

Muhammad bin Ibrahim: The resurgence of payments in a digital world

Keynote address by Mr Muhammad bin Ibrahim, Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the Malaysian E-Payments Excellence Awards (MEEA) 2018 "The resurgence of payments in a digital world", Kuala Lumpur, 11 April 2018.

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Thank you for inviting me to speak today. Ten years ago, the word “payments” was only heard in small and exclusive circles. Those in banking understand the importance and criticality of the payment system. Huge resources are devoted to this function. Understandably so. Payment services are the bread and butter of banking and the lubricant for the economy. It is at the heart of all economic activities. Its services are indispensable. Yet, only a few took an interest in payments, except maybe those in the financial services community.

Today, this situation has reversed. Payments is now at the top of everyone’s minds. Globalisation of the financial markets and the consequent flows of funds across borders necessitates modernisation and strengthening of the financial system. Huge investments are being put in place. Technological advancements accelerate this process.

Out of the \$27.4 billion raised globally for fintech funding in 2017, 30% of the funds went to payment companies. In the third and fourth quarter of last year, 4 out of the top 10 global fintech deals were for payment services.

A few factors have driven changes in the payments sphere; digitisation, competition and innovation. In Malaysia, the payment system has significantly transformed over the last 25 years.

The journey started many years ago in 1997, major changes to the payment landscape occurred with the consolidation of the three ATM networks in the country into MEPS. This initiative removed duplication and enhanced the network multiplier effects. In fact, Malaysia was among the first in the world to complete the migration to the more secure chip-based payment cards in 2005. To provide a roadmap for the development, in 2011, Bank Negara Malaysia developed a 10-year Financial Sector Blueprint which amongst others, outlined the initiative to displace paper-based payment instruments, namely cheques and cash, in favour of the more convenient and cost effective e-payment methods.

We now have PayNet, the domestic shared infrastructure at the heart of the country’s payment systems. We envision PayNet to be a catalyst, one that challenges the status quo to drive its diverse members to foster competition and innovation, develop cost effective solutions and advance financial inclusion through digital payments. We should expect PayNet to ensure that the payment infrastructure of this country will always be at the cutting edge of technology. This will enable the economy to innovate, be competitive and productive.

The results speak for themselves; we have made great strides. Payment card spending has increased by more than threefold since 2006 to RM176.9 billion in 2017. From 2011 to 2017, e-payments per capita have more than doubled to 111 transactions. In the same period, we have reduced cheque usage by more than 40% to 119 million cheques. We have almost doubled the number of point-of-sale (POS) terminals to over 407,000 units. Debit card transactions have also increased by more than six times to 162 million transactions in 2017. All these are achievements that we should be proud of as a collective industry.

The progress that we have achieved so far is only possible with the collective contribution of all in the industry. This annual award ceremony recognises the achievements of those who have contributed to the progress, modernisation and enhancement of our payment systems.

While we celebrate our achievements, we need to forge ahead with greater vigour and perseverance, especially to displace cash. Cash remains prevalent in most retail transactions in Malaysia. Managing cash is expensive. This is most evident among lower tier merchants, who continue to prefer transacting in cash. It is more costly to use cash, as you know, and much cheaper, efficient and secure to adopt e-payments. It is a cost effective solution that makes business sense. Based on a study by the Royal Bank of Scotland and Natwest in 2014, a customer who uses mobile and online banking instead of going to a physical bank branch stands to enjoy about 24 hours of time saved and about 10 kilometers of travelling distance saved per year. Most likely, if a similar study is conducted in Malaysia, the results would show bigger savings here, given the greater digital connectivity we have today.

Our efforts over the years have shown some encouraging developments. The aggregate data points that we are on the right track. The growth rate of cash in circulation (or better known as CIC) in Malaysia has been slowing down for three years in a row since 2015. Measured against GDP, CIC decreased albeit marginally for the first time last year since 2014.

With high penetration of debit cards and mobile devices, Malaysia is well-positioned to transition into a cashless society in the medium term. To continue our collective effort to ensure widespread adoption of e-payments becomes a reality, my remarks today will touch on the following perspectives; future proofing the Malaysian payment infrastructure, embracing digital disruption that will redefine the payment mechanism as we know it, and some thoughts on public engagement and consumer protection.

Future-proofing Malaysia's payments infrastructure

The use of big data will provide a competitive edge among payment service providers. Payment flows used to be an operational matter, but now have immense strategic value. It has to do with the enormous amount of data and information that the system collects on the payment habits of the public.

With data analytics, these data can provide deep insights on consumer and merchant behaviour, and even the economy at large. With this information in hand, there is also the enormous responsibility to ensure that it is not being abused and mishandled. The issue of data security, integrity and privacy relates to the issue of trust, which is crucial for the functioning of any financial system. Data security and confidentiality should be a priority for financial institutions. Continuous investments in people, system and process will assure customers that their financial affairs are kept secure and private.

New payment providers are also emerging. In the age of mobile apps, platform-based companies can overlay existing commercial networks with payment services. In China for instance, this has fuelled the meteoric rise of mobile payments.

Customer expectations are also changing. Whether hailing a taxi or having lunch, today's consumers want things almost instantaneously. They want it now and the same is being expected from the payment system.

The payments infrastructure must therefore keep pace with these developments and expectations. It needs to meet the customer's expectations and offer value-added services that enhances the customer's experience. In this regard, the merger between MyClear and MEPS to form PayNet last year is an important milestone. By realising the natural synergies and aligning industry resources, PayNet is well-positioned to drive the Malaysia's payment infrastructure to be future-proof.

We should be most excited about the upcoming Real-time Retail Payments Platform or RPP. The RPP will be a game-changer for the Malaysian payment landscape. It will allow Malaysians to make and receive payments conveniently using their IC, mobile and business registration

numbers or by scanning a common Quick Response (or better known as QR) code. We do not need to suffer the agony of remembering our account numbers ever again. The RPP will be facilitated by a National Addressing Database (NAD) and an interoperable QR code payment scheme. Seamless and secure payments between bank and non-bank e-money accounts will also become a reality.

Given the overwhelming benefits from this initiative, it is incumbent on all of us to drive the promotion of RPP, such as in facilitating user registration with the NAD and merchant adoption of the common QR code. Let us make the RPP services a household service and transform all mobile phones into mobile wallets. The RPP should not be merely a banking service, but a lifestyle solution.

The industry ought to build upon the RPP and enhance its research and development capabilities. One such area is through the publication of Open Application Programming Interfaces (or better known as Open APIs). Based on our interaction with the banking community, there is interest for this among our banks. The Bank's survey last year indicated that more than 50% of banks in Malaysia view Open API as a high priority. Thus, the industry should leverage on Open API to facilitate collaboration with fintech firms to introduce innovations and facilitate new use cases to enhance the RPP's value proposition to businesses and consumers.

Notably, the RPP can offer a treasure trove of data. This can be mined to develop more tailored payment solutions, fraud detection capabilities, and to support potential strategic partnerships with financial or non-financial players. But as I mentioned earlier, confidentiality and privacy should not be compromised.

Part of future-proofing our payment systems is to enhance the efficiency of cross-border payment services. In this globalised world, there is a growing demand for faster, reasonably priced and more transparent cross-border payments. This will become even more important as international trade and investment linkages deepen, such as through the growth of e-commerce.

Yet, cross-border payment services still pale in comparison to domestic payments, which are increasingly real time and zero cost. PayNet and the payment system operators in Indonesia, Singapore, Thailand and Vietnam have entered into a Memorandum of Understanding (MoU) to link their respective real-time payment systems. This will give rise to great opportunities for the region to forge closer economic and financial integration.

The industry should capitalise on such developments to enhance their cross-border payment offerings to better serve their customers, reduce costs and enhance safety. Harnessing greater efficiencies of cross-border payments can be a lucrative area and those who can innovate will certainly benefit most.

Embracing digital disruption that redefine payments

This brings me to my second point. Technology, as you know, is fundamentally changing the way we live. Many industries have redefined themselves and embraced digital disruption to remain relevant. Unlike previous disruptions that came from within the industry, we now see enormous interest in mobile payments and the proliferation of non-bank payment providers. Data collected showed an increase in the number of non-bank e-money issuers from 26 in 2016 to 41 as at the end of last month.

The Bank more than welcomes a more competitive payment landscape. We desire new entrants. We are not in the business of protecting the incumbents. We also do not pick winners and losers. The market will decide those who will prosper. Existing players were given this notice long time ago. Banks especially, will have to reinvent themselves or risk being disrupted. What matters most, from the public policy perspective, is that Malaysian businesses and consumers will benefit from a more vibrant, competitive and efficient ecosystem. We should expect

enhanced competition to spur innovation in the products and services that are being offered.

Globally, we have seen collaborative strategies emerging as a response to the changing market dynamics. From Scandinavia to Asia, banks in some countries are increasingly competing on a united front. This includes industry partnerships with the payment system operator and fintech firms. In these markets, collaboration on common mobile applications seeks to enable banks to develop more innovative use cases by leveraging on pooled R&D resources, and facilitate mass adoption through common awareness and promotion campaigns.

Collaborative efforts enable greater economies of scale through the pooling of resources. Establishing a common platform among banks defrays the cost of testing out new technologies and new ways of doing business. This can go a long way in fostering a culture of experimentation.

Collaborative strategies will enhance the probability of success. This is the essence of the merger between MEPS and MyClear. Maintaining the status quo is simply not an option.

To set things in motion, we introduced the Interoperable Credit Transfer Framework (ICTF) last month. Along with the RPP, the ICTF is also expected to be a game changer for Malaysia's payment landscape, particularly for mobile payments. For the first time in Malaysia and likely in the region, banks and non-banks will be connected on a single payment network.

This is a good example of a strategy of collaborative competition, or 'co-opetition. Payment providers collaborate at the infrastructure level via the shared payment infrastructure and compete on the service level. This expands network reach, lowers costs and avoids duplication of resources by the industry.

It also focuses competition at the product level. Looking ahead, we envisage industry players to develop more innovative value-added features to provide better service levels to consumers and merchants.

Another important area where innovation plays a prominent role, is to advance financial inclusion through digitalisation. Out of the Malaysian adult population of 24 million, we estimate that about 10 million do not use online banking, while 2 million remain unbanked.

We look to the industry, both banks and non-banks, to come up with new and imaginative ways to accelerate the onboarding of these underbanked and unbanked segments of our society. In supporting this, the transaction fee for instant transfer transactions up to RM5,000 will be waived effective 1 July 2018 for individuals and SMEs. Strategies beyond monetary incentives also need to be employed. For example, mobile payment applications should be convenient, fast, secure, simple and intuitive. With so many things competing for our attention these days, the design of customer experience is critical. Delivering a superior customer experience is a major source of competitive advantage.

Intensifying public engagement and consumer protection

Our migration to e-payments would not be successful without intense public engagement and consumer protection efforts. Firstly, much more needs to be done to promote debit card usage. The Bank has taken the lead by lowering the costs of debit card acceptance through the Payment Card Reform Framework (PCRF) in 2015. Consequently, Malaysia's debit card interchange fee rates are now among the lowest. They are up to 10 times lower than the rates in other regional economies.

The industry should take advantage of this. We need to educate merchants on the availability of a lower cost debit card network. To move this forward, PayNet will drive an industry wide awareness campaign. Merchants who cannot afford the cost of accepting the more expensive

credit card should opt to accept only debit cards. This would lessen the incentives for merchants to impose surcharges to recover their payment card acceptance cost which would ultimately benefit the consumer.

Secondly, good customer engagement through effective disclosures can be a source of competitive advantage. Payment providers should consider differentiating themselves by disclosing key security features and safeguards against fraud and malware threats. This would demonstrate how the customer's hard earned money and sensitive personal data are being protected.

Our regulatory focus going forward will take into account the potential for greater market transparency and competition. Market discipline will be strengthened. The regulatory framework will be improved to ensure that e-payment services remain secure and reliable. Regulators will not be the cause for bankers' inertia.

In the coming months, the Bank will introduce minimum standards for the nascent but growing area of mobile payments. Mobile payment providers will be required to disclose key security features of their services, such as in-app safeguards against malware and protection against unauthorised transactions. This will make it easier for consumers to compare between different providers, thereby promoting greater consumer empowerment to make better informed decisions.

Thirdly, enhancing customer awareness of basic safety tips is paramount as a first line of defence against payment fraud. This is particularly relevant for the emerging modus operandi of social engineering, where fraud victims are duped into disclosing confidential information that are used to commit fraud.

In this regard, the industry can do much more to educate consumers. Consumer education initiatives have to be more targeted. They should be designed to address specific modus operandi that are known to be prevalent or emerging. The messages should be simple and tailored to the diverse profile of payment users. This should also account for demographic, behavioural and psychological factors that may be at play.

Financial institutions must also regularly review and measure the effectiveness of consumer education initiatives. If the results are not satisfactory, then the strategy must be changed.

The Bank will continue to collaborate with the industry in the area of public education and awareness. The Bank will be working with both bank and non-bank players to develop common promotional messages that provide "do's and don'ts" for e-payment transactions. This will ensure a more cohesive communication strategy to amplify the impact on the public at large.

Concluding remarks

When I started, I highlighted the lack of public awareness on the payment system despite its importance as one of the key pillars of the financial services industry.

Times have changed. Widespread digitisation, disruptive technologies and heightened competition have reshaped and magnified the potential of payment services.

We should be bold in taking advantage of this great potential to deliver e-payments for all and realise the aspiration of making Malaysia a cashless society.

Before I close, I would like to congratulate the winners of today's ceremony. May our achievements today inspire even greater ones tomorrow.