

François Groepe: Improving the security and cost-effectiveness of banknotes

Address by Mr François Groepe, Deputy Governor of the South African Reserve Bank, at the 18th conference of the Association of African Banknotes and Security Documents Printers (AABSDP), hosted by the South African Bank Note Company (SABN), Cape Town, 17 November 2014.

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Good day ladies, gentlemen and fellow central bankers, a warm welcome to South Africa, welcome to the Mother City and the 18th Conference of the Association of African Banknotes and Security Documents Printers (AABSDP).

Cape Town is one of the most beautiful and well-known cities in the world – it is rich in history, art, culture, nature and I sincerely hope that you will enjoy your stay. Its fame, and that of South Africa, has been lifted by the extraordinary courage and dignity of one man, Nelson Mandela, and I am proud that our new currency pays homage to this great man.

I have been informed that we have more than 300 delegates attending the Conference, representing 80 organisations around the world, of which more than 25 central banks are represented and various government institutions, such as printing works and mints. From the outset we have aimed to invite a broad spectrum of people as possible and I am delighted that we have succeeded in this endeavour.

The theme of this Conference this year is top of mind in the Security Printing Industry today, as well as for Central Banks – that of improving security and cost effectiveness of banknote production and circulation which, if done successfully will contribute to efficiencies in the cash management cycle.

Following the Great Recession, most central banks had either their mandate expanded or their mandate was more explicitly defined to include financial stability. The supply and availability of cash is a critical component of financial stability because a shortage of physical cash can lead to socio-political instability which may result in spill-over effects. Hence, it is important that central banks approach and treat cash management with the same diligence as they treat their monetary and financial stability mandates, as it does not stand separate from those mandates, but in fact is a key component of those mandates.

Central Banks are continuously confronted with new developments in the design, production, circulation and destruction of banknotes. The participation of various and new stakeholders in the banknote lifecycle, trends in substrate choice, features and banknote life expectancy, heightened demands for improved productivity and efficiency and emerging threats from counterfeiters all add to this challenge.

Banknotes remain the most important contact point for Central Banks with the public and therefore they play a key role in the reputation and public perception of the central bank. The quality of banknotes in circulation also poses a reputational risk for the central bank and in fact for the country. Poor quality banknotes cannot be used by the people to pay for example their parking tickets where the pay-station will not accept poor quality banknotes. Furthermore, poor quality banknotes, would lead to jamming of automatic teller machines but also increases the risk of counterfeiting. These are but three examples of why it is important that the quality of banknotes in circulation should be efficiently and effectively monitored and controlled by the central bank, irrespective of the degree to which off-sorting may have been privatised within a particular country.

The type of substrate to be used remains a very topical subject within the industry. Central banks from both large and small economies have challenged the long accepted wisdom over security and the longevity of banknotes. The longer a banknote lasts, the more value the

central bank will obtain from that particular note order. Given the size of orders, even a small improvement in percentage terms can mean a substantial improvement in profitability. During the Conference we will be debating this at length. Among our speakers, we have the Bank of Canada, they recently changed their notes from paper to polymer and will share their experiences with us.

The demand for cash is increasing and so is the cost of transporting and processing the cash. Central banks increasingly recognise the need to revisit nationwide arrangements for distribution and consider the role of the private sector; however, outsourcing brings with it its own risks.

Whether sorting is carried out in-house or outsourced, central banks are under increasing pressure to improve efficiency. During the course of the Conference some of the presenters will focus on the different cash management systems employed by central banks.

Another challenge, facing the industry, is the forecasting of the demand banknotes. It seems that there is no simple method to do this calculation. In South Africa, as in many other countries, the demand for currency is showing an increasing trend. In 2012, the demand for currency increased by 11 per cent with approximately R110 billion (US\$ 10.6 billion) worth of notes in circulation as at the end of the year. Central banks, therefore, are faced with challenges to either reduce the volume of cash produced; or reduce the cost of producing the cash, while at the same time enhancing the security and durability of the currency.

A new challenge for central banks is the requirement that all key business areas should be included in effective contingency plans. High profile incidents around the world have highlighted the importance of central banks having in place, considered and tested plans, to deal with outages due to everything from supplier problems to natural disasters.

Generally, central banks source their banknotes from one, or a small number of international companies. Currency managers need to weigh-up the importance of price against considerations, such as time of delivery, quantity of order and quality of product. They also need to consider if more than one supplier for, say ink, could be beneficial for operational risk concerns. Procurement from external suppliers is expensive, complex and may span several years. As with any outsourcing arrangement, production and quality, a standard needs to be monitored.

The impact of technical innovations for the distribution of cash or payment mechanisms is developing at a rapid pace, especially for the under-banked. The use of mobile phone technology to transfer money is becoming a popular method due to efficiency and the lower cost associated with this payment mechanism.

A further consideration by central banks is the cost that security features add to the banknote production process. We all appreciate the need for security features to avoid the counterfeiting of banknotes, but the question is at what cost and whether these costs can be optimised? These issues will be presented and debated upon during the next few days by all the participants and hopefully assist central banks with their deliberations in this regard.

The objective is, through the diverse nature of attendees at this Conference, to improve the understanding of the issues for those involved in providing and managing banknotes; coins and other secure documents and at the same time improving the understanding of the consumers' needs by the suppliers. The Conference has set out to achieve this with a mixture of presentations, workshops and panel discussions that touch on the latest developments and technologies in the industry and allow adequate time for discussion and dialogue. You are all encouraged to seek answers by asking questions and discussing the issues. The overall aim is to improve understanding through education – Africa has some catching-up to do, compared with the rest of the world. This is our attempt to start that ball rolling strongly in the field of banknotes, coins, ID and other security documents and to position this great continent as a producer, as well as a user of such products.

It is our sincere hope that you will gain in knowledge and establish contacts and relationships that will continue into the future; but most of all our hope is that you will enjoy having an enjoyable time.

Thank you