PAYMENTS INDUSTRY INTELLIGENCE

Payments
CARDS & MOBILE

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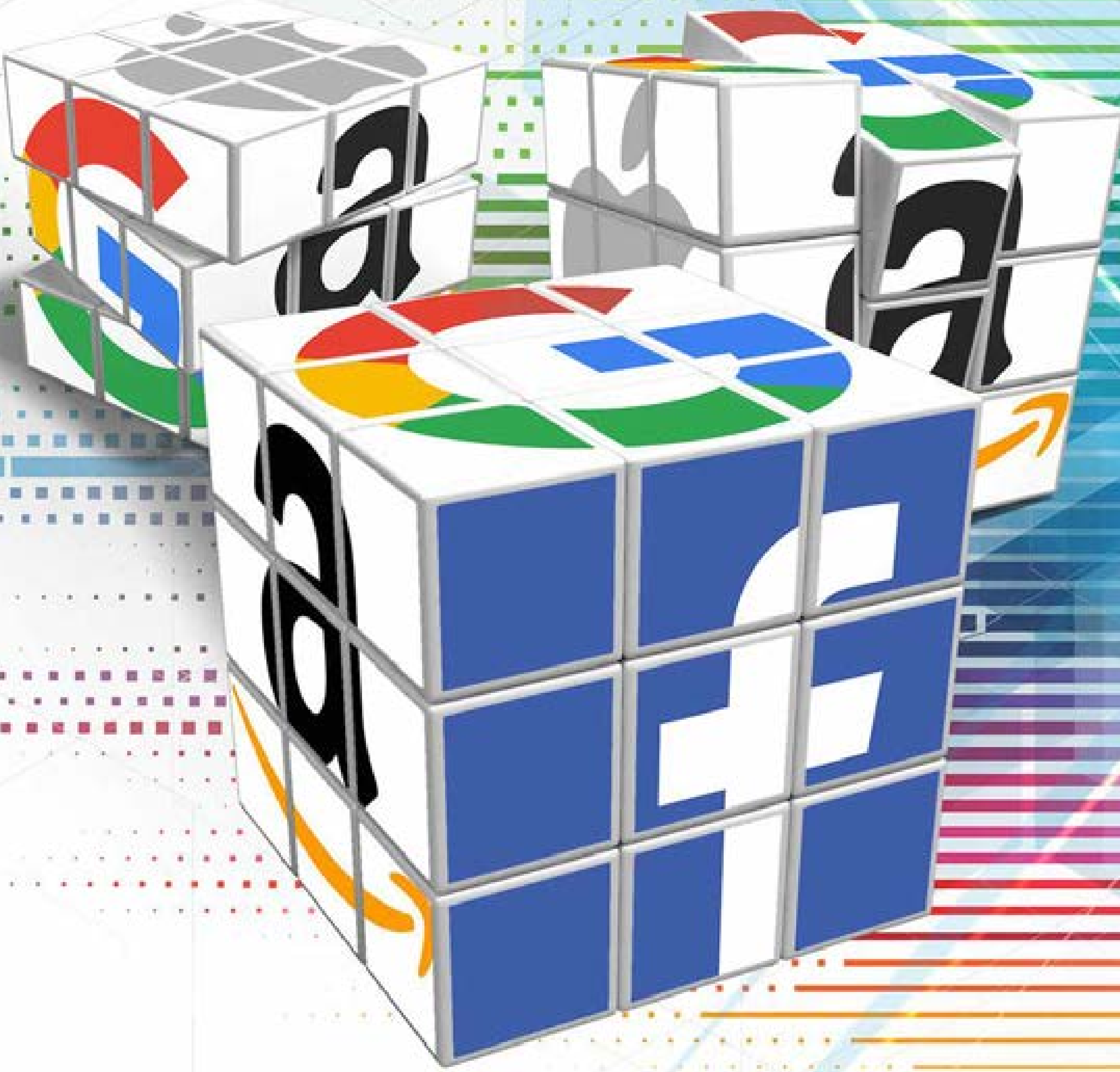
25 YEARS



COVER FEATURE

BIG TECH AND PAYMENTS

NATIONAL PAYMENTS INFRASTRUCTURES

by James Wood, PCM Editor

Growing numbers of countries are rebuilding their national payments infrastructures (NPI), including the UK, Australia, India, Canada and Singapore. PCM Editor James Wood looks at what's gone right and wrong, the pitfalls and expected benefits, and the role of the private sector in these changes.

"If it ain't broke, don't fix it" is not a maxim that works well in payments: fast-changing technologies, new payments methods and the ever-present threat of fraud all make for an environment in which no-one can afford to stand still – least of all countries seeking to create modern, dynamic economies. Making upgrades to a nation's payments infrastructure sends a positive signal to international investors, and can have economic benefits such as speeding up the rate at which money flows in an economy and enhancing economic growth.

That's why many countries have been looking at their payments infrastructure. It has to be said right away that some of these upgrades are badly needed, with various markets either not having an infrastructure or employing systems that are so out of date as to be at serious risk of collapse.

The State of Play

Recognising the benefits of a coherent approach, some states have already delivered new NPIs in partnership with the private sector. Although some of these initiatives are claiming major economic benefits, they have not been without their teething problems.

Take India's Unified Payments Interface, or UPI. Created in 2008 as part of the Indian government's demonetisation initiative by the National Payments Corporation of India and regulated by India's Reserve Bank, the system offers instananeous transfers between bank accounts via mobile devices. Consumers can undertake mobile P2P transactions using UPI, and to numbered bank accounts either via QR code or using India's Aadhaar, a personal digital indentification system run by the state.

India's UPI has engaged more than ten banks, including HSBC and Citibank, as what it terms "Payment Service Providers" – or providers of the accounts on which UPI is run. The UPI system should be seen in the context of other state-sponsored electronic payments initiatives, including Bharat BillPay, for utilities payments, and the Immediate Payments Service, or IPS, for real-time interbank transfers. Taken together, these initiatives constitute a real attempt to create new platforms for the country in the digital economy.

Although most commentators would count India's UPI as a success, there have been problems – including serial data breaches by hackers that have rendered the system unuseable. These breaches have typically occurred in other state-sponsored organisations, such as Aadhaar, and have disabled UPI for significant periods of time. Another problem with UPI, not unrelated to the data breaches, has been the superior performance of private sector companies that do more or less the same things, such as PayTM. Launched in the same year as the UPI, PayTM offers an online marketplace, utilities payments, P2P money transfers and other services, including a bank – without the cost to taxpayers or the data breaches suffered by UPI.

India's UPI experience raises the question of what a national payments infrastructure is for, especially if private sector actors are able to perform the same roles more effectively and at lower cost. Aniruddha Makeshwari, Payments Consultant at Icon Solutions, agrees: "There needs to be a business case for these developments in national infrastructure. For India, the NPI has brought a largely unbanked population into financial services by using rails developed for cellular communications." However, Makeshwari admits the UPI has seen "a slow build up" and cites the importance of understanding the market's appetite for changes to infrastructure as critical to success.

Rising up down under

Australia appears to have taken industry consultation to unprecedented levels in the creation of its National Payments Platform (NPP), launched in February 2017. Working with 13 financial institutions, Australia's NPP has created a platform for real-time payments between banks and individuals which has processed 90 million transactions worth AUD 75 billion in its first year. More than 2.5 million Australians, or just over 10 percent of the population, have registered for online PayIDs, and the first commercial product to use NPP rails, Osko, has been launched, offering person-to-person real-time money transfers via text messaging apps. Furthermore, the NPP has created a regulatory sandbox and opened its APIs to developers, allowing the private sector the chance to participate in creating a new generation of payments products using NPP's rails and the international ISO20022 data standard.

Despite this level of planning, there have been complaints about the slow take-up of PayIDs by individual Australians, something NPP lays at the door of private-sector banks for not encouraging consumer adoption. According to Mark Flamme, Managing Director at AlixPartners management consultants, creating a flexible regulatory framework and engaging the private sector are key – "A government's regulatory oversight should encourage innovation, including changes to regulation where appropriate, such as special payments licenses. Governments should also create national faster payments networks to run these innovative products, and the private sector can then partner with government to develop and launch solutions relevant to each market." In both Australia and India, there appears to have been some disconnects between the private and public sectors – something countries now looking at their own infrastructures would do well to consider.

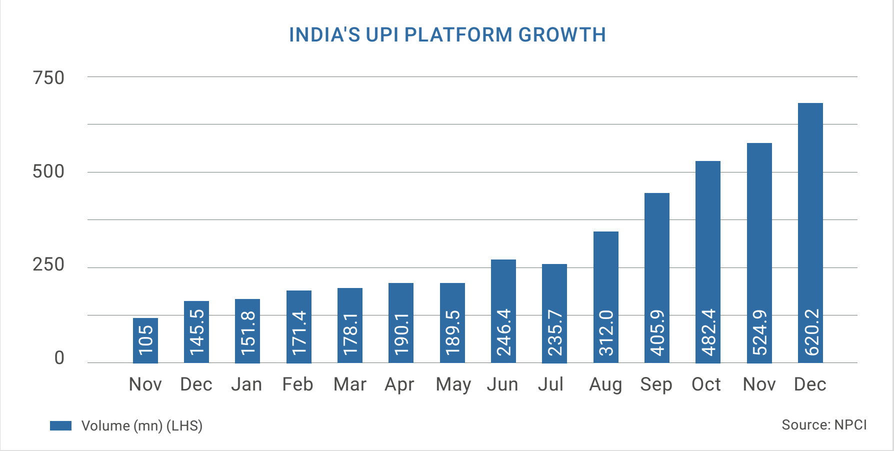
Singa Roars Ahead

If India and China demonstrate the need to forge strong partnerships between the public and private sectors, then Singapore seems to have taken this lesson to heart. Always one of Asia's most developed economies, with a 96 percent banked population and an average of two mobile devices per person, Singapore has partnered with KPMG since 2016 on the roll-out of a new payments infrastructure.

KPMG's original report to the Monetary Authority of Singapore (MAS) recommended strengthening regulation around consumer protection, supporting the FAST system for faster payments, and enabling easier direct-to-account payments and bill collections direct from account. Curiously, KPMG's strategy does not mention digital and mobile payments. However, such payments are projected to grow by 16 percent each year to 2023, accounting for more than US$19.2 billion in that year. It's as if the MAS and KPMG have identified a clear role for government, and left business development to the private sector as far as possible – an approach worthy of consideration by similar markets around the world.

The Shape of Things to Come

Canada and the UK are both currently planning overhauls of their national payments systems. Pay.UK, an organisation set up by the British Government, claims to have engaged with 2,500 individuals and organisations in the development of the New Payments Architecture (NPA), which it describes as "a new conceptual model for the future development of UK retail payments." The idea behind the NPA is to merge existing infrastructures for BACS, Faster Payments and Cheques into one entity, removing barriers to progress such as the three-day clearing period for BACS transactions. This infrastructure, which will be responsible for processing more than £7 trillion of transactions, is forecast for implementation after 2021 and is intended as the first phase of a multi-stage approach. In a statement to *PCM*, Pay.UK said that it expects future phases to "unlock new



business opportunities in everything from new uses of payment data to new transactional services."

Canada, long seen as a laggard in banking infrastructure, also has ambitious plans under its Modernisation Programme to deliver Faster Payments (FP) and a version of Open Banking conforming to the ISO20022 data standard. Acknowledging the country's somewhat mixed reputation, Payments Canada's Executive Director for Modernisation, Tracy Black, said in an interview with *PCM* that there is a "huge opportunity for customer experience improvement, and our mission is to deliver the infrastructure that enables this improvement." Following a "visioning exercise" undertaken in partnership with the private sector and including the views of government, consumers and businesses, Payments Canada published its modernisation roadmap in December last year. Elements of Canada's planned new infrastructure will include a new High-Value Payments System for interbank transfers called Lynx, a new rail to enable Real-Time Payments (RTP) for both consumers and businesses, and a Retail Batch Payments system which lets businesses move funds more frequently and benefit from same-day transaction settlement.

Absent Friends …

Canada's southern neighbour appears conspicuous in not having announced any plans for an infrastructure upgrade, despite being the world's largest economy. It's possible that the US considers the private sector best placed to manage any banking infrastructure challenges the country faces – or equally possible that the country is laying itself open to future difficulties, including fraud migration, by not planning properly for coming developments such as Open Banking or adhering to international standards such as ISO20022. In levelling this criticism, it's important to record that US banks have partnered with the Federal Reserve to launch the US Faster Payments Council in December 2018 with the mission to enable Americans "to pay safely and securely at any time."

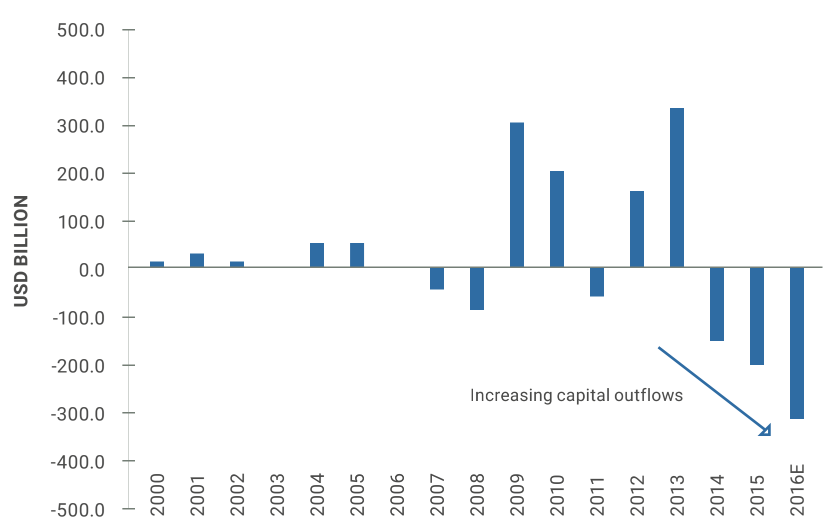
Likewise, as the world's second-largest economy and a country famous for its regimental economic planning, China appears to lack a coherent approach to the future development of national payments infrastructure – although the People's Bank of China (PBOC) underwent a major modernisation programme between 2005 and 2015, introducing cheque imaging, internet payments, foreign currency processing and a successful High-Value Payments System (HVPS). Despite these successes, the rapid proliferation of reliable private-sector P2P apps such as AliPay and WeChat has seen some businesses turn to these systems for their business banking needs, frustrated by slow settlement times and the regulatory complexity of "official" payments systems. The same is true of foreign transaction settlement, where private companies have been able to deliver clearing and settlement between Yuan and other currencies more rapidly than state actors. Both of these systems have been implicated in aiding capital flight from China through fake invoicing: the Chinese government is desperate to control uncontrolled capital outflows, which amounted to more than US$ 500 billion in 2016 alone, according to research from BNP Paribas.

Those in Payments Peril

Both the US and China demonstrate the potential risks of not having an NPI – in the case of the US, the private sector is acting only where it sees a need, rather than in the longer-term national interest. China shows how a state risks losing regulatory oversight in financial services when the private sector is able to perform certain functions more effectively without state engagement. The answer does seem to be partnership – although India and Australia's experiences demonstrate even this approach is not without its pitfalls.

The lack of coherent national approaches from poorer and developing nations may be of greatest concern for our collective future. The US and China can make the case that their economic success proves they don't require an NPI. But what of those countries, especially in Sub-Saharan Africa, with large unbanked and cash-only economies, which would clearly benefit from new payments infrastructure? The World Economic Forum and Norwegian Government are hosting a symposium in Oslo next month to address this issue, including the proposal to send fintech entrepreneurs to Zimbabwe and Uganda to see how the infrastructure of these countries could be improved. Without further action, the gulf between the developed and developing worlds – with all the attendant risks of fraud and financial crime being exported from those markets to leading economies – could be about to get worse. National Payments Infrastructures are useful, and the whole world needs them, however hard they are to develop and implement.

CHINA'S NON-FDI FLOWS*



*change in FX reserves - current account balance - net FDI flows, adjusted for FX valuation effect

Source: CEIC, BNPP IP (Asia)