Muhammad bin Ibrahim: Mobile payment – the next wave

Keynote address by Mr Muhammad bin Ibrahim, Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the Payment System Forum & Exhibition 2017 "Mobile Payment: The Next Wave", Kuala Lumpur, 8 December 2017.

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Welcome to the Payment System Forum & Exhibition 2017. This year's theme 'Mobile Payment: The Next Wave' is the continuation of our country's e-payment transformation that started seven years ago. In 2011, we launched the 10-year e-payment roadmap in the Financial Sector Blueprint 2011–2020. Various reform measures were instituted to remove pricing distortions, instill market incentives and induce competition to reduce costs in our effort to create a conducive environment to accelerate migration to e-payments.

These measures have been effective in reducing Malaysia's usage of cheques and fostering the adoption of e-payments. The total cheque volume has declined by 42% from 205 million cheques in 2011 to an estimated 120 million cheques in 2017.

Electronic fund transfers have increased from 66 million transactions in 2011 to an estimated 329 million transactions in 2017, surpassing the number of cheques issued by almost three times. At the current rate of decline, we are likely to achieve the Financial Sector Blueprint target of reducing cheque usage to 100 million in the year 2019, one year ahead of schedule.

Encouraging progress has also been made in the expansion of the point-of-sale (POS) terminal network. The reform measures in the Payment Card Reform Framework (PCRF) implemented since 2015 have enhanced transparency and competition, bringing about a continued decline in the average merchant discount rates (or MDR). Merchants have benefited from lower cost of accepting card payments, with an estimated cost savings of about RM422.4 million from 2015 to September this year. Consequently, the annual growth of POS terminals has more than doubled from about 6.8% for the period between 2011 and 2014, to 17% for the period between 2015 and 2017.

Key trends shaping our payment landscape today

Since the Payment Forum in 2015, many developments have taken place in the payment landscape both domestically and internationally.

Firstly, society has become increasingly digital and connected, driven by the Internet and mobile revolution. For a population of 32.1 million in Malaysia, there are 42.8 million mobile phone subscriptions while smartphone penetration stands at 70% and is increasing.

Secondly, payment technology has become more advanced, scalable and increasingly low-cost. For instance, innovations in the area of merchant acceptance has lowered the cost for merchants to embrace electronic payments through the use of Quick Response (QR) codes.

Likewise, the advancements in biometric and tokenisation technologies and the shift towards greater publication of Application Programming Interfaces have enhanced the ability of payment service providers to develop new use cases and deliver superior customer experience.

Thirdly, the market players in our payment landscape have become more abundant, diverse and increasingly non-traditional. In 2017 alone, Bank Negara Malaysia has processed applications from 43 new non-bank players, an increase of 91% compared to the past two years. This is in line with global developments where the size of the global payments industry has increased to account for 34 percent of overall banking revenues in 2016 and is projected to become a USD$2 trillion dollar industry by 2020. This is a significant turning point. In essence, the traditional payment channels are increasingly being replaced by nimble, innovative and lower cost alternatives.

We must embrace the next wave of technological and e-payment transformation. As a nation, we need to rise and seize this exciting opportunity, take a proactive rather than a reactive role, and benefit from the enormous opportunities brought about by technology to improve our payment system's security, efficiency, productivity. We need to bereft ourselves of the inertia to move forward with the times.

There are a few strategies we ought to adopt, to reduce further the wastage arising from the cost of maintaining two parallel systems by accelerating the displacement of cheques, harness the pervasiveness of mobile payments to ensure reach, and focus on solving the last mile obstacles to enhance migration to e-payments.

The enormous cost of maintaining two parallel systems

Cheque is a very costly payment instrument to process compared to electronic fund transfer. Our study shows that the unit cost for cheque processing by banks has increased from RM3 in 2011 to RM4 in 2016, and is estimated to be about RM6 by 2020. At around 120 million cheques currently, this translates into an enormous cost of around RM480 million, a sheer wastage to the economy.

It is also costly for businesses to handle cheques. We estimate an average processing cost of about RM6.80 per cheque due to expenses incurred on delivering, depositing, reconciling and handling of returned cheques. On the contrary, the cost of processing an Interbank GIRO and Instant Transfer (IBFT) are around 30 sen per transaction. Such unit cost is likely to decline further due to economies of scale as e-payment adoption gains further traction.

In Scandinavian countries, higher cost has been the one of the key factors that drove the cheque volume to a negligible level. Denmark, for example, turned off its interbank cheque clearing system on 1 January 2017 once cheque usage was widely displaced by electronic fund transfers and debit cards. In the case of Malaysia, we estimate that at the current rate of decline, it will take us about 27 years before cheques can be reduced to a negligible level of 0.1 per capita, with an estimated cost to the banking and business community of about RM12.9 billion. This is a huge amount of prodigality. By accelerating the pace of cheque decline, we can shorten the number of years needed to reduce cheque usage to a negligible level and derive greater cost savings for the country.

Harness the prevalence of mobile payments to expand reach

Most Malaysians are likely to carry both a debit card and mobile phones and there are 45.4 million debit cards and 42.8 million mobile phone subscriptions. For a population of 32.1 million this is considered high. We need to take advantage of this. In particular, for debit cards. We need to optimise the use of this medium.

In the case of debit cards, the Merchant Discount Rates are still very high despite the direct debiting of the users' account. Acquirers should reduce the rates further. There are certain segments of the merchant community that are cost-sensitive and may not be able to afford the MDR of card payments. In this regard, mobile payment has the potential to complement the debit card as a low-cost alternative to accepting cash. Mobile e-wallet is a strong alternative to debit cards as merchants can accept payment through a QR code.

The use of QR codes has enormous potential. Out of 24 million adults in Malaysia, there are only 12 million active online banking accounts. We estimate that there are about 10 million bank accountholders who are not using online services, while the remaining 2 million adults are likely to be unbanked. In this regard, I am encouraged by the fact that non-bank e-money issuers are targeting to increase their product penetration in these unserved segments since the banks are not servicing this particular segment. The QR code could be a catalyst to reach this group.

To encourage QR code payment, avoid market fragmentation and broaden financial inclusion, Bank Negara Malaysia has issued an Interoperable Credit Transfer Framework (ICTF) for consultation. The ICTF aims to connect both banks and eligible non-bank e-money issuers to ensure reachability of bank accounts and e-money accounts. For the first time in our history, customers of both banks and non-banks will soon be able to transfer funds across the network seamlessly by just referencing the mobile number and IC numbers of the recipients or scanning the QR code of the recipients.

In this regard, PayNet, the merged entity of MEPS and MyClear, as the operator of the country's shared payment infrastructure would provide open and fair access to its clearing system and other shared payment utilities to both banks and eligible non-bank e-money issuers. This would enhance the network multiplier effects and foster better allocation of industry resources, as market players would be able to compete based on value-added services rather than on the basis of infrastructure.

In addition, the Interoperable Credit Transfer Framework would level the playing field between banks and non-bank players, by subjecting them to risk management requirements that are proportionate to the nature, scale and complexity of their business activities. The framework would enhance consumer protection and confidence in the use credit transfer services.

Focus on solving the last mile obstacles to enhance migration to e-payments

To remain relevant, it is important for all stakeholders to step up their game to drive innovation and new use cases to accelerate the displacement of cash and cheques. PayNet, as the operator of shared payment infrastructure, will facilitate the pooling of resources to develop innovative use cases to meet the evolving needs of end-users. For this to happen, PayNet might need to establish an innovation lab and publish open APIs to leverage on the creativity, resourcefulness and innovativeness of the fintech community.

Banks and non-bank players should focus on solving last mile obstacles by alleviating the 'pain points' faced by consumers and businesses. Subject to the observance of data protection laws, market players should mine customers' data to develop innovative solutions and deliver superior customer experience. Customers can now look for digital solutions that enrich their quality of life. This may necessitate entities to forge strategic alliances to deliver innovative services leveraging on each other's competitive advantages.

Equally important, are efforts to enhance cyber security and promote greater public awareness of the security features and safety tips to mitigate fraud. Bank Negara Malaysia will work with the payment industry to take preemptive actions to protect the security of customer funds and financial market infrastructures.

Conclusion

In our quest to engage in the digital economy, migration to e-payments is a critical component. It will benefit Malaysia through greater efficiency and productivity, thereby enhancing our country's competitiveness. We have no choice but to improve the way we conduct our financial affairs. The banking system has allocated huge amount of resources. From 2009 to 2017, the industry has invested RM893 million to enhance the e-payment infrastructure. Moving forward, the industry will invest a further RM346 million to expand the POS terminal network and RM40 million to develop the Real-time Retail Payments Platform to spur the usage of mobile payments.

By the end of 2020, it is envisaged that individuals and businesses will be able to make and receive payments seamlessly via online banking, payment cards and mobile payments. There are no reasons whatsoever for us not to migrate from a costly and inefficient payment mechanism to a cheaper, safer and more efficient payment mode.

To reflect the higher cheque processing cost, hasten the migration away from cheques, and incentivise individuals and businesses to migrate to a lower cost of doing business, beginning 2 January 2021, the cheque fee will be increased from 50 sen to RM1.00 and gradually thereafter, to reflect the actual cost of cheque processing. However, users of financial services will continue to be given a choice of using cheques, if they prefer to use an expensive and inefficient option rather than a cheaper one.

To support businesses and individuals, over the next three years a few initiatives will be implemented. To drive the migration to e-payments during the transition period, the Instant Transfer fee of 50 sen would be waived for transactions up to RM5,000 per transaction made by individuals and SMEs effective 1 July 2018.

The e-Payment Incentive Fund (ePIF) will be enlarged with an additional contribution of RM198 million from financial institutions. The funds will be used to assist account holders to migrate efficiently to e-payments. Individuals and businesses are advised to take advantage of these incentives and engage their respective financial institutions.

In line with this year’s theme of ‘Mobile Payment: The Next Wave’, we have invited a total of 18 exhibitors comprising both banks and non-banks to showcase their new and innovative payment solutions. Do take the opportunity to visit the booths to gain further insights on how the solutions would benefit your business and cater to your payment needs. With this, I wish you a productive forum ahead.

Thank you.