"Developing a Safe and Secure Electronic Payment Ecosystem to Promote Financial Inclusion"
Speech by Deputy Governor Muhammad bin Ibrahim

Ladies and gentlemen, it is my pleasure to be here today to deliver the Keynote Speech for MasterCard's Regulatory Forum for the Asia Pacific region with the theme "Developing a Safe and Secure Electronic Payment Ecosystem to Promote Financial Inclusion".

With 2.5 billion people across the world still unbanked, financial inclusion is a significant global agenda to ensure that all segments of the society, including the most vulnerable groups, have access and usage of quality and affordable financial services.

This forum, which brings together regulators, international financial institutions and other payment system stakeholders, is an important platform to surface and exchange ideas on emerging trends, risks and opportunities in the use of cost-effective electronic payment system to drive financial inclusion.

Over the years, Bank Negara Malaysia has taken many measures in promoting financial inclusion and in accelerating the country's migration to electronic payments (e-payments). I will share some of my thoughts on the key areas in the payment value chain that could drive and expand the financial inclusion agenda via e-payments.

Measures taken by Bank Negara Malaysia to promote financial inclusion

Since its inception in 1959, getting the public to have access to financial services has always been a focus area for Bank Negara Malaysia. In the Central Bank of Malaysia Act 2009, financial inclusion has also been legislated as one of Bank Negara Malaysia's primary functions. Bank Negara Malaysia has designed the development of a diversified financial system which meets the needs of various consumers and businesses.

Many efforts were implemented. For example, to facilitate ease of access to bank accounts, Bank Negara Malaysia has introduced basic banking service, a no frills and low cost savings account. On the financing side, the *Pembiayaan Mikro* framework was established in 2006 to facilitate the provision of uncollateralised micro financing by financial institutions in a fast, easy and convenient manner.

The Central Bank has also focused on strengthening the enabling infrastructure through the establishment of the Credit Guarantee Corporation (CGC) to provide credit guarantees to enable SMEs with limited collateral and track record to have access to financing. Since its establishment in 1972, CGC has assisted more than 417,000 SMEs to obtain financing amounting to about RM50 billion.

To facilitate financial institutions in their lending decisions, the Central Credit Reference Information System (CCRIS) and the Credit Bureau Malaysia were also established to gather credit history from borrowers within and beyond the regulated financial sector, respectively. To date, CCRIS has a database of 9 million users covering approximately 53% of the adult population while the Credit Bureau Malaysia has over 28,000 registered members and generated more than 1.4 million credit reports.

To empower consumers to make well-informed financial decisions, Bank Negara Malaysia has also established financial advisory centres and contact points such as the Credit Counselling and Debt Management Agency and BNMLINK. Since its inception in 2006, AKPK has provided financial education to the public, benefiting more than 260,000 people nationwide.

To provide financial knowledge to the young, financial education elements are now incorporated as part of the syllabus for primary schools and will be extended to secondary schools by 2017. Consumer education efforts in Malaysia are also reinforced by a holistic consumer protection framework to ensure financial institutions practise responsible financing, conduct effective product transparency and disclosure, as well as, appropriate debt collection practices.

These measures have produced positive outcomes. As a result, 92% of adults (aged 15 and above) in Malaysia have access to a deposit account and basic banking services. Malaysia has also been ranked first for 6 consecutive years since 2007 for “Getting Credit” in the “Ease of Doing Business” index by the World Bank.

Accelerating the migration to e-payments as a key enabler for financial inclusion

The success of any financial inclusion tool or policy would depend largely on the presence of a reliable, efficient and safe payment system. In this regard, with the advancement and the willingness of the general public to experiment with new technology, the electronic payment system possesses distinct advantages over the traditional paper-based payment system.

While the unbanked and the underbanked may have limited access to financial services due to geographical limitations and cost considerations, the usage of e-payments by the underserved via mobile technology could help transcend these obstacles by delivering financial services efficiently, securely and at a lower cost compared to the traditional brick and mortar branches.

Accelerating the migration to e-payments remains a primary agenda for the country. In carrying our mandate to foster a safe, efficient and reliable payment system in Malaysia, a clear roadmap has been formulated to drive the country's migration to e-payments.

As provided in the Central Bank's Financial Sector Blueprint (2011 to 2020), specific targets have been set to reduce the number of cheques processed per annum from 207 million in 2010 to 100 million by 2020 and to increase the number of point-of-sale (POS) terminals from 7 per thousand inhabitants in 2010 to 25 per thousand inhabitants by 2020. At the same time, targets are also set to increase the per capita e-payment transactions from 43 in 2010 to 200 by 2020 and the per capita debit card transactions from 0.6 in 2010 to 30 by 2020.

Continuous infrastructure investments in this country have provided the enabling infrastructure which can be leveraged to serve the needs of the unbanked and the underbanked. Malaysia has a high mobile phone penetration of 144 per 100 inhabitants as at end-2013. In addition, the country's broadband penetration at 67 per 100 households as at end-2013, is projected to increase with the implementation of the second phase High-Speed Broadband (HSBB) project.

Malaysia also has a wide network of about 9,000 access points to banking services comprising bank branches and agent banking network accounting for approximately 4 access point per 10,000 adults.[1] Under the agent banking network, basic banking services are provided to customers through third party agents such as post offices, petrol stations, retail outlets and telecommunication agents. The access points are also complemented by 12,430 ATMs nationwide which represents about 6 ATMs per 10,000 adults. All districts and Parliamentary constituencies now have access to basic banking services[2].

We believe that the payment instrument that has the highest potential to drive financial inclusion in Malaysia is the debit card. Malaysia has a high debit card penetration of 19.2 million 'active'[3] cards-in-circulation which is almost equal to the bankable population of approximately 20.4

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[1] As at end-May 2014, there are 2,953 bank branches and 5,802 agents under the agent banking network nationwide.
[2] The total sub-districts served have increased to 92.5% while the total State Legislative Assembly districts served has increased to 99.8%.
[3] With at least 1 transaction per month

million adults. The unbanked on the other hand can leverage on prepaid cards which function just like debit cards.

While the number of POS terminals in Malaysia at about 9 per thousand inhabitants is still relatively low compared to about 22 to 33 per thousand inhabitants in other advanced countries[4], the POS network is anticipated to grow with the introduction of the Payment Card Reform framework.

Key focus areas to drive financial inclusion via e-payments

While there are success stories globally where e-payments have helped advance financial inclusion, such success stories must be the norm rather than an exception. In this respect, the public and private sector collaboration goes to the heart of any successful policy and developmental agenda. We also need to take a longer term view rather than focusing on short term and narrow self-interests. In this regard, I wish to highlight four (4) areas that could drive financial inclusion to the next level, via the use of e-payments. These areas are:

(1) Correcting price distortions and promoting competition;
(2) Development and sharing of infrastructure investments;
(3) Strengthening transaction security; and
(4) Consumer protection and education.

1. Correcting price distortions and promoting competition

We need to address price distortions and promote competitive practices. A market driven environment would ensure that the correct price signals

[4] Australia, the United Kingdom and Norway

are provided to promote the usage of the more cost-effective payment instruments whilst injecting competition.

The idea is for market players to lower cost and widen the access channels to make financial services more affordable and accessible to the general public. A monopolistic market would result in less innovative products and higher cost over the long term.

In Malaysia, the presence of price distortion had caused e-payments to be costlier than paper-based instruments, thus making it less affordable to the masses. For instance, e-payment services such as Interbank GIRO (IBG) used to be priced above cost at RM2 per transaction. Cheque, which costs RM3 to process however, was not directly priced except for the stamp duty of 15 sen.

To correct the price distortion, Bank Negara Malaysia had introduced a Pricing Reform framework where the price of IBG and cheques are aligned closer to their cost of production. At the same time, the public are provided with an alternative e-payment option which is cheaper and more efficient. To ensure that adequate e-payment services are provided, Bank Negara Malaysia will collaborate with the industry to establish a market-driven incentive framework to drive expansion in the various delivery channels.

Since the commencement of the Pricing Reform framework, we have seen significant improvements. IBG transaction volume grew at a higher rate of 45.6% on a year-on-year basis for the first half of 2014 compared to 12.4% for the same period last year. Likewise, cheques declined at a faster pace of 9.8% or 10 million cheques for the first half of 2014 compared to 2% or 2 million cheques for the same period last year. While the data suggests some improvements, more need to be done.

A particular area that requires huge efforts is the distortions in the debit card usage in Malaysia. Despite a seemingly high debit card penetration of about 19.2 million ‘active’ debit cards in contrast with 5.5 million ‘active’ credit cards, the per capita debit card transaction is only 1.7 compared to 11.3 for credit card in 2013, indicating a ratio of 1 debit card transaction to about 6 credit card transactions.

Acquirers charge merchants the same merchant discount rate (MDR) for the acceptance of debit and credit cards despite their differing cost structure, which makes debit cards just as expensive as credit cards. It is difficult to comprehend the charges imposed on debit cards, which have ready cash in them, is similar to the charges on credit cards. There has also been a slowdown in the growth rate of POS terminals in Malaysia since 2012, which indicates a potential saturation of POS terminals at those merchants who can afford the MDR.

This is further compounded by increases in interchange fees which are likely to cause the MDR to be raised to even higher levels on a system-wide basis, thus hindering the wider expansion of the POS network and depriving society from the convenience of using cost-effective payment cards.

The debit card should be positioned as a cost-effective payment card to make it more affordable for small merchants to accept card payments. The expansion of the POS network would allow for wider acceptance of the debit card to be used more pervasively, to displace the use of cash, thus bringing about cost savings for the country in the long run.

To correct the distortions and promote competition in the domestic payment card market, a Payment Card Reform is certainly timely to stem the indiscriminate increases in interchange fees and correct the price signals with the view to widen the POS network especially in non-traditional industries and rural areas.

2. Development and sharing of infrastructure investment

To be successful, e-payment solutions must not only be affordable, their expansion must also be sustainable in the long term. Sustainability entails the ability to leverage on an enlarged network which enables market players to build critical mass and achieve the desired economies of scale.

In this regard, the importance of collective industry efforts to develop and share infrastructure cannot be emphasised enough. Infrastructure development is very expensive and the banking industry ought to share the required investments. Infrastructure should not be used as a competitive tool but rather as an enabler that would promote modernisation of the payment system.

Besides minimising cost and lowering the entry barrier for new players, collective infrastructure development and sharing of infrastructure costs would allow market players to compete directly on product offerings and quality of services, thus providing better value to consumers. While regulators can act as the catalyst in prescribing interoperability standards and garnering industry efforts to facilitate infrastructure development and sharing of infrastructure costs, the industry must also play its role by adopting new standards quickly.

In Malaysia, there is currently an industry initiative to migrate the ATM cards to the EMV standard with the objective to widen the acceptance of the ATM cards for retail payments. There is also an on-going project to establish the National Bill Payments Scheme (NBPS), a common bill payment platform where billers only need to connect to one bank in order to receive payments from customers across all banks. All these efforts are intended to make e-payments for the public seamless and reduce duplication of resources in infrastructure investment.

3. Strengthening transaction security

Let me now turn to the third focus area which is the importance of strengthening transaction security to minimise fraud and instil greater confidence in the use of e-payments. Fraud and risk management measures must not only be effective, it must also be proportionate to the level of risk. Otherwise, it may be too costly to implement or too cumbersome to use, and people might revert to using cash. Equally important is the presence of effective payment system rules so that all parties in the payment value chain are held accountable for ensuring a minimal standard of security and service level.

It is of paramount importance to sustain consumers' perception and confidence in the safety of payment instruments. Malaysia is the first country in the Asia Pacific region to migrate from magnetic strip cards to chip-based payment cards. This transition, which was completed in 2005 despite the initial resistance by the industry, had successfully eradicated cases of fraudulent skimming or counterfeiting of payment cards. The investment cost of RM200 million was recovered within two and a half years from fraud avoidance. I think it is important for the banking industry to take note of this fact.

The various regulatory measures introduced by Bank Negara Malaysia and the continuous investment made by the industry have caused the cases of fraud incidents in e-payments to remain at a very low level over the last decade. In 2013, fraud incidents only accounted for 0.0054% of total transaction volume and 0.0011% of the transaction value of e-payment transactions. While we should be satisfied with such encouraging outcomes, there is no room for complacency as fraudsters are always on the look-out for possible weaknesses to exploit. Therefore, continuous efforts need to be taken both at the policy-making and at the industry level to continuously identify, remedy and tackle emerging security risks.

4. Consumer protection and education

The unbanked and the underbanked might find e-payments to be too sophisticated and lack the personal touch. In this respect, policymakers and market players have an important role to play in educating and creating awareness among consumers on the benefits of e-payments and the security steps that they can take to minimise fraud incidents. Such efforts would be effective when complemented with a consumer protection framework and product disclosure requirements that would instil user confidence and acceptance.

Bank Negara Malaysia constantly collaborates with the industry to conduct roadshows, payment system forums and other outreach programs to educate the public of the benefits and security of e-payment transactions. Apart from issuing requirements on consumer protection and product disclosure, an important milestone was achieved last year where protecting the rights and interests of consumers of financial services and products has been enshrined as one of regulatory objectives that Bank Negara Malaysia shall strive for in the Financial Services Act 2013 and the Islamic Financial Services Act 2013.

Conclusion

Ladies and gentlemen, we are now living in an exciting time with rapid technological advances in e-payments which, if harnessed well, would serve to drive financial inclusion in a major way.

To be successful in an increasingly competitive payment space, the industry should adopt a long term horizon and be prepared to sacrifice immediate term profits in order to sustain its profits and build affordable and sustainable e-payment solutions that cater to the needs of the masses, including the unbanked and the underbanked. Collective efforts to build and share infrastructure would be a step in the right direction.

Policymakers on the other hand have the duty to create the enabling environment by removing price distortions, promoting competition and protecting the interest of consumers.

Equally important are the continuous efforts to safeguard transaction security and enhance user confidence in order not to undermine the role of e-payments as a key enabler for financial inclusion.

Since there are participants from around the region especially from the ASEAN countries, I hope that one day we would have one card for ASEAN, where ATM cards issued by any bank in the ASEAN countries can be used to transact within the ASEAN region.

I hope you will benefit and be inspired from the discussions, debates and sharing of best practices during this forum. I also hope there would be a change in the mindset of the industry in driving financial inclusion via e-payments. On this note, I wish you all an engaging and productive forum.