Anita Angelovska Bezhoska: Shaping payments innovation

Speech by Ms Anita Angelovska Bezhoska, Governor of the National Bank of the Republic of North Macedonia, at the 15th Conference on Payments and Market Infrastructures, Ohrid, 29-30 June 2023.

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Your Excellences, Dear Ms. van Dijk, distinguished speakers,
Ladies and gentlemen,

It is always a privilege and a pleasure to address you at our traditional Conference on Payments and Market Infrastructures. An event, organized in collaboration with the Dutch central bank, a successful partnership that lasts for fifteen years. Therefore, this year we mark an important anniversary. And I have no doubts that celebrating this occasion, while contemplating on the cutting-edge payment innovations, will be much more memorable in the surrounding of the iconic beauty of Ohrid, a city whose breath-taking architecture speaks of creativity and innovations of past civilizations. As the Dutch writer, a friend of the city of Ohrid said, "In fact, it is worth going from Paris to the Balkans just to see Ohrid. What a magnificent location on that steep hill! And the town, an extraordinary mixture of customs and centuries...".

Creativity or using original ideas to create something new, and innovations, which is introducing new things, are more than ever features of our societies. The ongoing fast wave of digitalization is having wide-ranging effects on many segments of our lives. It has been transforming public and private services, making them more accessible and convenient to consumers, contributing to higher inclusion. More broadly, it means improving the wellbeing of economies as finance, knowledge and data become more widely available. Particularly rapid are technological innovations in financial services, with the payment industry being at the forefront.

Current and future trends in payments innovations and implications for central banks will be the focal point of my address. Innovations in payments rest on three main pillars (World Bank, 2022). The first one relates to the changes of the links between payments and accounts. For example, for a long time, access to payment services was dependent on access to bank account. The so-called pre-paid concept (e-money) broke the exclusive link between payments and bank accounts. The second pillar rests on the changes in the way payments are processed (payment systems) – we observe proliferation of fast payments, distributed ledger technologies, QR codes, digital IDs etc. And the third pillar relates to the changes in the way consumers interact with payments with growing accumulation of customers data and tools for analysis.

Innovations along these three pillars are redefining business models of payment providers with far reaching effects on the very structure of the payments market. This means, entrance of non–banking providers, stronger competition, costs reduction and real time payments as a new "must have" feature in payment services. Seems that banks as incumbents have also benefited from competition pressures, modernizing and sophisticating their payment infrastructure. In fact, digitalization of banking is not a new phenomenon. It has been here for more than 30 years, although this last wave is of unprecedented scale. Yet, the market is transforming, which is also visible through the change in the revenues sources of banks. According to McKinsey Global Payments Report, payments revenues of banks are declining, as standardization, technology and regulatory pressure for open banking allows for new entrants and pressures on profit margins.

The consequence of this payments overhaul is shift from cash, checks and paper-based credit transfers to digital payments, especially contactless and fast payments whose value and volume reached historically highest levels. According to Red Book statistics, in the last decade the annual average number of digital payments per person increased from 179 (2012) to 332 (in 2021). In a similar vein, the Global World Bank Findex Database, points that the percentage of adults who made/received digital payments increased from 44% in 2014 to 64% in 2021. These trends are evident in the Macedonian economy as digital payments per person more than tripled during the last seven years.

In addition to more convenient, cheaper and faster payment services, digitalization has been conducive to rising financial inclusion. In 2021 compared to a decade ago, the percentage of adults holding a bank account increased globally from 51% to 76%. In the Macedonian case, this indicator is set above the global average at 85%, compared to 74% ten years ago.

Apparently, we do see fast and profound changes in the financial industry that inevitably affect central banks in many ways. On the one hand, we operate, regulate, supervise and oversee payment systems that are important for the overall financial stability, the transmission of monetary policy, and for the confidence in the currency, eventually. As innovation in finance does not only bring benefits but risks as well, central banks must ensure that risks are contained and do not impair financial resilience and traditional mandates of central banks. On the other hand, we have to keep pace, incentivize and support financial innovations.

So how is the central banking community grappling with the new and innovative payment eco-system? According to the Central Banking Fintech Benchmarks Survey (2023), over 80% of central banks pointed to payment innovations and central bank digital currencies (CBDCs) as top research priorities. About two thirds of the central banks have created innovation hubs, although more in advanced than in developing economies, and half of the central banks use machine learning technologies or artificial intelligence.

Regulatory and legislative changes are taking place intensively. According to IMF – WBG Fintech Survey, 73% of surveyed jurisdictions review and amend their policy frameworks with a view on encouraging fintech investments, innovation and adoption. The oversight and supervisory profile of central banks is changing as well. As we have to supervise non-bank payment institutions, we deal with entities with different risk profiles and put greater focus on issues such as transparency, pricing, market conduct, consumer protection. The flourishing of new technologies requires increased focus on cybersecurity. Overall, changes in the financial scenery require regulatory, organizational and operational redesign in central bank perimeter.

One of the most explicit responses of central banks to the digitalized and modern uptakes in the payment industry is the idea of launching CBDCs. Currently, central bank money for retail is available only in physical form - cash, but the rapid digitalization is underlining the risks of diminished use of cash and its role as a monetary anchor. To make sure that money supply remains in the hands of central banks, CBDCs are increasingly gaining prominence, in particular retail CBDC. According to the latest data - 114 countries, representing over 95 percent of global GDP, are exploring a CBDC. Three years ago, only 35 countries were considering a CBDC. Eleven countries have fully launched a digital currency. In the G20 countries, 18 are now in the advanced stage of CBDC development. ECB plans to complete investigation phase by the end of this year.

Motivations for the issuance of CBDCs go beyond maintaining monetary sovereignty. It is also about strengthening monetary policy pass-through in digital era, combating the illicit use of money, strengthening competition for e-money payment providers, improving payments efficiency and safety, and promoting financial inclusion for underbanked citizens. Of course, it does not come without risk and challenges. The most prominent risk is the risk of disintermediation if the issuance of digital currency results in deposits flowing from commercial banks to central bank accounts with adverse implications for lending activity and consequently, real economy. In particular, in case of financial systems distress, it can intensify the run risk and amplify the shocks. The need to balance between integrity and the privacy of money also comes to the fore. Elevated cyber risk is also inevitable, given the technologies deployed for digital currencies. All this indicates that central banks have "fulltime job" in devising the most appropriate CBDC design that will minimize these risks and maximize benefits.

Our national efforts more or less resemble global trends and initiatives. As a central bank, we strive towards encouraging innovation in finance, as visible through the establishment of our Innovation Hub. We map the ecosystem, via fintech surveys to better understand its current state and act towards eliminating barriers, while containing risks. The recently adopted Fintech Strategy is providing a platform for coordinated and streamlined efforts by all stakeholders in the regulatory area. A recent Central Banking Survey revealed that only 54% of surveyed central banks do have a strategy that underscores our visionary approach towards the fintech area. We have already created a stimulating legislative background, with the new Law on payment services and payment systems that entered into force this year, Furthermore, we have recently embarked on exploring the possibilities for introduction of digital Denar. Last but not least, propelling efficient and harmonized cross border payments is key to support and stimulate cross border integration. This is particularly the case for small-size economies, such as ours, with growth model based on international trade and finance. Our regional efforts to comply with European standards, fulfill SEPA requirements, and integrate into the Target Instant Payment System-TIPS of Euro system is a step in a right direction.

Looking forward, it is always challenging to foresee the future, but it is highly probable that the pace of financial transformation is set to continue, if not to accelerate. Few years ago, a study denoted ten avenues that will shape the future of payments, and some of them are already taking place. Issuance of digital currencies, more active role of regulators, data – based payments value chains, a consensus on data privacy, biometrical ID, and strong collaboration between new entrants and traditional players. These are now all already existing dimensions of the finance matrix. I would add that ESG concerns are one of the key feature of the future of payment industry as well. In that new world of finance, the only way to minimize the risk of being left behind is to be agile and fast adapting institution.

At the end, let me conclude that the world of finance is moving ahead. Keeping the pace, anticipating and addressing risks, while encouraging innovative solution must be central banks focus.. Let me refer again to A. den Doolaard, who ones said, "We lived among miracles, but we never understood them". Now, in the world of finance more than ever we face new miracles, innovations and novelties that we need to understand, and be prepared and competent to support and protect.

Thank you.