Ravi Menon: Three "C"s of a good payment instrument

Welcome address by Mr Ravi Menon, Managing Director of the Monetary Authority of Singapore (MAS), at the Currency Conference 2011, Singapore, 3 October 2011.

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Why cash is still king

Distinguished guests, ladies and gentlemen, good morning and a warm welcome to Singapore and the 2011 Currency Conference. Singapore is honoured and delighted to host this flagship event.

The late Mr John Shepherd-Barron, who pioneered in 1967 the development of the Automated Teller Machine, or ATM, said during a 2007 interview: "*Money costs money to transport. I am therefore predicting the demise of cash within three to five years.*"

Shepherd-Barron believed fervently that we would soon be swiping our mobile phones at till points, even for small transactions. We have indeed seen an increasing use of cashless payments at point-of-sale. Electronic payment alternatives have mushroomed in many countries, ranging from contactless stored value cards in Singapore to real-time settlement of electronic fund transfers in the United Kingdom.

But cash remains "king". Even in advanced economies. This is especially so for person-to-person transactions and micro-payments. Take high-tech Singapore. The use of electronic payments has proliferated rapidly in recent years. Yet, currency-in-circulation has been growing at an average 7 per cent per annum during the last ten years. This has reflected demand from a growing population and a growing economy.

Less well known is how the demand for cash globally is being driven by tourism. Tourists have a habit of taking back home unused currency – both notes and coins. This represents a leakage from circulation and needs to be replaced. We don't have good data on this. But take for example, Singapore. Last year, we received almost 12 million visitors. If everyone took 8 coins back with them, close to 100 million coins would have leaked out of the country. And it will cost MAS about S$10 million to replace them. That's why we have been working with the Singapore Mint, Changi Airport Group, and charity organisations to increase the availability of boxes in various parts of Changi Airport, for tourists to donate their excess notes and coins before they leave the country.

Physical cash commands a premium during times of uncertainty. We saw this during the 2008 global financial crisis. Within the first month of the collapse of Lehman Brothers, there was an exceptionally large withdrawal of high denomination notes by banks in Singapore. Typically, 90 per cent or more of the high-denomination notes withdrawn from banks are re-deposited within the month. During the initial months of the 2008 crisis, only 70 per cent of the $100, $1,000 and $10,000 notes withdrawn were returned.

This phenomenon is insightful. The safety and soundness of banks in Singapore was never in question, and the impact of the crisis on Singapore's financial system was minimal. But there was a discernible effect on consumer behaviour – people preferred to keep more cash in a climate of heightened uncertainty.

The bottom line? Reports of the demise of cash are vastly exaggerated. Notes and coins have been with us a long time, and have served a crucial role in the growth of the modern economy. I suspect they will be with us for quite some time more.

Three "C"s of a good payment instrument

But be it physical cash or electronic payment, the medium of exchange for transactions must satisfy three requirements. I will refer to these as the three "C"s of a preferred payment system – confidence, convenience, and cost-effectiveness.

First, *confidence*. Businesses and consumers must be assured of the security of payment instruments. The widespread circulation of counterfeit notes and coins can impair confidence in a country's currency. As John Maynard Keynes put it nearly a century ago, quoting Lenin, "*There is no subtler, no surer means of overturning the existing basis of society than to debauch the currency.*" Keynes was, of course, talking about the deleterious effects of inflation. But it applies just as well to debasing the currency through counterfeiting.

Ensuring the fidelity of notes and coins and the soundness of electronic payments is therefore a critical function. Central banks and currency issuing authorities must continually innovate and stay ahead of fraudsters. In electronic fund transfers, we have instituted more end-to-end security measures like two-factor authentication. Modern currency notes come with very advanced security features. I wanted to give some examples, but have been advised that it would be tantamount to giving away our secrets!

Confidence in a currency comes not only from its security but also its availability, especially during times of uncertainty. Central banks and financial institutions must have robust business continuity measures to ensure adequate supply of cash to meet surges in demand and the resilience of national payment systems.

The second "C" is *convenience*. Although cash is widely used and accepted in our society today, e-payment alternatives such as mobile payments and electronic wallets are gaining popularity. The "tap-and-go" feature of contactless cards is much in sync with the hurried lifestyles of today, hence the growing popularity of these cards.

Convenience is an important consideration in developments within the cashless space of payments. In 2008, for the first time, GIRO overtook cheques by volume of transactions in Singapore. In fact, GIRO itself – which is based on batch processing – will be eventually overtaken by straight-through, real-time payments systems.

The third "C" is *cost-effectiveness*. Handling cash is costly. According to a 2010 study by Retail Banking Research, the cost of distributing, managing, handling, processing and recycling cash in Europe is estimated at €84 billion. This is equal to 0.6 per cent of Europe's GDP.

How to reduce the cost of cash without compromising confidence and convenience? A number of countries are exploring alternative note substrates and coinage materials to increase their durability, quality, security, and cost effectiveness. Besides managing manufacturing costs, countries are looking at the end-to-end costs of currency distribution and collection. Some have outsourced their currency functions, while others have automated their currency facilities to improve efficiency in currency processing.

In Singapore, we began automating currency processing and warehousing operations in 2000. Today, Singapore has one of the few fully automated currency handling facilities in the world.

Conclusion

All of us gathered here share a common objective in establishing a secure, convenient, and cost-effective payment system. It is important for central banks and key industry players to engage one another and share best practices and lessons learnt.

The Currency Conference serves this purpose. We have a large turnout from some 75 countries. We have many excellent speakers, and a diverse cast of delegates. I hope all of us can benefit from the sharing of experiences and the networking opportunities provided by the Conference. I wish you all a successful and fruitful Conference; and to our guests from abroad, an enjoyable stay in Singapore.