% of total exports of the nation. While private initiatives drive the economy, the Government has a critical role in providing an enabling environment for private enterprises to thrive.

The National SME Development Council (NSDC) was established to formulate broad national policies and strategies aimed at creating an enabling environment for the comprehensive development of SMEs across all sectors. BNM served as the Secretariat to the NSDC until 2008. The NSDC, chaired by the Prime Minister, is the highest policymaking body for SME development in Malaysia and brings together of more than 15 ministries and 60 agencies under a coordinated national strategy. To implement the policies of the NSDC, the SME Corporation Malaysia (SME Corp) was established in October 2009 as a dedicated agency to ensure the effective implementation of SME development programmes to bring SMEs to the next level, broadly focusing on three strategic areas: strengthening the enabling infrastructure, enhancing the capacity and capability of SMEs and enhancing access to financing. For the year 2013 alone, a total of 161 programmes amounting to RM12.0 billion (US$3.8 billion) were implemented to develop high performance and resilient SMEs.

Moving forward, the SME Masterplan 2012-2020[13] which was endorsed by the NSDC will create a conducive ecosystem to accelerate the growth of SMEs

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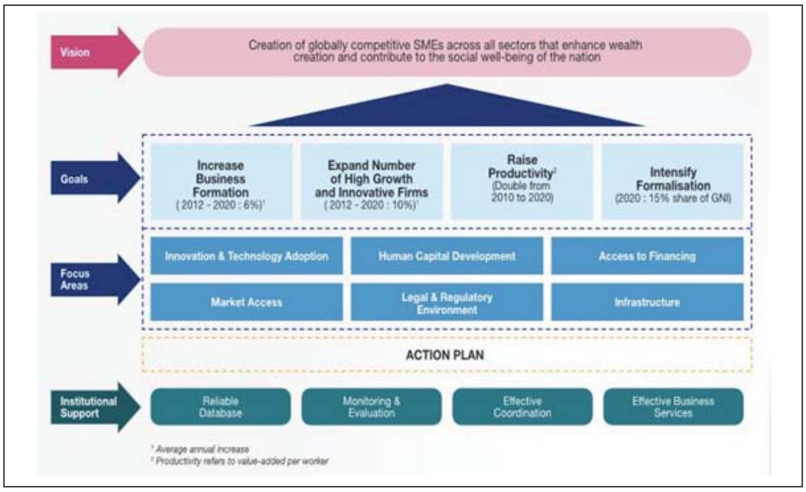
13. SME Corp, SME Masterplan 2012-2020; Available at: <http://www.smecorp.gov.my/vn2/node/190>.

towards achieving a high income economy. The SME Masterplan is an inclusive plan for all SMEs, across sectors, regions and strategic areas which translates bold measures into strategies across 6 focus areas, namely:

(i) Innovation and Technology;
(ii) Market Access;
(iii) Access to Financing;
(iv) Legal and Regulatory Environment;
(v) Human Capital; and
(vi) Infrastructure.

Illustration 2
SME Masterplan 2012-2020

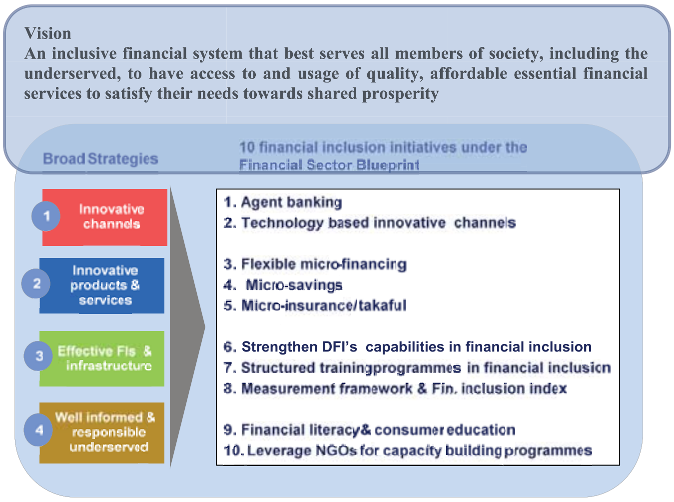


Source: SME Corporation Malaysia.

3. Current and Future Priorities in Elevating Financial Inclusion

The financial inclusion agenda continues to be advanced with the introduction of a holistic Financial Inclusion Framework under the Financial Sector Blueprint (FSB). The Framework includes 10 initiatives in relation to four broad strategies focusing on innovative delivery channels, enhancing financial products and services, increasing the efficiency of the FIs and enabling infrastructure, and empowering consumers through financial education. As at end of September 2014, five of the financial inclusion initiatives have been implemented. The key achievements of these strategies are illustrated in this section.

Illustration 3
FSB's Holistic Framework to Further Financial Inclusion



3.1 Enhancing Access Through Innovative Channels

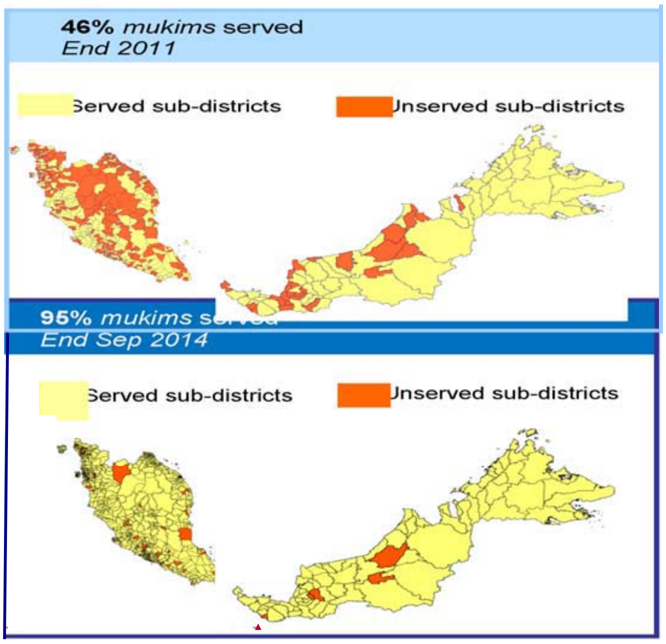
A diverse set of delivery channels have been deployed to ensure widespread access to financial services. The branching policy has encouraged FIs to establish an extensive branch network across the Malaysia to ensure sufficient access to financial services. As at end-2013, there were 1.5 bank branches per 10,000 adults and 5.4 automated teller machines (ATMs) per 10,000 adults in Malaysia. Banks are also encouraged to establish mini branches and mobile units in rural districts.

In facilitating the expansion of financial access points, the Agent Banking Guidelines was introduced in 2012, superseding the Shared Banking Services circular issued in 2007[14]. BNM is encouraging the expansion of agent banking by enabling non-financial businesses such as sundry shops, post offices and petrol

14. The Shared Banking Services Circular was introduced in 2007. The circular allows up to two domestic commercial banks to utilise the branches of DFIs and Pos Malaysia to deliver the commercial banks' products.

stations to provide basic financial services in a safe and cost-effective manner. This initiative has enabled all 144 districts in Malaysia and 95% of the 837 sub-districts with more than 2,000 populations to have access to essential financial services. As at end-2013, there were 5,474 banking agents nationwide with accumulated transactions valued at RM1.6 billion (US$487.8 million).

Illustration 4
Percentage of Sub-districts (Mukims) which are Financially-served



Source: Bank Negara Malaysia.

FIs are also encouraged to leverage on innovative digital channels such as internet banking to increase access of banking services to more people while keeping costs low. BNM has issued several guidelines to facilitate the development of electronic banking and e-payment system. As at end-2013, there are 15.6 million internet banking subscribers representing 52.2% of the total adult population[15].

15. Bank Negara Malaysia, Malaysia's Payment Statistics, Available at: <www.bnm.gov.my/index.php?ch=ps&pg=ps_stats&eId=box1>.

3.2 Introducing Innovative Financial Products and Services

In order to meet the diverse financial needs, particularly of the underserved community, BNM had facilitated the development of a broader range of micro financial products. This initiative includes the development of flexible micro financing that meets the needs of the micro enterprises that have irregular or seasonal income streams; long-term contractual micro-savings with low committed periodical savings and favourable terms to inculcate a healthy savings habit; and microinsurance/microtakaful to provide financial protection against unexpected adverse events. Currently, all three products are at the pilot stage to test the demand and acceptance by the targeted consumers.

3.3 Developing Human Capital

In developing quality human capital to support financial inclusion, BNM has partnered with the Irving Fisher Committee (IFC) on Central Bank Statistics, AFI and OECD to organise various capacity building programmes for policymakers globally on financial inclusion. Meanwhile, the Asian Institute of Chartered Banker's programme provides leadership and technical training to micro finance practitioners in the region.

3.4 Enhancing the Measurement of Financial Inclusion

Recognising the importance of measurement in translating policies into real impact, BNM adopted the Sasana Accord during the Alliance for Financial Inclusion (AFI) Global Policy Forum 2013 in Kuala Lumpur, by developing a set of key performance indicators and a financial inclusion index (FII) framework to track the progress and estimate the impact of policies to intensify the outreach of the financial sector. This has enabled BNM to prioritise areas of focus for its policy and development initiatives (discussed further in the next section).

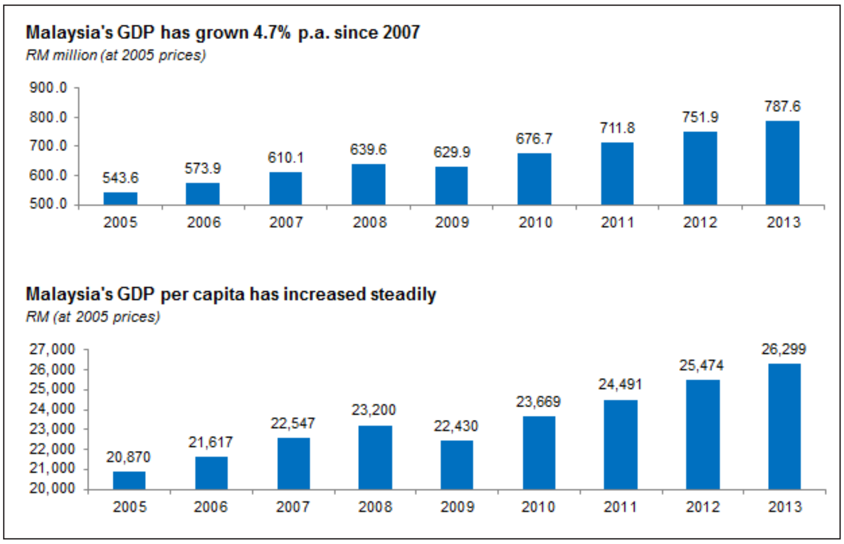
3.5 Ensuring Proportionate Regulation

Proportionate regulations advocate a risk-based approach to regulations that balance the objectives of financial inclusion, integrity and stability. In the context of financial inclusion, BNM aims to ensure that regulations such as those on anti-money laundering and prudential requirements serve to adequately protect the financial ecosystem without hindering the implementation of financially-inclusive policies. Thus, BNM fully supports the creation of the Global Standards Proportionality Working Group (GSPWG) under AFI which is working to develop a Guideline Note for regulators to effectively implement risk-based frameworks that contributes to balancing of integrity and inclusion[16].

4. Assessing the Impact of an Inclusive Financial System on the Economy

Malaysia is an upper-middle income economy oriented towards the exports of goods and services, especially electrical and electronic goods. Between 2010 and 2013, Malaysia's GDP[17] grew at a compounded annual growth rate of 5.2% from RM676.65 billion (US$219.44 billion[18]) in 2010 to RM787.61 billion (US$240.02 billion[19]) in 2013. Unemployment figures have remained steady for the past years, ranging from 3.0% to 3.2% between 2010 and 2013.

Illustration 5
Significant Growth in Malaysia's GDP



Source: Department of Statistics Malaysia.

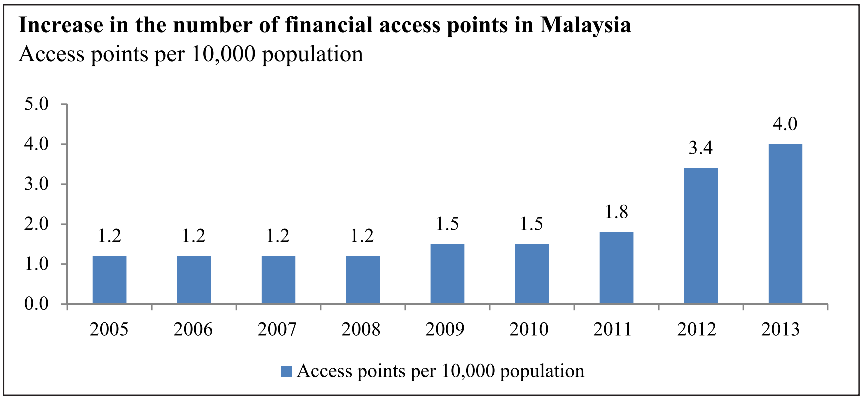
16. Alliance for Financial Inclusion, "Balancing Inclusion, Integrity and Stability," Available at: <http://www.afi-global.org/policy-areas/balancing-inclusion-integrity-and-stability>.

17. At constant 2005 prices.

18. Based on US$1 = RM3.0835, on 31 Dec. 2010.

19. Based on US$1 = RM3.2815, on 31 Dec. 2013.

Illustration 6
Growth in Financial Access Points has Risen Correspondingly[20]



Source: Department of Statistics Malaysia.

Aside from economic development, Malaysia has actively sought to improve the living conditions of its population, especially those from the low-income groups. Combining progressive social policies with the industrialisation of the economy and the development of the financial sector, the incidence of poverty has fallen from 49.3% in 1970 to 1.7% in 2012 while income equality has improved from a Gini coefficient of 0.513 in 1970 to 0.431 in 2012. Malaysia scored 0.773 in the Human Development Index, as published in the United Nations Development Programme's 2014 Human Development Report, which classifies Malaysia as a High Human Development country.

Despite these achievements, Malaysia recognises that there are still areas where further improvements can be made. Furthermore, the level of satisfaction in using the available financial products and services is difficult to determine since high take-up does not necessarily equate to high satisfaction.

An important first step in addressing these perceived issues is to identify and consequently measure the impact of financial inclusion initiatives. In this regard, BNM has established a comprehensive monitoring and evaluating approach as outlined in the FSB, mainly relying on financial inclusion indicators, supported by a few key economic indicators.

20. Inclusive of bank branches and banking agents. Data prior to 2009 exclude DFIs. The agent banking initiative was initiated in 2011.

Box Article
Financial Inclusion Index

In 2012, BNM introduced a financial inclusion index to measure the level of inclusive finance in the country. The index incorporates four equally-weighted dimensions into the determination of an index score, measuring convenient accessibility, take-up rate, responsible usage and satisfaction. Data for the index is collected both from the supply side and the demand side database. This data is included into the financial inclusion index formula that will compute a score ranging from 0 (indicating a lack of any financial services) to 1 (indicating full financial inclusiveness) which is then used to rate the level of a country's financial inclusion.

The following table illustrates the distribution of weight for each indicators and each dimensions measured by the financial inclusion index:

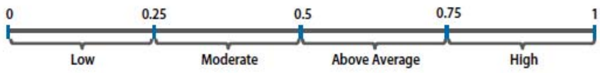
Table 2
Distribution of Weightage of the Financial Inclusion Index Indicators and Dimensions

Indicators		Dimension indices		Index
Indicators	**Weightage**	**Dimensions**	**Weightage**	
% of *mukim* with >2,000 people with at least one access point	0.5	Convenient accessibility	0.25	Index of Financial Inclusion
% of population in *mukim* with at least one access point	0.5			
% of adults with deposit accounts	0.5	Take-up rate	0.25	
% of adults with financing accounts	0.25			
% of adults with life insurance / takaful policies	0.25			
% of customers with active deposits	0.5	Responsible usage	0.25	
% of customers with performing financing accounts	0.5			
% of customers satisfied with overall financial services	1.0	Satisfaction	0.25	

A brief elaboration of the dimensions and the rationale for choosing them are provided in Appendix II.
Inputting data from the Financial Inclusion Demand Side Survey into the abovementioned formula results in the following FII score of 0.77, based on data from 2011.

Table 3
Malaysia's Financial Inclusion Index Score among the General Population

Dimension	Indicators	Data (%)	Target (%)	Index of Each Indicator	Weight	Index of Each Dimension	Equal Weighted Dimension	Equally Distributed FII
Convenient Accessibility	% of *mukim* with at least 2,000 population with at least one access point	46	90	0.51	0.5	0.64	0.25	0.77
	% of population living in *mukim* with at least one access point	82	95	0.86	0.5			
Take-Up Rate	% of adult population with deposit accounts	92	95	0.97	0.5	0.70	0.25	
	% of adult population with financing accounts	36	50	0.72	0.25			
	% of adult population with life insurance / takaful policies	18	40	0.45	0.25			
Responsible Usage	% of customers with active deposits	87	90	0.97	0.5	0.98	0.25	
	% of customers with performing financing accounts	97	97	1.00	0.5			
Satisfaction Level	% of customers who are satisfied - overall financial services	61	80	0.76	1.0	0.76	0.25	
Index ranges from 0 –1, with 1 being perfect financial inclusion							1.00	0 – 1.00



At 0.77, Malaysia can be considered to have high financial inclusiveness mainly supported by the high number of active deposit accounts and performing financing accounts, as well as the significant number of individuals that live within *mukims* that have access to financial services.

4.1 Major Findings and Policy Implications

Using the financial inclusion index and given comparable data, the level of financial inclusion of different economies can be measured side-by-side. The FII can be utilised to analyse financial inclusion for the different income-levels within a single country. This assists policy-makers in the formulation of appropriate recommendations by highlighting the differences in accessibility, take-up, usage and satisfaction between the general population and any income group, especially the low-income households.

In the case of Malaysia, the results supported the hypothesis that low income households experience lower financial inclusiveness, scoring 0.68 in contrast to the general population index score of 0.77.

Table 4
Malaysia's Financial Inclusion Index Score among the Low-Income Households

Dimension	Indicators	Data (%)	Target (%)	Index of Each Indicator	Weight	Index of Each Dimension	Equal Weighted Dimension	Equally Distributed FII
Convenient Accessibility	% of *mukim* with at least 2,000 population with at least one access point	46	90	0.51	0.5	0.64	0.25	0.68
	% of population living in *mukim* with at least one access point	82	95	0.86	0.5			
Take-Up Rate	% of adult population with deposit accounts	89	95	0.94	0.5	0.32	0.25	
	% of adult population with financing accounts	10	50	0.20	0.25			
	% of adult population with life insurance / takaful policies	8	40	0.20	0.25			
Responsible Usage	% of customers with active deposits	87	90	0.97	0.5	0.98	0.25	
	% of customers with performing financing accounts	97	97	1.00	0.5			
Satisfaction Level	% of customers who are satisfied - overall financial services	60	80	0.75	1.0	0.75	0.25	
Index ranges from 0 –1, with 1 being perfect financial inclusion							1.00	0 – 1.00

Comparing the results between the general population and the low-income households, it is noted that the latter recorded a lower FII score driven by a lower index score in the take-up rate dimension. In particular, low-income households indicate lower take-up rates for financing, and life insurance and takaful policies. Nevertheless, even among the low-income households, the take-up of deposit accounts is high.

Similar scores for convenient accessibility is expected as accessibility is a geographical measure and given the limited exposure of the lower-income households to financial products other than deposit accounts, the high rating for 'responsible usage' is reasonable. In terms of satisfaction, 60% of respondents from low-income households expressed satisfaction with overall financial services, a similar percentage for the general population (61%).

As at end-2013, Malaysia's FII score is at 0.88 based on available data. Comprehensive updates of the FII scores are limited by the frequency of the financial inclusion demand-side surveys are conducted[21].

21. The last financial inclusion demand-side survey conducted in 2012.

From the empirical analysis, strategies to further enhance financial inclusion in Malaysia will aim to increase the following dimensions of financial inclusion:

- Percentage of *mukims* with populations of 2,000 or more with at least one access point
- Percentage of the adult population with deposit accounts
- Percentage of the adult population with financing accounts
- Percentage of the adult population with life insurance or takaful policies
- Percentage of customers who are satisfied with overall financial services

Of these identified areas for improvement, the most impact to financial inclusion can be accomplished by improving the number of access points. A key area for improvement is enhancing access to more mukims with populations of 2,000 and above. as well as extending financial access points to more than 1 access point per mukim especially for those with large populations.

In regard to the issue of take-up, responsible usage and satisfaction, BNM is cognisant that these can be addressed through the continuation of the financial awareness and financial literacy programmes. These programmes serve to raise awareness of customers to available financial products, making oneself bankable and the proper utilisation of these financial services. Combined with convenient accessibility, it is envisaged that meaningful financial inclusion can be attained.

A key channel for the delivery of these financial services is agent banking. It is envisaged that agent banking will be instrumental in extending the availability of financial access points to locations that are considered economically unviable for a formal bank branch to be set up.

5. Conclusion

Although the financial inclusion initiatives in Malaysia have resulted in significant achievements in terms of outreach and the prevalent usage of deposit accounts, there are areas of access to financial services which require continued improvements including extending further the availability of financial access points and increasing the take-up of insurance/takaful products services. As access is increased and more financial products are taken up, financial institutions must ensure that the quality of service is upheld so that satisfaction is maintained and does not negatively affect the acceptance of formal financial services.

The empirical evidence also highlights the need to factor in different considerations in efforts to enhance financial inclusion for low-income households. Beyond overcoming the challenges of providing access to financial services, authorities must invest in initiatives that bring up the level of financial awareness and financial literacy. Promoting financial education for all ages and income will require close coordination between relevant ministries and other stakeholders.

Last but not least, BNM recognises the importance of learning from international experiences in financial inclusion as well as benchmarking with global best practises. Malaysia will continue to collaborate closely with financial inclusion experts and international policymakers from the Alliance for Financial Inclusion (AFI) as well as other organisations such as the United Nations Capital Development Fund (UNCDF) and the World Bank in furthering financial inclusiveness in the country.

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Appendix 1

Selected Key Indicators of Financial Inclusion in Malaysia (as at end-2013)

Accounts	
No. of loan accounts (individuals)	19,058,559
No. of loan accounts (SMEs)	676,144
No. of deposit accounts	72,173,792
Access Points	
No. of bank branches	3,226
No. of ATMs	11,904
No. of cash-in & out agents (POS and BSN's agents)	5,474
No. cash deposit machine	5,177
Other cash-in & out access points - BSN's mobile units	10
Total no. of cash-in & out access points per 10,000 adults	4.0
Mukims (sub-district) served with financial access points (%)	92.5% (out of 837)
DUN served with financial access points (%)	99.8% (out of 576)
Note: All 144 districts have access points by June 2011	
Access to Loans	
% of adult with active loan accounts *	37%
No. of loan accounts per 10,000 adults	8,673
No. of loan accounts (SMEs) per SME population	1.0
% of oustanding SME loans to total business loans of FIs	42.1
% SME financing to GDP	21.6%
Access to Deposits	
% of adults population with deposit accounts [1]	92%
% of adults with active deposit accounts *	92%
No. of deposit accounts per 10,000 adults	32,846
Proportion of Basic Savings accounts [2]	18.4%
Proportion of Basic Current accounts [3]	10.9%
Branch and ATM Penetration	
No. of bank branches per 10,000 adults	1.5
No. of ATMs per 10,000 adults	5.4
No. of CDMs per 10,000 adults	2.4
Insurance Penetration	
% of adults with life insurance policy *	33%
No. of conventional policies in force [4]	11,716,875
No. of takaful policies in force [4]	4,171,045
No. of conventional & takaful policies in force per 10,000 adults	7,231
Conventional & takaful premiums to GDP (%) [5]	3.2

Denominator Items

Total Malaysian adult population [6]	21,973,341
Total no. of SMEs in Malaysia (SME population) - Census 2011	645,136
GDP at current price (RM million) [7]	984,453

* Source: JPS, National ID Survey (IC Project), 2013.

[1] Financial Inclusion Demand-Side Survey 2011.

[2] Data for basic savings accounts refer to savings accounts that are opened by individuals (Source: JPS).

[3] Data for basic checking accounts refer to accounts that are opened by individuals and SMEs (Source: JPS).

[4] Source: JPS.

[5] Source: Insurance data-JPS, GDP-DOSM.

[6] Projection of total adult population for 2013 based on Population and Housing Census of Malaysia 2010 (Source: DOSM, 2011).

[7] Source: DOSM.

Appendix 2

Rationale for the Choice of the Four Financial Inclusion Indicator (FII) Dimensions

i. *Convenient accessibility*

Convenient access to financial access points is the cornerstone of any financial inclusion programme and should be the starting point of any measure of financial inclusiveness. As such, the FII deems that a given geographical administrative unit has access to financial services if there is at least one financial access point within it.

The geographical administrative unit that was utilised for Malaysia's financial inclusion index is the *mukim* (sub-district) with populations exceeding 2,000 people. The rationale behind choosing the *mukim* is that it allows for the survey results to be collected and compiled based on established administrative groupings, while at the same time filtering out geographical units with smaller populations. 837 *mukims* in Malaysia were included for having populations of more than 2,000.

Convenient accessibility is measured by the percentage of *mukims* with populations exceeding 2,000 that has at least one financial access point and the percentage of the total population that live in these *mukims*.

ii. *Take-up rate of financial products*

The second dimension measures banking penetration through the size of the banked population. While the first dimension measure gauges the accessibility of populations to a financial access point, the second dimension looks at the number of adults that utilises these access points to avail to financial services.

The take-up rate is measured through the percentage of respondents who stated that they have any deposit accounts, financing accounts, or life insurance or takaful policies.

iii. *Responsible usage*

The third dimension on responsible usage further refines respondents to measure those who do not only have access to financial services and utilise them, but who also use these financial services actively and responsibly. This is based on the concept of the underbanked and the marginally-banked, referring to people with bank accounts that they do not or hardly ever use[22]. By including this dimension into the FII, the FII is adjusted for the overstatement of effective financial inclusion from the non-utilisation of services by these marginally-banked persons.

Responsible usage is measured by the percentage of respondents that indicated that they actively use and service their deposit and financing accounts.

iv. *Satisfaction level*

The final dimension measures the satisfaction level of the respondents to the overall financial services received. Although satisfaction is less easy to quantify and doesn't directly contribute to the availability or utilisation of financial services, we believe that it is an indispensable component to any financial inclusion index. Measuring satisfaction serves to countervail against the implementation of superficial improvements in outreach which sacrifice quality of service to achieve quantitative objectives.

In the FII, satisfaction is measured by the percentage of survey respondents who answered that they felt 'satisfied' or better with the overall financial services.

22. Chattopadhyay, S.K., (2011), "Financial Inclusion in India: A Case-Study of West Bengal," *RBI Working Paper,* WPS (DEPR) 8 / 2011.