

Nestor A Espenilla, Jr: Third pillar of central banking

Speech by Mr Nestor A Espenilla, Jr, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the "Providing a Safer, More Efficient, and More Inclusive Philippine Payments and Settlements System" Conference, Manila, 27 July 2018.

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Friends from the industry, media, fellow BSPers, subject matter experts, esteemed guests, ladies and gentlemen, good morning. The BSP is pleased to host this conference on "Providing a Safer, More Efficient, and More Inclusive Philippine Payments and Settlements System."

There are three pillars of Central Banking. Every BSPer knows this. The first pillar is price stability through the conduct of monetary policy. The second is financial stability through financial system supervision and regulation. The third is an efficient payments and settlements system through the issuance of currency, the operation of the real-time gross settlement system, and oversight over the payments system.

The spotlight is often on the first two pillars and we hail the policies and initiatives pursued to achieve them. The importance of the third pillar is often glossed over. The payments system is often compared to the plumbing system. Very important but not very exciting.

Lately though, this has been changing. And this change excites us for all the possibilities it brings! Developments are unfolding at a rapid pace and more and more digital payments systems and services are being introduced.

In the not-so-long-ago-early-1990s, settlement of interbank transactions was a manual system. Since 2002, the settlement of time-critical and large-value financial transactions has been handled by PhilPaSS, the country's very modern real-time gross settlement system when it was installed. In its first 5 years, PhilPaSS processed an average of 1,000 transactions daily, valued at Php35 billion per day. In the last 5 years, the daily average is at 6,000 transactions, valued at Php 1.4 trillion per day!

Today, we are in the process of upgrading PhilPaSS to replace the system implemented almost 16 years ago. This will further enhance the safety, efficiency, and resiliency of the country's settlement system. At the same time, we are migrating the communication and messaging systems of the infrastructure to the global standard ISO 20022. This shall prepare our payment and settlement system to be regionally and globally interoperable.

Indeed, a safe and efficient payment system is a critical market infrastructure of a stable financial system. The payment system not only provides channels for funds to be transferred among banks and other institutions. It also functions as an essential tool for the effective implementation of monetary policy. It plays a pivotal role in the smooth functioning of money and capital markets. But it is no longer simply the large value payment system – those that has long been recognized as systemically important – that are getting the attention of regulators and policy makers globally. Retail payments are increasingly becoming an important piece of the overall infrastructure that rightly warrants our developmental focus.

An efficient retail payment system has the potential to transform the economy through the efficiency it brings to business transactions and the savings generated from a shift from paper-based to digital instruments. It benefits the consumers and businesses in terms of the affordability, convenience and speed of payment services – the most basic and most used financial service. This is financial inclusion.

Given these, the BSP is giving the payment and settlement system the attention it deserves. We recognize that having an efficient payment system is not just about operating infrastructure, but

also providing an enabling regulatory environment that promotes interoperability, efficiency, and consumer protection.

On December 9, 2015, the framework for the National Retail Payment System (NRPS) to create a safe, efficient, affordable, and interoperable electronic retail payment system was launched. Ultimately, the goal is to increase retail electronic payment transactions to twenty percent (20%) by 2020 and improve the country's economic competitiveness.

Realization of this goal requires an enormous collaborative effort among various stakeholders. We have achieved significant progress to date. Two automated Clearing Houses (ACH) – PESONet and INSTAPAY were introduced last November 8, 2017 and April 23, 2018, respectively. Both ACHs provide digital payment solutions to the current payment challenges encountered by government, businesses and ordinary consumers.

We have also issued various operating guidelines that promote level playing field and greater participation of smaller players without compromising safety. Our current efforts include the development of a national QR code standard to prevent the proliferation of closed loop infrastructures and instead promote interoperability of systems, domestically and even regionally.

On the legislative side, we are pursuing measures to support reforms in the payments landscape through the enactment of the Payment Systems Act which provides for the clear mandate of the BSP for the regulation and oversight of the payment system.

In order for the financial system to reach everywhere even to the remotest access points, we encourage increased use of affordable digital channels for payments, remittances and fund transfers. Our regulations allow banks to prudently service even low-income clients by allowing the participation of convenient, familiar and non-intimidating third party entities like grocery stores, pharmacies and other retail outlets as cash agents.

Money service businesses and remittance agents are also now covered by enhanced regulations for anti-money laundering, risk management and consumer protection.

We recognize that with digital developments, technology-related risks have and are increasing. In 2017, the BSP issued various prudential guidelines enhancing information security management, as well as anti-money laundering/combatting the financing of terrorism (AML/CFT) concerns related with the use of fintech. We continue to pursue policy and supervisory enhancements relevant to cybersecurity.

Even as we provide an enabling environment for technological innovations in the payments system, the BSP likewise is internally undergoing transformation by digitalizing its own payments processes and upgrading its organizational resources and capabilities. Recently, a unit dedicated to studying cybersecurity threats was established in the BSP. We are also strengthening the skills, proficiency and capability of IT specialists. Moreover, a new subsector within the Financial Supervision Sector (FSS) has been created to conduct the effective oversight of fintech and other innovative alternatives.

We are indeed putting more focus on our third mandate. And part of the journey is promoting awareness and exchanging knowledge about the country's payment and settlement system.

Ladies and gentlemen, in today's conference, there will be discussions on the Philippine retail payments industry, on the large-value payments and settlement system, on the oversight framework, and the value of measuring cybersecurity risks. These are very relevant issues and from whichever point of view you stand, whether you are from the policy group, whether you are operators of FMs, or come from support departments... as members of the ever increasingly interconnected financial ecosystem, it is urgent that we know and understand the developments in the industry.

We hope you would take advantage of this time to ask questions and learn from our subject matter experts who have very willingly agreed to be here for us. It is through opportunities such as this that we can enhance our roles in building a more efficient, safe, and inclusive national payment system.

Thank you and I wish everyone a good and productive day.