

Tongurai Limpiti: Innovation and growth – finding the right balance

Speech by Ms Tongurai Limpiti, Deputy Governor of the Bank of Thailand, at the 3rd Thailand Financial Services Summit 2014 “Driving Growth through Innovation”, organized by IDC Financial Insights, Bangkok, 9 October 2014.

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Good morning. It is a pleasure to be with you today and I would like to thank the IDC Financial Insights for inviting me to deliver a keynote address today. The topic I cover today is “Innovation and Growth: Finding the Right Balance”, which is currently an interesting issue that we have to carefully watch.

What do we see when we think about innovation and growth? We see that the financial sector nowadays is highly competitive due to the number of players and the approach of regional economic integration. We see that digital economy is becoming a reality; thus, IT investment is one of the keys to success as it enables financial institutions to broaden business market and strengthen their internal operation. As a central banker, we encourage all financial institutions to improve their operational efficiency and capacity through innovation and IT investments in order to be strong domestically and to be able to compete internationally. Increasing operational efficiency has been a focus of Thailand’s Financial Sector Blueprint I and II and IT infrastructure development will play a crucial role in the next phase of Financial Blueprint. Regulators will have to be prepared for such a change in order to ensure sustainability and economic growth.

1. Balance between innovation & growth and security

Talking about balancing between innovation & growth and security, in the world of digitization, it is a challenge to find the right balance between innovation & growth and security which lie in our responsibilities. First of all, we have to understand the creation of the matters as well as their main drivers.

Innovation and growth result from consumer’s and business’s demands for variety, speed and lower cost that come with competitions to develop such technology facilitating financial transactions and creating sophisticated banking products. Seeing that, their main drivers are users’ demand for financial facilities and technology together with a need for proper uses of banking products and services, leading to security concerns, which have occurred in parallel with the innovation and growth.

Security of IT system uses are prioritized as one of the most considerable issues, due to its importance and interconnectedness, to accomplish our own goal of financial system stability that is at the heart of effective supervision. So, it is our responsibility to prevent such fragility before it is too late.

2. Regulatory schemes, bank business models and IT platform

In the world of highly competitive markets, in particular the banking sector, players have continuously tried to create new banking products to serve the needs of consumers and to move forward to penetrate market shares. As a result, sophisticated banking products along with adaptive bank business models have emerged.

Unfortunately, once regulators respond to the changes steps after, financial crisis comes. At the wake after 2008 global financial crisis, regulators actively strengthened regulatory frameworks by reforming agenda such as strengthen market infrastructure, effective supervision, resolution and addressing systemic important institutions.

From the banks’ point of view, the implementation of the new stronger regulations at the time of post-crisis has undoubtedly caused burdens to implementation. From the Centre for the

Study of Financial Innovation (CSFI) survey, it indicated that, “regulation” is the greatest threat to the banking industry (from the survey, it climbed up from no. 6 in 2012 to no. 1 this year). As banks have encountered the higher costs to run businesses, some may seek for less regulated sectors and some seek for changes in their business models to deal with such a situation. It might be implied here that regulation is the key influence to changes. Therefore, it illustrates the need to find the right balance. As a consequence, regulators have to respond to those changes, updating and revising their regulatory frameworks to be more advance to keep up with the business models; hence, the regulatory schemes run consistently with the shifts of bank business models.

3. The main drivers

i. Current innovation and growth of banking sector

What is the main driver? I would like to pinpoint here that current innovation and growth of banking sector is one of the main drivers. Even though many countries including Thailand have been affected by financial crises and regulatory reforms, we are currently in the stage of revival with high potential growth among ASEAN countries.

According to the IDC Financial Insights’ observation on key structural shifts, trends of financial institution sector are: *expansion of banking industry*, particularly, in South Asia and Southeast Asia due to an escalation of financial inclusion and new-entry of financial players; *technology refresh* to serve with more sophisticated financial products and services; and *regional integration (AEC) and the growth of Asian insurance business*. These are paths to higher competition among banks, in which, IT innovation is a key to distinguish each brand. Undoubtedly, banks and related parties invest more in IT projects to advance their services responding to digital era.

To be more specific, we have to admit that we live in the world of digitization with an escalation of Internet users and Y generation. Consequently, this group of people becomes a new targeted customer group for banks. Interests in higher conveniences of services which result from high integral digital environment and multi-task lifestyle of the people prompt banks to respond with “Virtual Banking Concept” – any interaction with a bank happens online instead of face-to-face meet up at a branch. To illustrate, the numbers of Internet and mobile banking users have grown up recently as well as volume and value of transactions via such systems. In Q2 this year, there are around 8.7 and 3.2 million agreements in Internet and mobile banking, respectively, of which 43 and 24 million transactions in volume that cost approximately 5,000 and 306 billion baths.

Some banks, therefore, strategically reduce the role of branches, intentionally pay attention to Virtual Banking Concept, to efficiently reciprocate the target customers and to facilitate international businesses that tend to grow due to trends of globalization and economic integrations.

The growth of IT investments and sophisticated products as well as advanced services in banking industry comes with a concern on “**security**”, which is the challenging key to propel the sustainability of such a growth. In our role as central bank, we put “security” as our first priority align with standard setting to promote advancement of banking services.

ii. The role of central bank (BOT)

What is our role? We have aimed at setting standards to create domestic and international banking networks as well as to promote banking and payment system stabilities by developing access to financial services including financial infrastructure for cross-border payment and IT systems or other innovations aligned with security.

In terms of cross-border innovation, the Bank of Thailand in association with the ASEAN central banks established the Working Committee on Payment and Settlement Systems:

WC-PSS in 2010 to study payment and settlement system environments in member countries and to present regional strategic plans in order to serve economic integration in 2015. WC-PSS created cross-border payment innovations: international stock markets network, electronic payment message standard, and ASEAN retail payment system network.

In addition, BOT in association with Hong Kong Monetary Authority (HKMA) launched a new cross-border payment-versus-payment (PvP) link between Hong Kong's USD CHATS, Hong Kong dollar Clearing House Automated Transfer System (CHATS) and Thai BAHTNET to ensure the simultaneous delivery of US Dollars in Hong Kong and Thai Baht in Thailand in order to eliminate or mitigate settlement and counterparty risks. The link operationally started since 28 July this year.

Aligning with cross-border payment innovations, growth of IT investment is another matter that the Bank of Thailand has promoted and monitored.

The widespread adoption of advanced technology in banks' key systems is to advance efficient internal operations – Big Data Analytics for processing customers' information to analyze customers' behavior and Cloud Computing for allocating IT resources, and to provide products and services through online platform such as Mobile Electronic Data Capture, Net Bank, Virtual Card, Near Field Communication Contactless, and etc. However, many people, especially in the baby boom ages, have not experienced the online banking services yet, partly because they have concerns about security. So it is our job to secure them.

BOT has continuously promoted online banking systems and are aware of their risks and impacts at the same time since we believe that no matter what we have in online mode, they are all connected.

As digital banking products thrive, so do the competency of cyber threats. In Banking Banana Survey this year indicated that technology risk rose from no. 18 in 2012 survey to no. 4 due to a high increase in the frequency and sophistication of cyber-attacks. Financial institutions have exposed to all risks of technology security: access risk, accuracy risk, availability risk, and agility risk.

Concerning the systemic risks, the Bank of Thailand as a regulator established the IT principle called "SIA", which stands for Security, Integrity and Availability that covers infrastructure protection at the prevention stage of both physical and logical controls: CCTV / access control; firewall, IDS / IPS, AntiVirus and password, respectively. In the arrangement of contingency plan, all systems will be tested or reviewed regularly. Furthermore, key risk indicators and risk tolerance will be closely monitored, and loss data collection will be reported to the board of directors and the Bank of Thailand. Lastly, the Bank of Thailand has to correct the IT contingency plan implementation. Additionally, market conduct will serve as an alignment to each stage to determine customer protection by sharing correct information and suggestions to customers; and by interacting with customers' complains.

As a central bank, we wish to support more on inter-operability for both wholesale and retail which is a part of standard setting I mentioned earlier: for example, standardized codes for all banks and real sector. In Thailand, we already have chip card and OTP token such as the rabbit card and SmartPurse, but what we really wish to see in the very near future is something more standardized and widely use like UK Oyster and Hong Kong Octopus. Above all, incentive enhancement for people to use such new banking products, services and systems is the most essential driver to extend the business advancement and that security is the key challenging solution.

4. Conclusion

Today's IT innovations have influenced our ways of living in many fields including banking industry and we all benefit from the new technologies; however, lessons learnt from past crises have taught and reminded all of us not to ignore what adverse effects might be

afterward. As a consequence, maintaining the right balance between banking innovation optimization and risk mitigation is the key in reciprocating the sustainability of growth. We should be more aware and prepared of any challenging IT innovations in order to prevent and mitigate such previous disasters we did encounter, and be more proactive in making policies and designing new models.

Ladies and gentlemen, I do believe that the **effective collaboration** between supervisors and financial institutions is necessary to encourage sustainable growth of Thai banking system against evolving threats. With that, this summit is another move for financial institutions and related organizations to share information and ideas; hence, I wish you all a productive and fruitful discussion today. Thank you.