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About OMFIF

Dialogue on world finance and economic policy

THE Official Monetary and Financial Institutions Forum is an independent think tank for central banking, economic policy and public investment – a non-lobbying network for best practice in worldwide public-private sector exchanges. At its heart are Global Public Investors – central banks, sovereign funds and public pension funds – with investable assets of $36tn, equivalent to 45% of world GDP.

With offices in London and Singapore, OMFIF focuses on global policy and investment themes – particularly in asset management, capital markets and financial supervision/regulation – relating to central banks, sovereign funds, pension funds, regulators and treasuries. OMFIF promotes higher standards, performance-enhancing public-private sector exchanges and a better understanding of the world economy, in an atmosphere of mutual trust.

Membership

Membership offers insight through two complementary channels – Analysis and Meetings – where members play a prominent role in shaping the agenda. For more information about OMFIF membership, advertising or subscriptions contact membership@omfif.org

Analysis

OMFIF Analysis includes commentaries, charts, reports, summaries of meetings and The Bulletin. Contributors include in-house experts, advisers network members and representatives of member institutions and academic and official bodies. To submit an article for consideration contact the editorial team at analysis@omfif.org

Meetings

OMFIF Meetings take place within central banks and other official institutions and are held under OMFIF Rules. A full list of past and forthcoming meetings is available on www.omfif.org/meetings. For more information contact meetings@omfif.org

OMFIF Advisers Network

The 173-strong OMFIF advisers network, chaired by Meghnad Desai, is made up of experts from around the world representing a range of sectors: monetary policy; political economy; capital markets; and industry and investment. They support the work of OMFIF in a variety of ways, including contributions to the monthly Bulletin, regular Commentaries, seminars and other OMFIF activities. Membership changes annually owing to rotation.
Back to square one

Deepening financial disparity between rich and poor risks causing massive damage to the world economy and upending incumbent political structures. Already over the last several years we have seen the dangers of inequality reflected in the rise of populist parties in major economies. Law-makers are drifting further away from the political centre, as they try to appeal to citizens dissatisfied with the status quo.

These challenging socioeconomic themes, of critical importance to politicians and monetary policy-makers alike, are addressed in this edition of The Bulletin by a troika of OMFIF economists, as well as representatives of multilateral institutions and central banks. As Kristalina Georgieva, chief executive of the World Bank, told OMFIF’s Julie Levy-Abegnoli, the progress made in recent decades to combat inequality and poverty ‘could be jeopardised as global headwinds intensify and the economic environment becomes more challenging’.

Pierre Ortlieb writes on how central banks must break the cycles of inequality that exclude parts of society from participating in the economy, as well as how some unorthodox monetary policy measures may have impaired financial inclusion. As Rodrigo Pereira Porto of the Banco Central do Brasil describes, policy-makers can promote socially responsible investment and banking practices in efforts to curtail such inequality and overcome the troubles that arise from unjust concentrations of wealth.

Of particular significance is the systemic exclusion of women from the financial system, as Kat Usita writes and as was illustrated by OMFIF’s latest Gender Balance Index. The index, now in its sixth edition, was launched on 7 March at the Swiss embassy in London and will be featured in Washington at the spring meetings of the International Monetary Fund and World Bank.

Advances in financial technology hold a great deal of promise, but they are not a panacea for economic exclusion. Greg Medcraft of the Organisation for Economic Co-operation and Development and Bhavin Patel write about how, in spite of fintech’s much-vaunted ambitions, such advances mean little if users are unable to engage easily with the technology.

The massive expansion of these services may, too, be inadvertently creating a new corpus of financially excluded people; if law- and policy-makers are unable to improve their society’s digital literacy (to say nothing of traditional literacy levels), large segments of the population risk being excluded from these digital services.

Policy-makers must be prepared to face up fully to these new risks. Unless they alleviate the factors that have long contributed to inequality around the world, economies and societies everywhere will be poorer.
Review: January

»25 January, Davos
Markets in Africa

AT THE Europe launch of the Absa Africa Financial Markets Index, Lesetja Kganyago, governor of the South African Reserve Bank, presented the initiatives required to boost the accessibility of the report’s 20 African financial markets.

»25 January, Singapore
Trade, China and Brexit

IN THE LIGHT of intensifying geopolitical risks across Europe, and trade disputes between the US and China, OMFIF and Camri convened a group of experts to assess these developments and discuss the economic outlook for 2019.

»23 January, London
Success and vulnerability

EIGHT months after finishing his term as vice-president of the European Central Bank, Vítor Constâncio remains a firm believer in the euro’s success. But speaking at an OMFIF City Lecture, he recognised that the next downturn could be just around the corner, and that member states may not have done enough to prepare appropriate responses.

»31 January, London
Outlook for reserve asset management

THE INCREASINGLY sombre tonality of the world economy overshadowed the asset management and risk deliberations of central banks, sovereign funds and private participants at an OMFIF seminar. The discussions on macroeconomic prospects were coloured by increasing fears that the previously brighter global outlook was turning worryingly gloomy at unexpected speed. Speakers included Ewald Nowotny, governor of the Oesterreichische Nationalbank, and Turalay Kenç, former deputy governor of the Central Bank of the Republic of Turkey.
Sustainable finance in the digital era

OMFIF convened a roundtable with Peter Estlin, lord mayor of the City of London. Discussions centred around how digitalisation is transforming green finance and the role of the City of London in promoting green bonds.

Central banks and supervisory technology

THE USE of technology in financial supervision is a growing concern for central banks and regulatory agencies. In the light of this, OMFIF convened central bankers, supervisors, private sector market participants and financial regulatory experts to discuss how the use of new technology in regulation and supervision could enhance financial stability. Topics ranged from the multiple uses of regtech and countering the risks of data security, to adapting bank business models and strategic planning processes for the implementation of new technology.

Currencies in emerging markets

OMFIF convened a meeting with Steve Hanke, professor of applied economics at the Johns Hopkins University. He discussed the effects of US monetary policy on emerging markets and the role of global currencies.

The long road to Brexit

THE UNCERTAINTY lingering over the UK’s withdrawal from the European Union was discussed in a roundtable led by Lord (Norman) Lamont, chancellor of the exchequer (1990-93), and Lord (Christopher) Tugendhat, vice-president of the European Commission (1981-85). They put forward the options facing the UK – as well as the rest of Europe – as the timetable progressed towards the originally scheduled Brexit date of 29 March.
Prioritising diversity in finance

GENDER diversity in public investment institutions has improved, but the overall picture remains heavily unbalanced, much more so than the equivalent in politics or in private sector finance. This was the message at the launch of the 2019 Gender Balance Index, now in its sixth year. The launch included a keynote presentation and panel discussion focusing on the findings of the research, with speakers that included Monika Bütler, member of the bank council at the Swiss National Bank, and Martin Taylor, member of the financial policy committee at the Bank of England.

Normalisation a ‘marathon, not a sprint’

PHILADELPHIA Fed President Patrick Harker, speaking at an OMFIF City Lecture, said that monetary policy normalisation ‘is a marathon, not a sprint. Even if economic and financial conditions evolve as anticipated, the composition of the balance sheet will not see any drastic change in the near future.’

Future of global integration

THE WORLD Trade Organisation and OMFIF organised a seminar on global trade tensions, to discuss topical subjects including trade in services, trade finance and geopolitical challenges to the world trade agenda.

China, US in the global economy

OMFIF and the China Construction Bank convened a global audience of private and public sector participants from China, the US and elsewhere to discuss economic and political developments in US-China relations and these countries’ roles in the global economy.

ECB monetary measures

THE FUTURE of the European Central Bank’s monetary policy following extra liquidity measures and a pause in tightening announced last week was discussed at an OMFIF roundtable with New York investors and Natacha Valla, the ECB’s deputy director for monetary policy.

Champion of financial inclusion

NESTOR Espenilla, governor of the Bangko Sentral ng Pilipinas, who died on 23 February aged 60, was a central banking veteran and champion of financial inclusion. An engaging participant in various OMFIF meetings, taking part in the first Asia meeting in Malaysia in 2010, Espenilla was also a regular contributor to OMFIF analysis and flagship publications, including last month’s 100th edition of The Bulletin.
Agenda

Monday 15 April, London
Navigating a new era of infrastructure development
A seminar on the regulation and governance of China-led Belt and Road projects. Bringing together policy-makers and private sector investors, the meeting will focus on how to implement environmental, social and governance initiatives in the project.

Thursday 1 May, London
The future UK-EU relationship and reforming the euro area
A City Lecture with Luis de Guindos, vice-president of the European Central Bank, who will discuss reforming the euro area and the future relationship between the UK and EU.

Friday 3 May, Fiji
Emerging digital technologies for financial inclusion: Role of central banks
A workshop on digital currencies and their impact on central bank and retail payments channels. Attendees will discuss distributed ledger technology, digital currencies’ benefits and risks, implications for financial markets and private market participation.

Tuesday 21 May, London
Responding to economic downturns and avoiding market shocks
A roundtable with Martin Flodén, deputy governor of the Swedish Riksbank, on how central banks could react in the face of a potential economic downturn and the policies necessary to avoid market shocks resulting from normalisation.

Tuesday 28 May – Wednesday 29 May, Prague
Prospects for euro integration in central and eastern Europe
A seminar with the Czech National Bank to discuss the outlook for growth in central and eastern Europe and the prospects of integration into the euro area. The aim of the meeting is to examine the benefits and challenges of joining the euro and the banking reforms required in the adoption process.

Monday 3 June, Vienna
Long-run economic growth and development in CESEE
A seminar with the Oesterreichische Nationalbank to discuss the goals, priorities and implementation strategies to ensure sustainable economic growth and development in central, eastern and southeastern Europe.

Wednesday 12 June, Singapore
Global Public Investor 2019 launch
A seminar for the launch of Global Public Investor 2019, the publication devoted to public sector asset ownership and management around the world. The meeting focuses on the key issue of sustainability and aims to share best practice among investors.

Tuesday 9 July - Wednesday 10 July, St. Louis
Assessing priorities and implications for society, politics and economics
A seminar with the Federal Reserve Bank of St. Louis and the OMFIF Foundation to look ahead to the next 10 years in finance, covering themes such as the future of central banking, economic inequality, sustainable investment, global governance and the role of technology in employment and education.

For details visit omfif.org/meetings
Central banks inadvertently hinder inclusion
New thinking would make monetary policy more effective

In a town-hall style meeting in Lisbon in June 2017, European Central Bank President Mario Draghi confronted economic inequality in uncharacteristically vociferous terms. ‘We have to fight against inequality,’ he noted, adding that deepening economic disparities have highly destabilising macroeconomic effects. Governments should use all tools available to them to achieve more equitable wealth distribution, said Draghi. Yet the urgency of his statements belies the role of central banks in exacerbating inequality, and the part they could play in alleviating it. Inequality obstructs financial inclusion, damps growth and breeds instability. There is an urgent need to rethink monetary policy.

Central bankers speaking out against economic inequality would once have been well-nigh inconceivable. In 1999, Federal Reserve Chairman Alan Greenspan acknowledged that there were ‘very major holdings of wealth by individuals’ in the US. He denied, however, that these came at the expense or at any significant cost to others. Academic and institutional research has altered this line of thinking. The International Monetary Fund has recognised that inequality undercuts the sustainability of growth and social cohesion. Gabriel Zucman, professor of economics at the University of California, Berkeley, has demonstrated how tax havens exacerbate distributive challenges. And economist Alberto Alesina has highlighted that high-inequality countries tend to experience more social unrest.

Cycle of inequality
Inequality hinders efforts towards financial inclusion and holds back growth through three principal, interlinked channels. First, it most clearly leads to worse outcomes – educational, financial, psychological – for those excluded from socioeconomic processes. Barring a share of people from full, meaningful participation in the economy harms growth and welfare.

Second, inequality self-perpetuates by constraining intergenerational mobility. Poor health or a lack of educational...
achievements among parents reduces their children’s access to quality education, inheritance and developmental stimuli, among other opportunities. This reduces these children’s longer-term ability to achieve financial inclusion due to factors outside their control.

Third, inequality has corrosive political effects, owing to the sociological implications of wealth. Wealthy individuals are better able to use their fortunes to wield political influence, producing regulatory capture and adversarial politics. This impedes efforts towards redistribution, and produces the kind of dysfunction that discourages investment and ultimately leads to lower growth, producing a vicious cycle.

Inequality thus produces a set of malign, self-reproducing socioeconomic outcomes. Crucially, none of these outcomes is inevitable. Intensive, inequitable concentrations of wealth are the unintended result of distinct policy choices. Monetary policy-makers in advanced economies have contributed to these outcomes through several different and often ambiguous mechanisms. At the same time, they hold the keys to reducing inequality. Deliberate, careful policy design would improve the transmission of monetary policy, and help central banks to fulfil their mandates.

As economist Branko Milanović notes in his work on long-run income distributions, inequality fluctuates over time in rich societies. This is driven primarily by three variables: technological change, openness and policy. In the early 20th century, policy choices such as President Franklin Roosevelt’s New Deal and the Bretton Woods system of capital controls contributed to a decline in inequality around the world. Since the 1970s, however, inequality has risen.

While technological innovation such as the development of information and communications technology has played a critical role in this shift, Milanović argues policy choices are equally significant. One example is global trade and investment liberalisation, which exerts downward pressure on national tax rates and disproportionately impacts western low-skill workers. In the US, the share of income going to the top 1% has risen to levels not seen since the 1930s. The wave-like nature of this relationship is visible in the curve’s recent upward motion.

The same pattern holds true for most developed economies, including the UK and the euro area. Crucially, the expansionary monetary stances that followed the 2008 financial crisis have played an important role in boosting the development of what Milanović calls the ‘Kuznets wave’ relationship between inequality and per capita GDP. As the ECB’s Benoît Coeuré noted in 2017, post-crisis quantitative easing was supposed to work through three steps: securities purchases lead to easier financial conditions, which support greater economic activity, leading to prices consistent with the ECB’s inflation target.

Yet compelling empirical evidence of success exists only for the first channel, as ECB easing programmes produced higher relative asset prices. Evidence for the two subsequent channels is mixed at best. In the euro area, the households holding the most assets are also those with the highest net wealth. While the first quintile of wealth distribution holds only €17,200 in total assets, the highest quintile holds €807,100 on average, mostly consisting of real estate and financial assets, according to the ECB’s Household Finance and Consumption Survey. The effect is twofold. The rise in asset prices benefits the latter group, while the former is harmed by the lack of real monetary policy stimulus.

There are ways monetary policy may exacerbate inequitable economic outcomes, including people’s source of income. Under expansionary monetary conditions, households reliant on capital income rather than labour income will benefit disproportionately if profits rise faster than wages. Similarly, the transmission of conventional monetary policies – such as interest rate changes – relies overwhelmingly on financial intermediaries, who may extract medium-term rents from their role in a central bank’s market infrastructure. These structural conditions reinforce the reallocation of wealth towards the rich.

The ECB argues that its post-crisis policies have led to disproportionately large employment gains among lower-income groups in the euro area. But this does not mitigate the outsized distributional impact.
that these policies have had. This applies not only for the euro area, but also for the US and other jurisdictions that have implemented large-scale asset purchase programmes.

Most central banks argue that their mandate does not allow or require them to grapple with the distributional consequences of their policies. While this claim is true on the surface, it obscures the fact that central banks would be better able to fulfil their mandates if they took the distributional consequences of their policies more seriously. Since interest rate pass-through relies in part on constituents’ marginal propensity to consume to stimulate economic activity, achieving a more equitable distribution of income would make consumers more sensitive to rate changes, making price stability somewhat easier to achieve. Greater financial inclusion and reduced inequality would thus be in the interest of monetary policy-makers, even considering their mandates in a narrow, strict manner.

There is no simple resolution to the relationship between monetary policy, inequality, growth and stability. However, it is clear that inequality aggravates financial exclusion, allowing it to persist across generations. Monetary policy has tended to exacerbate this relationship, benefiting asset owners more so than lower-income earners.

Policy design should adapt to take these developments into account. For example, increasing the share of European Investment Bank securities bought in asset purchase programmes would result in greater capital investment, producing more equitable economic outcomes in European economies. Piloting programmes which directly provide payments to citizens, entirely bypassing financial market infrastructure, may be similarly beneficial. Importantly, these changes would make conventional monetary policies more sensitive and more effective.

While monetary policy alone is not enough to remedy the problems associated with inequality, it can and should take an interest in doing so to bolster the ethics and efficacy of central banking. Pierre Ortlieb is Economist at OMFIF.

Breaking down financial inclusion

The UN sustainable development goals can provide a blueprint to help nations and institutions promote financial inclusion. The goals include:

- Gender equality
- No poverty
- Decent work and economic growth
- Reduced inequalities

Only 65% of women globally hold bank accounts, in contrast to 72% of men.

Two-thirds of unbanked adults have a mobile phone

Source: Global Findex database; Gallup World Poll 2017

Is universal basic income a viable solution to address widening economic inequality? See page 34 for our advisory board’s opinion on how viable the policy could be.
Women’s widespread financial exclusion

Solutions should go beyond poverty alleviation

Kat Usita
OMFIF

Women’s financial inclusion is often regarded as an issue of poverty. Solutions tend to focus on access to financial services that can help them overcome economic difficulty. This is an important endeavour, but the financial system excludes women on a much broader and systemic scale, even when economic conditions are relatively good.

The most basic measure of financial inclusion – ownership of a bank account – shows a gender gap. Only 65% of women globally hold bank accounts, in contrast to 72% of men, according to the World Bank’s Global Findex. The gap of seven percentage points has persisted since the survey was launched in 2011. The difference is more apparent in developing countries, where only 59% of women have a bank account, against 67% of men. In high-income countries, owning a bank account is nearly universal for both genders.

For this reason, most financial inclusion programmes targeted at women are designed and delivered in the context of poverty alleviation and economic empowerment. Financial literacy helps to improve women’s ability to manage household finances. Microfinance gains access to capital that is typically out of reach for women who do not own collateral, and provides opportunity for self-employment. Encouraging women to open their own bank accounts and access financial products can influence their ability to save and invest.

These programmes respond to the most urgent financial challenges that women face and should be refined until outcomes improve significantly, as their success reaps financial and socioeconomic benefits. Women with spending power can purchase goods and transact independently. Female entrepreneurs create jobs for their communities, especially when familial obligations force them to run their business activities close to home. Mothers who earn can reinvest in their children’s health and education.

However, this presents only one dimension of women’s financial exclusion. Even when women have bank accounts, access to credit and financial independence, they are routinely disadvantaged in a financial system that has been overwhelmingly run by men, for men. This applies even in the world’s most developed economies.

Industry gap
Glaring exclusions can be seen in industry. Many women enter the financial services sector, but few progress to the highest ranks in these businesses. The UK’s Financial Conduct Authority reports that only 14% of partners in private equity firms, hedge funds and other financial service firms are women. Globally, a study by the International Monetary Fund found that less than 2% of 800 financial institutions in 72 countries are led by female chief executives. The lack of gender diversity means these firms are missing out on female talent, and casts doubt on whether the products and services they offer are designed with an understanding of women’s financial needs.

Women’s entrepreneurial activities are constrained and left out of funding opportunities. Out of $150bn raised through venture capital in the US in 2018, only $2.9bn, or 2.2%, was channelled to female-founded start-ups. In the UK, less than 1% of venture capital investment has gone to start-ups led by women. Among British small and medium-sized enterprises, only one-fifth are led by women. These figures indicate industry bias against hiring, promoting and investing in women. They may also be a result of women avoiding entry into fields that are overwhelmingly male.

Age-related exclusion
More broadly, women’s financial power is limited by the gender pay gap across industries. In the European Union, men on average earned 16% more than women in 2017. The gap deepens as women enter retirement, with the average pensions gender gap in the EU at 37%. The disadvantage women face curbs their ability to spend, save, borrow and invest – an opportunity for growth that the financial system is failing to maximise.

Aside from having to grapple with lower pensions income, older women face the same age-related exclusion as men. The rapid pace of innovation and digitalisation in banks has left some older consumers unable or apprehensive to perform basic financial transactions.

Financial inclusion at the minimum is about removing barriers to access to financial products and services. There is a need to identify different dimensions of the financial system that exclude women, whether it is because of gender biases or structural problems. Financially empowering women in developing countries can have multiplier effects on the wider economy. Likewise, striving for meaningful financial inclusion for women elsewhere in the world, at all stages of their lives, would be a boost to growth.

Kat Usita is Deputy Head of Research at OMFIF.
Account inactivity impeding inclusion drive

Businesses must capitalise on large online networks through mobile technology

Financial inclusion can be best defined as access to and usage of affordable, appropriate and accessible financial services, including savings and investments, remittances, financing and insurance. By this definition, much remains to be done.

Access to accounts may have increased, but the usability and uptake of services on digital platforms remain low, especially in developing markets. According to the World Bank’s Global Findex report, 1.2bn adults opened a bank account between 2011-17, with more than 500m doing so after 2014. This illustrates an acceleration towards a more ‘banked’ population globally, where 69% of adults have a digital means to save, pay and invest their money.

However, there is still a large gap in financial inclusion between the rich and the poor and advanced and emerging economies. Among adults in the richest 60% of households within developed economies, 74% have an account. But among those in the poorest 40% of households, only 61% do, leaving a global gap of 13 percentage points. The difference is similar between advanced and developing economies, and neither gap has changed significantly since 2014.

A major issue is account inactivity. Of the 515m adults who became financially included between 2014-17, almost 20% of these new accounts are now dormant. This inactivity is higher in emerging markets, where 30% of all account owners have not used them for digital payment and transactions; the corresponding figure in high-income countries is 3%. This is symptomatic of the favour that banks give to simple and quick solutions as a way to meet arbitrary financial inclusion targets.

Financial inclusion is not just about enabling access to services; it must also encompass their potential and actual use of these services. Exclusion can be voluntary, where an individual or business does not use the service despite having access to it, or involuntary, where the cost to use features of the service – such as transaction fees – are too high.

Of the 515m adults who became financially included between 2014-17, almost 20% of these new accounts are now dormant.

According to the Findex survey, the most common reason for voluntary exclusion in developing markets is that people simply do not have enough money to make a deposit. Lack of savings, coupled with poor digital adoption between merchants and local vendors, means cash continues to dominate the retail payment infrastructure. In such a scenario, the full benefits of adopted technologies are not being utilised.

Market-specific solutions
The rapid spread of mobile phones can help to realise the economic benefits of digital finance. Globally, almost 90% of people have their own mobile phone, while 58% have access to the internet in addition to owning a mobile phone.

More should be done to utilise these online networks. Targeted solutions that consider individuals’ specific needs are required. Providing blanket solutions is ineffectual, and a key reason why so many accounts remain inactive.

Encouraging supply-side competition is one effective way to create market-specific solutions. Local vendors and businesses can benefit significantly from digital financial services, especially in economies where account holders are more likely to have mobile phones than debit cards.

As more and more retail outlets begin to accept digital payments, consumers benefit from positive network externalities, and the utility of joining the network increases. China, where ecommerce functions have improved in line with the growth of scalable and cost-efficient non-bank payment providers such as Tencent and Alipay, offers a good example to follow.

On the demand side, the uptake of digital banking services can be improved if issues of access quality and service affordability are overcome. The partnering of incumbent banks and financial technology companies could prove fruitful. Banks can leverage their capital, trust, customer bases and brands to expand rapidly in partnership with fintech companies, which in turn can help fill gaps in banks’ channels, innovations, product sets and processing capabilities.

Financial inclusion should not end with just opening accounts. Customers must be able to use these services on a regular basis, conduct transactions, budget expenditures and grow their credit histories. Otherwise, these accounts will devolve into deadweight.

Bhavin Patel is Senior Economist and Head of Fintech Research at OMFIF.
Financial inclusion is an evolving concept, usually associated with policies that lawmakers hope will raise low-income individuals’ ability to use financial services to protect themselves and their families against hunger, crime and natural disasters.

The poor are excluded from formal financial services for many reasons, including financial illiteracy. Few institutions can meet or focus on low-income people’s needs. A weak supervisory framework may enable financial abuse. And inadequate or risky infrastructure, particularly a lack of internet access, hampers investment.

Around the world, poor financial inclusion begets high rates of social and economic inequality. It may also be the driving force behind threats to social welfare. The 2008 financial crisis showed that the duties and responsibilities of governments, the private sector and even consumers had not been outlined clearly.

**Principles for inclusion**

Recognising the importance of this topic, in 2009 the G20 began working on an innovative global financial inclusion strategy. It emphasised the need to raise public awareness and mobilise the private sector, as well as the crucial role of standard-setting bodies.

The Global Partnership for Financial Inclusion was launched in 2010 to oversee progress on this strategy. In 2016, the GPFI introduced the G20 high-level principles for digital financial inclusion. These aim to leverage the huge potential of new technologies to offer affordable financial services. They pave the way to adapt infrastructure and legal frameworks to the new and disruptive elements of digital culture.

The principles highlight responsible practices as a key requirement for financial inclusion. These include consumer and data protection, transparency, and the disclosure of any information relevant to decision-making. This helps prevent irresponsible lending and over-indebtedness. It promotes better governance by engaging with stakeholders on risks and expectations.

Investments in large-scale financial services platforms and new data management tools are an opportunity for market players to understand and better serve clients, no matter what segment they represent in society.

**Responsible practices**

Recent international initiatives, such as the principles for responsible banking promoted by the United Nations Environment Programme Finance Initiative, encourage financial institutions to implement corporate social responsibility practices. CSR is gaining prominence in the private financial sector, reflecting the common interests between banks and their clients.

There should be regulation in place to foster equality of opportunity and avoid anticompetitive conduct that could stifle responsible practices. It should remove unnecessary compliance costs and balance out the relationship between banks and consumers.

It is good practice to foster an enabling environment for data sharing and management. Market participants should be required to implement CSR policies and disclosure standards. This could enhance market discipline and improve risk management and the overall governance framework.

Policy-makers must take stock of the lessons from financial crises. They are unlikely to achieve economic stability without inclusive policies and diversified infrastructure for responsible, digital finance. Innovative solutions tailored to different clients’ risk profiles are needed to bring down the traditional barriers to finance.

Rodrigo Pereira Porto is Adviser at the Banco Central do Brasil.
Policy-makers must advance digital literacy

New, uncharted geographies of financial exclusion

When researchers Andrew Leyshon and Nigel Thrift wrote in 1995 about the ‘Geographies of Financial Exclusion’, the subtitle of their article was ‘financial abandonment in Britain and the US’. In those two developed countries, large proportions of the population were unable to access financial services. To make matters worse, financial service providers were actively pulling away from existing clients, seeking to reduce the risk of non-performing loans and to cut costs through branch closures.

Fast forward 20 years or so, and a new array of providers are reaching out to the remote, the excluded and the financially vulnerable with cheaper, flexible financial products delivered through digital channels. Data from the 2017 Global Findex, a database on the use of financial products, show that around 515m people globally have been brought into the financial system since 2014, many of these through access provided via mobile phones. Over the same period, the proportion of adults in developing countries using digital payments rose to 44% from 32%.

Digital technology can facilitate faster, more convenient and more cost-effective services that can provide access to previously marginalised and underserved groups. It makes it possible to provide financial services that are cheaper and better tailored to consumer needs, with fewer physical infrastructure requirements.

Such innovations have the potential to increase consumer welfare and support increased growth of the economy in a more equitable way.

At the same time, digitalisation raises new challenges and risks, which are likely to be amplified among new users. Consumers can behave differently when transacting online in terms of their spending and borrowing behaviour. The digital environment also creates new opportunities for fraudulent activities and abusive practices, and personal data becomes more vulnerable to theft, manipulation or misuse.

Protecting consumers

The convenience of digital financial services is not a universal truth. Access to such products requires a sound infrastructure and access to relevant hardware – telephone networks, internet connection, a reliable power supply, a computer and so on. Product design is also important. The likelihood of regular and somewhat unpredictable changes in the design and operation of financial products and services can cause considerable frustration and confusion among customers. Such changes could include the introduction of new interfaces and operations, changing forms of identification such as voice recognition, pin codes or pass phrases, documents shared in different file formats, or the possibility to gain access to an account through different types of platform. Virtual products delivered through rapidly changing platforms and communication channels may also pose problems for consumers who need to keep track of the products they hold and monitor changes. This is particularly problematic for products that are rarely consulted once bought, such as insurance and pension products.

Such inconveniences may affect certain segments of the population more than others. People in rural locations and those on low incomes are more likely to face difficulties created by inadequate infrastructure. People of all ages with reduced cognitive abilities or motor skills may find it difficult to learn new digital skills, handle passwords or enter pin codes. In this way, the tools intended to increase inclusion may inadvertently create a new group of excluded citizens, creating new forms of inequality.

To capitalise on the opportunities afforded by digital financial services, policy-makers must ensure that all consumers, including the most vulnerable, have the necessary financial and digital literacy to make the most of the products they hold. Financial consumer protection frameworks must continue to adapt to the changing landscape.

The Organisation for Economic Co-operation and Development leads global policy work on financial literacy and consumer protection in support of financial well-being and inclusive growth through the G20 OECD Task Force on Financial Consumer Protection and the OECD International Network on Financial Education. It has developed guidance notes on policies to support digital financial literacy and financial consumer protection in the digital age, and continues to work on the specific issues facing various vulnerable financial consumers including the elderly and microentrepreneurs.

Greg Medcraft is Director of the Directorate for Financial and Enterprise Affairs of the Organisation for Economic Co-operation and Development.
In conversation

Amplifying financial access

Kristalina Georgieva, chief executive officer of the World Bank and interim president of the World Bank Group, speaks to OMFIF’s Julie Levy-Abegnoli about combating extreme poverty, mobilising private sector capital and shifting to low-carbon economies.

Julie Levy-Abegnoli: The World Bank achieved gender parity among its senior ranks in late 2018, ahead of its 2020 target. How was this made possible, and what lessons can other financial institutions draw from this?

Kristalina Georgieva: Gender parity at senior management level at the World Bank Group is not an accident. It reflects a conscious and deliberate effort to walk our talk. We believe that gender equality is good economics and we want to amplify this message by example.

We pursue gender parity through ongoing efforts in recruitment, mentoring, promotion, retention and training. This includes a commitment to equal pay for equal work. We’re also deploying new technologies to increase women’s representation in the pool of job candidates for senior positions.

The lessons from this? First, that gender parity in the senior ranks is a realistic and achievable ambition. Second, that achieving this requires, like any business objective, an explicit strategy, senior ownership and regular reporting. Third, that achieving gender parity in the senior ranks helps deliver institutions’ full potential and meet the challenges of clients.

JLA: Financial inclusion relies heavily on technology, but those living in extreme poverty are becoming harder to reach. Without the right infrastructure in place in the world’s most deprived regions, how can poverty be tackled effectively?

KG: Infrastructure can catalyse economic growth and social development. And digital infrastructure helps poor and vulnerable people to access the digital economy, which can unlock access to education, healthcare, financial inclusion and jobs.

Broadband connectivity and participation in the digital economy are essential to long-term prosperity, yet around 4bn people still don’t have access to the internet. That’s why the World Bank will invest up to $25bn and mobilise at least $25bn from the private sector to get every government, business and individual in Africa digitally enabled by 2030. Both in Africa and elsewhere, efforts to boost connectivity must include people in low-income, rural and isolated areas.

It is possible to scale-up access, reduce costs and create inclusive internet experiences by tapping into new private sector business models and technologies such as small-cell solutions, drones and wifi balloons. By sharing networks and infrastructure, as well as combining civil works with private investments in sectors like energy or transport, we can get much closer to the goal of connecting everyone to the global digital economy.

JLA: In an increasingly fractured world, and as US foreign policy becomes increasingly unpredictable, is it more difficult for the World Bank to reduce poverty?

KG: Since 1990, 1.1bn people have been lifted out of extreme poverty, an incredible achievement. But progress is slowing, and poverty is becoming more concentrated, especially in sub-Saharan Africa and in conflict-affected countries.

And the progress we have made could be jeopardised as global headwinds intensify and the economic environment becomes more challenging. To make sure we eradicate extreme poverty, countries need to invest in people, foster inclusive growth and help develop resilient, low-carbon societies.

To achieve this, we need to work on new solutions to help countries access finance, especially from the private sector. We also need to focus on addressing fragility, conflict and violence by emphasising prevention and early action, remaining engaged during active conflict, and working in countries transitioning to peace.

JLA: Women face cultural barriers to access to finance and employment. What →
Supportive laws are an essential first step towards gender equality, by breaking down formal restrictions on women’s access to finance and employment. Changes to norms and behaviours need to follow these official changes to the legal system.”
is the World Bank doing to help countries overcome these barriers?

KG: There is broader recognition today that cultural barriers worsen economic constraints for women, such as their relative lack of assets and low participation in paid employment. For example, lenders may demonstrate unconscious bias against women by making decisions based on stereotypes about their ability to repay. In employment, social norms underlie occupational gender segregation and the undervaluing of work that is done predominately by women, in sectors like health and education.

Supportive laws are an essential first step towards gender equality, by breaking down formal restrictions on women’s access to finance and employment. Our 2019 report on ‘Women, Business and the Law’ shows that over 10 years, 131 economies have made 274 legal reforms, for example removing bans on women working in certain jobs or opening bank accounts without a male relative’s signature.

Changes to norms and behaviours need to follow these official changes to the legal system. This requires not just sustained political will but also strong civil society and women’s movements, given risks of backlash as women make gains and during economic or social crises. We also know that men need to change for there to be true gender equality. Progress has been slow on that front, even with a growing number of male champions for gender equality.

JLA: The World Bank is on track to reach its ‘universal financial access by 2020’ goal of enabling 1bn people to gain access to a transaction account. What will be the next steps in terms of ensuring this success is sustained in the long term?

KG: Compelling evidence shows that basic payments and financial services can improve resilience and productivity, helping reduce poverty at the household level. This makes a solid business case to expand and scale the range of interventions to improve financial inclusion.

Between 2011-17, 1.2bn previously ‘unbanked’ adults opened accounts for the first time at regulated financial service providers, according to the Global Findex database. Over the past six years, our work on this agenda with partners has convened knowledge, investment, and financial services in 25 priority countries, including 13 low-income countries.

Nonetheless, the 1.7bn adults who remain unbanked pose an urgent development challenge that we must address. To keep up the momentum through 2020 and beyond, we are providing targeted assistance to reach adults in hard-to-reach areas, low-income countries and fragile economies.

JLA: What will the most pressing challenges of the next 10 years be for the World Bank?

KG: Climate change is an acute threat to global development and efforts to end poverty and will have an outsized impact on the poorest and most vulnerable. We estimate that climate impacts could push an additional 100m people into poverty by 2030, unravelling development gains to date.

Climate action offers a major opportunity to ensure sustainable global development and boost economic growth. Through 2030, a shift to low-carbon, resilient economies could translate into $26tn in economic benefits and create 65m new jobs.

We are working to make sure economic growth benefits all people and addresses the challenges to economic stability. At the centre of our efforts is our commitment to ensure that growth works for the poor and helps narrow gaps for women and disadvantaged groups.

Technology is disrupting the world of work by changing the nature of firms, creating new business models and expanding job opportunities. While advances in technology put some jobs at risk, they also provide economic opportunity for millions of people living in poor countries.

The challenge will be to prepare people to seize that potential, so we are helping countries make smart investments in their people and accelerate progress in programmes that foster nutrition, health, education, jobs and skills. And because workers are expected to have multiple careers, not just multiple jobs over their lifetime, countries must invest in lifelong learning. The changing nature of work will also require new social protection systems as diverse and fluid forms of employment may leave many with no or little access to social protection.

‘By sharing networks and infrastructure, as well as combining civil works with private investments in sectors like energy or transport, we can get much closer to the goal of connecting everyone to the global digital economy.’

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Profile

Education: Holds a PhD in Economic Science and an MA in Political Economy and Sociology from the University of National and World Economy, Sofia.

Career: Georgieva held many high-profile positions before becoming CEO of the World Bank. She previously helped shape the agenda of the European Union starting in 2010, first as commissioner for international cooperation, humanitarian aid and crisis response. As European Commission vice-president for budget and human resources, Georgieva oversaw the EU’s €161bn budget and 33,000 staff across its institutions around the world, and tripled funding available to the refugee crisis in Europe. She had a successful tenure at the World Bank before joining the Commission, starting in 1993 as an environmental economist, eventually becoming director for environment and social development for the East Asia and Pacific region and then director in charge of environmental strategy, policies and lending. In 2004, Georgieva was made World Bank director for the Russian Federation, based in Moscow. From 2007-08, she was director for sustainable development in charge of policy and lending operations in infrastructure, urban development, agriculture, environment and social development. Between 2008-10 she was vice-president and corporate secretary, serving as the interlocutor between the World Bank Group’s senior management, board of directors and shareholder countries.
Global public investors and a sustainable world economy

This panel discussion marks the launch of the sixth annual Global Public Investor publication devoted to public sector asset ownership and management around the world. The meeting focuses on the key issue of sustainability and aims to share best practice among investors.

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Money Matters

Why we should care more about money
Central banks should anchor policies in more solid economic relationships

Juan Castañeda and Tim Congdon
Institute of International Monetary Research

At a recent event in London with former senior officials of the European Central Bank, a member of the panel, when questioned about the sluggish growth of broad money in the euro area, claimed that ‘nobody cares about money’. Central banks seem to be focused – perhaps too focused – on the determinants of inflation in the very short term.

In this timeframe, the information conveyed in monetary data may appear to be useless for policy purposes. It normally takes one to three quarters for changes in money growth to affect output, and longer for them to influence inflation (or deflation). But the lags do not disqualify money as a major policy indicator. The problem is that, in the short term, there are myriad indicators affecting the rate of inflation and output; when making policy decisions, central banks ‘cannot see the forest for the trees’. It would be better for central banks to anchor their policies in well-established and solid relationships, such as that which holds in the medium and long terms between changes in the quantity of money and changes in nominal national income.

The latest figures on money growth in the euro area are worrying. This is the first month we have data since the ECB halted its asset purchase programme at the end of 2018. In the euro area, in the three months to January 2019 broad money growth (M3) fell to 3.4% from an annualised rate of 5.7%. In addition, there was a drop in the quantity of money not only in Spain, Italy and Greece, but also in Germany. Similar concern must be expressed about Japan and the UK, where money growth has been weak (1.0% and 2.4% in the last three months at annualised rates, respectively).

Upward pressures on inflation are absent from these economies, while legitimate fears arise of further deceleration in output growth in 2019 and even into 2020. More positive news comes from the US, where in the three months to February 2019 broad money expanded at an annualised rate of 7.1%. The contractive effect of the Federal Reserve’s asset run-on on the quantity of money is being offset by a robust increase in bank credit. The more patient approach to the shrinking of the Fed’s balance sheet announced by Chairman Jay Powell argues for at least trend demand and output growth in coming quarters.

Juan Castañeda is Director and Tim Congdon is Chairman of the Institute of International Monetary Research. For a more detailed analysis of the latest money trends, see the IIMR monthly report at https://www.mv-pt.org/monthly-monetary-update.
Worldview

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The Fed that Trump built
President’s bluster on monetary policy is unusual, his Fed nominees less so

President Donald Trump has appointed or reappointed all but one of the five members of Federal Reserve board of governors. Two openings remain on the seven-member board after two other nominees in the previous Congress never received Senate confirmation.

In late March, Trump said he would nominate an economic adviser, Stephen Moore, to one of the board vacancies without waiting for the usual vetting procedures. Moore has been a fierce defender of the Trump economic policy he helped fashion and co-authored in March a Wall Street Journal op-ed criticising the Fed as a threat to growth.

The Moore nomination, which is likely to face an extended review and considerable opposition in the Senate, marks a departure from Trump’s earlier nominations to the Fed, which were largely mainstream economists. It represents an escalation of his fight against Fed Chair Jay Powell to keep interest rates low, even though Fed policy-makers have since pivoted to a pause in rates. Markets now expect the Fed to cut rates this year rather than raise them.

Even as he bashes Fed policy, Trump has a relatively free hand to fashion a Fed according to his priorities. He has made it clear he wants low interest rates, a not-so-strong dollar, and likes people willing to do what he says. The Moore nomination is the first that is clearly in line with those priorities.

Trump moderated his criticism of the Fed after Powell led a pivot on policy. Powell had a ‘cordial’ White House dinner with the president in February. None of that stopped Trump returning to his critique at the Conservative Political Action Conference in early March. The president pilloried Powell (without naming him) for raising rates and tightening liquidity, setting up the Fed as scapegoat if the economy falters.

One of last year’s failed nominations was Carnegie Mellon economist Marvin Goodfriend, an inflation hawk who raised doubts in his Senate hearing that he would pursue both goals of the Fed’s dual mandate (stable prices and maximum employment) with equal vigour. It was a curious nomination from a president who at CPAC criticised Powell for preempting inflation that isn’t there.

Goodfriend was not nominated again in the new Congress. The other nominee was Nellie Liang, a long-time Fed staffer now at the Brookings Institution. She foundered in the Senate on her penchant for enforcing tough bank regulation, which goes against Republican principles.

Trump’s appointments so far have included Randal Quarles, a former Treasury official and private equity investor, who became the first to occupy the vice-chairmanship for supervision established by the Dodd-Frank financial reforms. In November 2018, Quarles was named head of the Financial Stability Board, the global group setting guidelines for bank regulation.

Michelle Bowman, former banking commissioner in Kansas and official at a small family bank, filled the seat allotted to community bankers, while Richard Clarida, a Columbia University economist and Pimco adviser, took the vice-chairman post. Alongside New York Fed President John Williams, ex officio vice-chair of the Federal Open Market Committee, the two economists flank non-economist Powell in steering policy.

Puzzling orthodoxy
Trump made Powell chairman in the belief that, unlike his predecessor, Janet Yellen, he would be more pliant in following the president’s desire for low interest rates. Whatever impression Trump had gathered from his conversations with Powell proved wrong, however, as the institutional momentum of the Fed took over.

The orthodoxy of nominees had been puzzling, given Trump’s priorities and recalling that during the campaign he seemed sympathetic to the principle of modern monetary theory that deficits don’t matter. ‘You never have a default because you print the money – I hate to tell you,’ he said to one interviewer.

Fed governors are supposed to be above politics, but appointments in the past generally kept a balance in political affiliation. Last year’s nominations were paired for balance, with Goodfriend affiliated to Republicans and Liang a registered Democrat. Among those being confirmed, there is less balance. The top three posts are occupied by men who were political appointees at the Treasury during Republican administrations. Bowman was a congressional aide for Republican Senator Bob Dole. Moore, of course, is Republican.

President Barack Obama appointed Powell in 2014 in those days of balance. Lael Brainard on the board of governors is the only other holdover from that time. Affiliated to the Democrats, she served in both the Clinton and Obama administrations. Her Fed term expires in 2026, though governors rarely stay that long. •

Darrell Delamaide is US Editor at OMFIF.
The US Treasury market is one of the largest, most liquid financial markets in the world. It serves as a critical store of value, hedging vehicle and risk-free benchmark, and is a key component of monetary policy. Some of the largest owners of US Treasuries include state, private and individual pension funds. The evolving regulatory landscape and recently implemented bank liquidity coverage ratios are increasing demand for high-quality liquid assets, including US Treasuries. The landscape for infrastructure, including securities clearance and collateral management in the US, is also transforming. This will facilitate greater access to highly liquid assets.

A priority for dealers, investors, regulators and clearing banks following the 2008 financial crisis was to reduce overall risk, empower market participants with resilient technology systems, and strengthen US tri-party repo infrastructure reform. Through partnership and collaboration, the industry implemented reforms recommended by the market-based Tri-party Repo Infrastructure Reform Task Force, formed in September 2009 under the aegis of the Payments Risk Committee sponsored by the Federal Reserve Bank of New York. Those reforms sharply reduced the market’s reliance on discretionary extensions of intraday credit by the clearing banks and led to improvements in market participants’ liquidity and credit risk management practices.

Building resilient systems
Several opportunities are arising in connection with the US government securities market, particularly as the rise in short-term yields from US Treasuries is restoring their attractiveness to investors as a short-term investment vehicle.

The US Treasury recently announced a net new issuance of around $1tn this year and anticipated increases next year that will contribute to increased demand for clearance, settlement and collateral management services.

An interesting trend in the Treasury market is the growth in the number of direct bidders at Treasury auctions. Direct bidders, including large investment managers and foreign banks, have increased their purchases through an online portal called Treasury Direct, where they can buy all varieties of US Treasuries.

Innovation in collateral management, technology risk and resiliency, as well as emerging short-term investment vehicles, will have an impact on the financial services industry in the coming years. Through the recently launched BNY Mellon Enhanced Collateral Portfolio Optimisation solution, our clients benefit from a better way to optimise and mobilise collateral across the globe. US Treasuries are a critical component for a variety of financing, investment and regulatory purposes used by the buyside and dealers.

Market participants are demanding increased mobility of collateral across depositories, efficient clearing of securities and new data services in the light of rapid advances in financial technology. It will be the industry’s shared responsibility to plan for risk and ensure resilient systems are in place to protect participants.

Brian Ruane is the Chief Executive Officer of BNY Mellon Government Securities Services and Segment Head for Alternative Asset Managers, and Banks & Broker Dealers. Views expressed are of the author and do not necessarily reflect the views of BNY Mellon. The mission of GSS is to enhance the capabilities, governance, transparency and resiliency in the US government securities clearance and US tri-party repo businesses.

‘Direct bidders have increased their purchases through an online portal called Treasury Direct, where they can buy all varieties of US Treasuries.’

US Treasury issuance breaks $1tn in 2019
Gross bond issues, $tn

Source: US Department of the Treasury, Bureau of the Fiscal Service
North Rhine-Westphalia is a highly diversified business location with conditions that offer investors optimal opportunities to grow their business. Above all, companies value the region’s central European location. With 17.9m inhabitants, NRW is the most populous of Germany’s 16 states. Around 160m people – almost one-third of all EU consumers – live within a 500km radius of the state capital Düsseldorf. From no other location in Europe can so many people with such high purchasing power be reached within such short distances as from NRW.

The state accounts for 21.5% of Germany’s purchasing power. NRW inhabitants spend more than €360bn annually on private consumption and already constitute an interesting consumer market in themselves. In 2017, the state generated 21.2% of German GDP at €692bn, equivalent to 23% of UK GDP. If it were an independent state, NRW would rank 22nd in the world by GDP.

The size of the market attracts companies to the Rhine and Ruhr. In 2017, industry turned over around €350bn and formed the basis for success in many sectors. NRW is home to large industrial corporations of global standing, as well as dozens of smaller companies that are leaders in their respective fields. One in four German world market leaders comes from NRW, and 20 of the 50 highest grossing German companies have their headquarters here, including Bayer, Bertelsmann, Deutsche Post DHL, Deutsche Telekom, E.ON, Henkel and thyssenkrup. Around 712,000 small and medium-sized enterprises form the economic backbone of the state. The trading volume is remarkable: 15% of German exports are ‘Made in NRW’, with a total value of €191.4bn. Of all German imports, 21.9% (€228.4bn) go to NRW.

Excellence through diversity
NRW has established itself by a wide margin as a leading investment destination for global companies. With €179.3bn at the end of 2016, the state recorded the largest share (26.1%) of the total €686bn of direct investment in Germany.


There are around 20,000 foreign companies based on the Rhine and Ruhr. Among them, 1,500 come from the UK, accounting for 22.1% of British firms in Germany. The UK’s leading online retailer for household appliances, AO, has its European headquarters in the region. The company takes advantage of the outstanding logistics infrastructure to capture the European market from NRW. Another example is the telecommunications provider Vodafone, which manages more than just its German business from Düsseldorf. It also operates the company’s Vodafone Innovation Park, where new technologies and services are developed.

NRW’s excellent infrastructure plays an important role in the choice of location. All major European cities can be reached within three hours from the two international airports in Düsseldorf and Cologne/Bonn, Germany’s third-largest cargo airport. A network of waterways, railways and roads provides fast routes to the sales and procurement markets in Europe and the world. In Duisburg, the world’s largest inland port ensures reliable connections to Belgian and Dutch seaports.

As an innovative business location, NRW is characterised by its diversity. More than 110 technology centres and non-university research institutes in the state form Europe’s densest research network. The wide range of studies offered by the 70 universities and universities of applied sciences with more than 772,000 students ensures that companies can find qualified employees here.

NRW.INVEST, the state-owned economic development agency, campaigns worldwide for foreign direct investments for NRW. In June 2018, the new NRW.INVEST UK office was opened. It provides companies from all sectors with individual services – from information on markets, locations or investment conditions to practical assistance with specific settlement projects.

nrwinvest.com
Asset managers in business of disruption
Embracing new technologies and shifting mentalities to remain competitive

Latest technology trends are reconfiguring the asset management industry. These forces – named for the disruptive companies from which they originate – include 'Watsonisation' (the development of cognitive computing), 'Googlisation' (the availability of ever_greater_volumes of data), 'Amazonisation' (the power of platforms and the accrual of user information), 'Uberisation' (the growth of computer-enabled on-demand business models) and 'Twitterisation' (working in an increasingly connected world). How asset managers adapt will decide whether their businesses survive.

Barriers to entry are lower in asset management than in other areas of finance. It is a low-capital and high-margin business, with supposedly low levels of innovation and investment underperformance. These factors make asset management an attractive target for new entrants, mainly technology companies.

To contend with this influx of competition from small and agile companies, incumbent asset managers must renovate their business models. Modern institutions must be intensely customer-centric, focusing on product diversity, flexibility of service, transparency and ease-of-use, especially with regard to connected technologies such as mobile apps and other digital platforms.

Asset managers must be both global and local, retaining knowledge of global markets while demonstrating proximity to local customers. When working across borders, it is essential to optimise distribution networks and forge partnerships with local entities. Seeking out distribution agreements with international banking networks is especially useful and can reduce costs when entering new markets.

Firms must look beyond savings and cash flow management. They should consider offering products pertaining to regulatory reporting and risk management, and develop other chargeable advisory services in areas relevant to the asset management industry.

Today’s battle is less about the big and powerful companies against small and weak ones, and more about competition between those that are agile and those that aren’t. Where possible, developing a network of financial technology start-ups (and companies in the related fields of ‘regtech’ and ‘insurtech’) makes sense for larger businesses.

Expert data management
Being agile means making the most of the surge in 'big data' and advances made in 'robo-advisers' that provide automated guidance and services, including in active management, 'smart beta' strategies and fund selection. Recruiting experts in robotic process automation can lead in the long term to lower costs and higher quality of services. By automating some parts of their business through software or the use of artificial intelligence, firms can increase productivity, improve process control, facilitate compliance monitoring and improve the quality of service provided to clients.

By better analysing available data, asset managers will be able to discover hidden factors that affect client behaviour. In the best_case_scenario, this will allow firms to forecast customers’ needs and preferences.

Robo-advisers pose a threat to traditional wealth managers, diverting flows away from active investment strategies to passive ones. According to Deloitte, by 2025 robo-advisers will manage as much as $7tn worth of assets, up from less than $30bn today.

Alternative indexing and smart beta strategies are similarly likely to see a rise in popularity as long as investors and regulators prefer low-cost and rules-driven approaches. These strategies forgo conventional market capitalisation weights in favour of alternative schemes based on measures such as dividends or volatility. In this way a manager passively follows an index designed to exploit systemic biases or market inefficiencies.

Expert data management leads to better decision-making. Instead of following the traditional hierarchical model, where decisions are made in accordance the opinion of the highest-paid person, asset managers should ‘listen’ to the data. This will allow equity portfolio management teams to seize more quickly upon trends and relationships between asset classes and assets.

As investments becomes more data-driven, the quality of transactions and trading platforms will be an increasingly important competitive factor. Blockchain will make it possible to enter automatically any online trade and provide full transparency for all transactions. By circumventing intermediaries, blockchain is likely to lower costs, require fewer error reconciliations, accelerate settlement and increase transparency with fast, simple, efficient and low-cost oversight.

To remain competitive and profit from new opportunities, asset managers must think more about their business models and look beyond simple improvements. We are in the business of disruption. This requires new thinking, a deliberate shift in mentality and effective leadership at both company and industry levels. These are the keys to success.

Philippe Ithurbide is Global Head of Research at Amundi.
Trilemmas obstruct cryptocurrency uptake
Digital currencies with centralised governance more likely to prosper

The fourth quarter of 2018 saw a strong contraction in the cryptocurrency market, leading to a 45% loss of almost $100bn in market capitalisation. This is hardly surprising: the value of peer-to-peer cryptocurrencies has no clear economic or legal basis. They do not satisfy the three basic functions of money as a store of value, means of exchange and unit of account. The steep increase in the exchange rate in the early stages of their adoption was simply unsustainable.

While the initial excitement around disruptors such as bitcoin is waning, the debate around crypto-assets is far from over. There are myriad reasons to keep watching this space.

Crypto-enthusiasts argue that, through the widescale adoption of blockchain technology and cryptocurrencies, it is possible to build a financial system with decentralised governance. There are several issues with this ideal. First, before you can trust an algorithm you need to trust its coder. Ultimately, the ‘money’ business is a ‘trust’ business. Supporters implore, ‘Trust the code, instead of the intermediary.’ But most people cannot interpret the code, so they need to hire someone to vet it on their behalf. But that only involves another intermediary, only this time it’s an auditor.

Second, a system operating on centralised governance is more likely to succeed, given the strong economies of scale behind the proliferation of digital assets. The economic forces propelling digital assets are no different than a platform-dominance game: the value increases (for all customers) as more clients join. For example, having one phone in a network is useless, but having 10 phones is much more useful. By extension, the value of the network increases as more people join.

Impossible trinity
One area where algorithms could potentially assist is in the conduct of monetary policy rules, such as the Taylor rule, the proposed guideline for how central banks should alter interest rates in response to changing economic conditions. However, it is hard to imagine central banks putting monetary policy ‘on autopilot’ without some form of public accountability. It would raise problematic questions about who would bear ultimate responsibility when things go wrong.

More importantly, monetary policy is often discretionary, not rules-driven. There is a difference between decentralised software, and a market without public intervention. Technology could help to address the first issue, but market failures exist irrespective of technology. Public intervention will not disappear even following a breakthrough in technological innovation.

There are two main issues stopping governments from adopting cryptocurrencies. One relates to technology, the other to international finance and politics. The first is what Vitalik Buterin, the co-creator of the cryptocurrency platform ethereum, calls the ‘scalability trilemma’. This describes the impossibility, at least with current technology, of having cryptocurrencies that are simultaneously scalable, secure and fully decentralised. You can choose two of the three, never all of them together. Bitcoin, for example, prioritised security and decentralisation over scalability. Conversely, if you want a decentralised and scalable cryptocurrency, you must make concessions on security.

The second relates to another popular ‘impossible trinity’, espoused by economist Lars Oxelheim. This states that a country cannot achieve free capital mobility, monetary policy autonomy and a stable exchange rate all at the same time. For example, if a small open economy decides to peg its exchange rate to that of a more developed country, then the smaller country must make a choice. Either it preserves the freedom to conduct monetary policy in the presence of capital controls, or it binds its monetary policy to that of the other central bank, preserving free capital movements. If two countries had, for example, different policy rates in the presence of free capital mobility, strong capital flows would add further pressure to break the parity.

The question then is how cryptocurrencies fit within the latter trilemma. On the one hand, governments can shut down cryptocurrencies at any time. However, even if they were to adopt a cryptocurrency as legal tender, the ‘impossible trinity’ would bind governments to stick to either option A or B (see Chart), diminishing their policy options.

The blockchain technology that underlies cryptocurrencies remains promising. One area with much potential is that of securities trading on a blockchain platform: security tokens. But I don’t expect there will be a wide adoption of private cryptocurrencies. Instead, policymakers are likely to forge ahead with central bank-issued digital currencies.

Carlo Cocuzzo is Economist at ING.
Cash is democratic, inclusive, secure and sets the efficiency benchmark for all payments systems. It does not carry any transaction fees, neither for the payer nor the merchant. Moreover, it is an indispensable and public good, underpinned by trusted public institutions, namely central banks. Altogether, cash is an excellent means of payment. But, at least anecdotally, cash seems to be losing favour, even as the number of banknotes in circulation continues to rise.

In advanced economies, most transactions are conducted electronically, without need for coins or notes. In addition to debit and credit cards, the use of other means of payment, such as bank apps on smartphones, is increasing in volume and value.

Demand for digital money is likely to increase. The burden is now on policy-makers to decide if this demand warrants the establishment of a central bank-issued digital currency, and if so fulfils those institutions’ public obligations.

In the private sector, cryptocurrencies like bitcoin, ethereum and others have attracted a great deal of publicity, but have not lived up to enthusiasts’ vaunted expectations. They do not satisfy all the functions of a currency, as a measure of value, unit of account and medium of exchange.

For central banks, the question is what kind of digital asset they could provide that complements cash. There has been an explosion of research, discussion and experimentation over recent years on the possible uptake of central bank digital currencies. These assets would be issued and controlled by the central bank and linked to the value of a country’s conventional elastic currency. The CBDC would have to be accepted everywhere as legal tender, and serve as a store of value and trust. It would have to meet the highest cybersecurity requirements while remaining inclusive and easy to use.

**Inclusion and innovation**

Various forms of CBDC are possible, each with different implications for payment systems. From our research and conversations with central banks, we have identified five key topics for consideration.

The first is control, as CBDCs could strengthen the position of central banks in the digital world. Central banks currently offer private individuals access to central bank money only in the form of cash, while consumer payments in the digital world are left entirely to commercial banks and other private providers.

When shaping its own digital currency, a central bank could design it to be inclusive and grant a level of privacy protection. Everybody should be able to pay for goods and services without disclosing their personal data to some third-party payment corporation. Equally, policymakers understand well that certain types of transactions must be transparent to curb money laundering and tax evasion.

The second topic relates to financial inclusion and ensuring unfettered access to payment services. By capitalising on the expansion of mobile banking technology, CBDCs could represent the next stage in advancing financial inclusion. This may prove especially relevant in countries with large unbanked populations. CBDCs, supported by appropriate digital infrastructures, can enable buyers and merchants to execute payments more efficiently.

The third concerns costs of digital payments, which CBDCs could reduce. Today, all forms of digital payment carry some sort of transaction fee, at least for the merchant. Cash serves as a corrective instrument to ensure competition among different payment instruments. A CBDC could fulfill the same function.

Fourth is innovation. A CBDC could offer access to central bank money for players besides commercial banks. This could facilitate experimentation and the creation of new services and business models. That being said, the digital currency market, as it exists now, is highly volatile and fragmented, especially among financial technology companies.

The fifth topic, invariably, is technology. A digital currency creates a new type of asset, based on new technology. This requires new institutional and legal arrangements that complement the existing architecture of payment systems. It will require, too, input from trusted partners with experience in these systems as well as in certified security solutions. Policy-makers will have to prioritise research into these arrangements and the related digital infrastructure that would support the uptake of CBDCs.

‘By capitalising on the expansion of mobile banking technology, CBDCs could represent the next stage in advancing financial inclusion.’

Christian Jüttner is Group Vice-President and Chief Project Officer of Currency Management Solutions at G+D Currency Technology.
In pursuit of fintech hubs
Companies flocking to locations that boast three key ingredients

Marcelo Giugale
World Bank

Financial technology centres hold the promise of high-paying, city-transforming, youth-employing jobs. They can bring in foreign currency and spur inventiveness. And they are seen as a way for poor people to access finance, and for poor countries to accelerate economic development.

Fintech hubs are the dots in the map where fintech entrepreneurs cluster. In places like Dublin, Mumbai, San Francisco, Shanghai and Tel Aviv, visionaries devise what the Bank for International Settlements calls ‘information technology-enabled innovations that result in new business models, applications, processes and products.’

Policy-makers the world over are trying to nurture fintech hubs, but it has not been easy. In November 2018, a consortium led by China’s Zhejiang University published the first Fintech Hub Index. It reviews and ranks 55 hubs, classifying them into ‘global’, ‘regional’ and ‘emerging’. The results are telling: other than ‘regional’ and ‘emerging’ category. The countries in which successful hubs have sprouted display three broad ingredients.

First, they have a sensible macroeconomic framework. No one would set up a technology business in an economy from which profits cannot be repatriated, or to which it is impossible to import what is needed. Nor is it advisable to start a business in a country where the tax burden is too large or too unpredictable, or whose banks and financiers have no incentive to lend to anyone but the government. In other words, market-based foreign exchange regimes, open trade, healthy fiscal accounts and sound financial systems are key ingredients to catalyse fintech.

The second ingredient can be called ‘enabling factors’. These include a large talent pool – or the possibility of obtaining a work visa – reliable broadband and physical space in which to collaborate with others. This is when a quality education system, efficient infrastructure and an appealing geographical location begin to matter.

Third, fintech entrepreneurs flock to countries that offer a legal and regulatory environment in which their business can operate more or less unencumbered. The issue is not just about the laws and regulations that protect intellectual property and data privacy. It is also about the speed at which legislators and regulators can catch up with the innovations put forward by the fintech industry. Just a few years ago, most policy-makers had never heard of Venmo, the digital wallet that lets you make and share payments with friends. Therefore, they could hardly regulate it. That is partly why governments wishing to speed up the birth of fintech hubs enact regulatory ‘sandboxes’, allowing companies to test new ideas without waiting for approval.

Room for hope
Few developing countries can provide the macro, enabling and legislative ingredients necessary for fintech hubs to emerge. But there is hope. Fintech is usually produced in ‘value chains’. Services like crowd-funding, mobile wallets, peer-to-peer transfers, digital currencies, e-trading, robo-advice and blockchain-enabled bonds are the result of functions that can be split and performed across borders. There is no reason why design and coding, data aggregation, portal management and hardware maintenance should be done in the same hub, or even the same country. The same applies to big data analysis, security monitoring, outreach, branding, customer service and regulatory advocacy. This opens the door for countries with less capacity to join the production chain at the point where it is easiest for them. These locations can become a hub for the lower-tech part of fintech. Kenya, Lithuania, Mauritius, Uruguay and others are likely to move in that direction.

Ultimately, whether at the top or at the bottom of the sophistication scale, fintech hubs require clear signs of political support in order to thrive. Mobile by nature, ‘hubbers’ only move in and stay if they are welcomed by those who make public policy. After all, fintech is about disrupting established markets – as was the case for commercial banks, travel agencies and taxi drivers. This is a process rich in winners and losers and, thus, in potential for political backlash.

Marcelo Giugale is the Director of Financial Advisory and Banking at the World Bank.
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In recent years, the idea of universal basic income has become an increasingly popular point of discussion as a potential means of improving financial inclusion. How viable a solution is this? If not UBI, how best can policymakers address widening economic inequality?

Poll of OMFIF website users, OMFIF advisory board and Twitter users.

UBI is no viable solution, it is only figments of imagination. The solution is quite more concrete and difficult to implement because of strong political opposition led by economic interests.

Hans Eichel, former minister of finance, Germany

UBI should not to be rejected prima facie, but before genuinely free essential public services are a better place to start. If income support is needed, then it is better done at the municipal level. This essentially is the Nordic welfare system.

Olivier Rousseau, Fonds de réserve pour les retraites

Everything depends on fiscal sustainability. Ideally, it should be part of a serious fiscal reform package. As most of economic agent’s decisions are based on marginal costs and benefits, UBI should not lead to lower allocation efficiency. It certainly can alleviate inequality.

Miroslav Singer, Generali CEE Holding

As my countryman Rutger Bregman said in his book Utopia for Realists, UBI can simplify the many subsidies, welfare and tax credits that complicate existing policies that are intended to support low-income groups. Experiments could be trialled at the local level. A better way to address widening wealth inequality is raising taxes on high incomes.

Roel Janssen, Dutch financial journalist, formerly of NRC Handelsblad

In 2014 Norges Bank commissioned Snøhetta Design to develop a concept for one side of a new series of banknotes. As their 1,000 kroner prepares to be sent into circulation in 2019, we interview Martin Gran, managing director of Snøhetta Design.

Your banknotes are very different from those that most people have encountered before. How did you go about developing these designs?

Our design explores the beauty of boundaries of the Norwegian coastline – the boundaries between sea and land, land and air, and air and sea. By linking the coastline with a design inspired by ancient mosaics, we have translated this analogue art form into the mosaics of our time and the digital era: pixels. In this sense, the design connects the idea of boundaries with travelling through time, between old and new, past and present. The waves and pixilated patterns differ for each banknote, whether a 50, 100, 200, 500 or 1,000 kroner note, by referencing the Beaufort scale that measures wind speed. On the 50 kroner note the wind is gentle, represented by a dense cubic pattern and long, tame waves. At the other end of the scale, the 1,000 kroner note is characterised by a strong wind, expressed through long, pixelated cubes and short, choppy waves.

Did security implications factor into the design, and were there any other challenges you faced compared to other projects you’ve worked on?

The security aspect was vast, and we were trained in all the security measures for banknote designs. We attended in-house security seminars and needed to set up a secure server for our work. It is probably the project with the strictest security measures in the history of Snøhetta.

Most banknotes still have highly traditional motifs. Should other central banks be more willing to commission similarly creative designs for their currencies?

Banknotes are indeed pretty traditional, and many times for good reason. The institutions that undergird them need to have a certain authority. This can be expressed through conservative designs that take cues from more traditional symbols and graphics. However, Norway’s high level of transparency and emphasis on equality can also be an interesting focus for a design. We wanted our banknote designs to reflect modern Norway.

Do you think there will still be room in the future for these sorts of innovative designs for banknotes? Do you believe the shift towards a ‘cashless’ society will fetter the medium?

We believe that banknotes will be present in our society for many years to come. Even if the decline in usage is high, banknotes have a very significant symbolic value. Some people believed that books would vanish when radio broadcasting arose at the start of 20th century, and yet we still read analogue books. It is almost like analogue media are taking their revenge in the digital era.
Adaptability

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