



# REPORT

A white circular graphic with a drop shadow, containing a clock icon, the number "15" in a large serif font, and the text "reading time" and "minutes" in a smaller sans-serif font.

  
**15** reading time  
minutes

## **Report on Accelerating Economic Growth: digitizing payments for fast and reliable transactions**

November 2020

**Report on Accelerating Economic Growth: digitizing payments for fast and reliable transactions**

**17 November 2020**

*This report is a summary of an online panel discussion held by IPR on 17 November 2020. The speakers were:*

- *Dr. Reza Baqir, Governor SBP*
- *Mr. Muhammad Aurangzeb, President & CEO HBL*
- *Dr. M. Sohail Rajput, Special Secretary, Commerce*
- *Mr. Irfan Wahab Khan CEO Telenor*
- *Mr. Ehsan Saya Managing Director, Daraz Pakistan*
- *Mr. Mick Wu, CEO FuiouPay (Pakistan)*

Chair: Humayun Akhtar Khan IPR

**Humayun Akhtar Khan Chairperson IPR:**

- Pakistan has much catching up to do in shifting from cash to digital payments which is needed for transaction efficiency and financial inclusion.
- Recently, SBP has filled much needed regulatory and policy gaps. Already, a dynamic though emerging set of fintech, PSOs, and PSPs have incrementally laid the foundation for digitization. SBP's support is helping scale up the effort.

- The combined efforts of all stakeholders will meaningfully increase the size of the digitization in the economy. This will stimulate economic growth and development in Pakistan.
- Improvement of card payment infrastructure and rationalizing merchant discount rates and their distribution by the State Bank, as well as capping the interchange fee, have given a major fillip to digitalization.
- These changes would allow satisfactory returns on installing capital intensive POS machines.
- State Bank's Asaan Mobile Account Scheme along with third party interoperability network providers will help improve interoperability in the country. There is need to include alternate delivery channels, such as EMIs, in the AMA scheme.
- The private sector must avoid small close systems and pool their efforts through open loop infrastructure sharing.
- Ireland is an example of an economy leap frogged from agriculture into high tech. While Pakistan needs to expand manufacturing, it too can leap to high tech. It has a young population and big enough footprint of mobile devices to have the scale for doing so.
- E-commerce and payment service industry in Pakistan is likely a great source of future growth.
- Pakistan could look at China as a technology provider both for hardware and software solutions.
- EMIs must play a greater role in cross border payments. Pakistan's e-commerce platforms still face hindrances in making payments to merchants outside Pakistan. We need effective systems to do so. EMIs must also capture overseas remittances

### **Dr. Reza Baqir Governor State Bank of Pakistan:**

- As macro indicators have become normal, SBP is focusing on structural reforms in financial sector. Digitization of payments and of business processes is an important initiative.
- SBP's National Payment System Strategy, NPSS, lays a road map to promote digital financial services and payments.
- This slowed because of COVID, but has now revived, along with the connected agenda of financial inclusion

- Organizationally, SBP has a dedicated Deputy Governor for digitization and inclusion.
- NPSS' focus is on:
  - Infrastructure development to enable:
    - Instant retail payment and faster transfer of funds.
    - Another priority is to bring smaller firms into the digitized ambit.
    - Currently, the Real Time Gross Settlement System processes an average of Rs. 1.5 Trillion/day.
    - SBP will soon launch the micro-system gateway.
    - SBP has enabled digitization of government collections and payments at federal and provincial levels. It has enabled use of alternative delivery channels for government transactions.
  - Policy and regulations:
    - In 2014, SBP issued rules for payment digitization by non-Banks. This helped introduction of several key digital payment channels and instruments such as the interbank fund transfer, digital utility bill payments, and launching Pakistan's own domestic credit card.
    - SBP has approved 11 PSOs or PSPs, of which four can offer commercial services<sup>1</sup>
    - In 2019, it issued regulations for Electronic Money Institutions, EMIs. It approved 7 EMI applications, of which 4 are in pilot operation. EMIs could add innovation and user friendly digital payment products.
    - To include small firms, SBP has introduced digital onboarding of merchants and standardization of QR codes in Pakistan.
    - Roshan Digital Accounts was launched to offer digital account openings for overseas Pakistanis. This has gained popularity with 700 to 1,000 new accounts/day. So far eight banks offer the service. Fintechs could come in if they comply with standards. Subsequently, SBP will allow domestic account opening.
    - To build security of transactions and to guard against cyber-attacks, SBP has issued several guidelines. SBP and financial institutions have conducted security due diligence.
    - SBP has encouraged Fintechs and is now facilitating small fintech firms to work with SBP.
    - Recently, SBP waived transactions fee for online fund transfers. Consequently, digital transactions grew from 190,000/day in March 2020 to over 700,000/day in October 2020.

---

<sup>1</sup> PSO = Payment System Operators, PSP = Payment Service Providers

- Third, SBP introduced direct cheque deposit facility, simplifying cheque clearance process.
  - SBP is establishing an innovation office that will strive for digital innovation across different areas of the financial sector such as payment services, market infrastructure, and data for credit appraisals and capital raising.
- Fourth, SBP will establish a fintech facilitation network where new fintech will receive guidance on their proposals
- Finally, SBP will carry out a review of the regulatory and legal oversight framework to bring it at par with international standards

### **Sima Kamil, Deputy Governor:**

- Working with fintech, banks, microfinance bank, and telecoms, SBP's innovation office will convert new ideas into reality, taking care to balance innovation with security.
- SBP's micropayment gateway will begin end December, focusing on bulk payments, such as dividend payments and then moving to salary and pensions.
- The present digital payments ecosystem does not encourage livestock or farm level transactions. SBP and HBL experimented during Eidul Azha by using QR Codes, but acceptability was low. SBP is engaging with the agriculture and other underserved sectors, including SMEs, to bring rural areas into the payment ecosystem. With a functioning micro payment gateway the situation will improve.
- International Payment Gateway permissions is given in stages. Applicants first receive initial approval, which means ascertaining capital requirement. They then move to a pilot phase, after which they get full permission.
- By reducing cash in the economy, implementation of monetary policy becomes effective. SBP is committed to reducing role of cash.
- An unexpected consequence of COVID-19 is a digitally literate customer, who now trusts digitized payments.
- SBP and banks have run financial literacy programs to build understanding of the benefits of DFS. Ability to lend digitally would be a major step-up, especially if it includes underserved segments.
- At present, security issues preclude cryptocurrencies, but a central bank digital currency is in SBP's plans.

## **Muhammad Aurangzeb, President HBL:**

- COVID-19 has given stimulus to digitization. Within weeks there was greater client readiness, client acceptability, and demand for faster and efficient payments.
- SBP's enabling environment has helped banks respond to this demand. Yet the overall ecosystem still needs to improve.
- Years of putting in place the hard and soft infrastructure enabled financial institutions to meet sudden growth in demand. HBL had in place an elaborate network and its large debit and credit cards portfolio with the country's largest digital payments mobile app.
- HBL also has the largest share in processing e-Commerce and digital salary payments. It has a 10-15% market share in QR merchants and in biometric devices for branchless banking.
- HBL wants to partner and work with Fin techs. It has decided to invest in Fin techs by launching venture capital and corporate funds.
- HBL welcomes non-Banks, such as EMIs and PSPs. Their turnover will grow as they progress.
- While banks must continue their efforts to boost digitization, the whole supply chain must transform. Digitization of small retailers is critical. It depends on the enabling environment, which is improving with SBP's lead. Yet, all stakeholders must respond. For example, in Punjab, digital payments attract a 10% sales tax advantage over cash payments. Such incentives boost demand for digital payments.
- Pakistan has over a million<sup>2</sup> retail outlets with a turnover of about Rs. 9 Trillion. In addition, there are 10 million farmers with an estimated annual sales of Rs. 3 to 4 Trillion. Within manufacturing, pharmaceuticals alone has 800 formal units with annual sales of Rs. 450 Billion. It is critical to bring them into the fold of digitization.
- Payment industry must move from closed loop to interoperability. This makes payment processing a commodity. When this happens, competition is based on value added services and innovation.

---

<sup>2</sup> Pakistan has about five million off-line merchants

- China has the largest banks in the world. Yet, 90% of payment businesses are outside the banking industry. There is a lesson here for Pakistan banks to improve digitization, or we may see a repeat here
- We must also learn about China's lending platforms. The regulators must ensure a level playing field in terms of capital requirements, liquidity and other needs to avoid surprises for new entrants.

## **Mohammad Sohail Rajput, Special Secretary, Commerce:**

- Government's E-commerce policy was fortuitously well timed, as the pandemic brought sudden growth in digital transactions.
- Potential GDP growth from e-Commerce in five years is estimated to be USD 36 Billion and an estimated 4 million jobs.
- Commerce Ministry's e-Commerce policy has five major pillars:
  1. Regulation and Facilitation
    - i. GoP has established a broad based and dedicated e-Commerce council mandated to drive e-commerce in the country. MOC is also working to facilitate cross-border e-commerce. GoP's rules of business have been amended to entrust this role to MOC.
  2. Financial inclusion and digitization
    - i. The Kamiyaab Jawaan program will offer loans to new entrepreneurs, especially women. GOP is incentivizing banks to participate more in this programme.
  3. SME and youth empowerment through e-Commerce
    - i. MOC will enable 50,000 SMEs in remote areas to become part of the online marketplace.
    - ii. MoC and TDAP are creating an e-Commerce business facilitation hub. Its goal is to scale up export enhancing e-Commerce and also help firms access venture capital finance.
  4. Consumer Protection
    - i. After enacting legislation for Islamabad, GoP will assist provinces to legislate protection of consumer rights in their jurisdictions.
    - ii. There is need to harmonize GST on services among the five jurisdictions in the country.
    - iii. This will enable firms to file a single return for all five jurisdictions via a single portal. Presently each business must file five returns.
  5. ICT Infrastructure and Telecom services

- i. There is need to enhance internet penetration in Pakistan and for effective implementation of Telecom Policy 2015.
- E-commerce logistics will also be automated. National freights and logistics policy is being prepared. MOC and MOITT<sup>3</sup> will ensure enactment of data protection Act. Likewise, they will issue a cloud server policy. A robust legal and policy framework will accompany these efforts.

### **Irfan Wahab, CEO Telenor Pakistan:**

- With 80% of our population using mobile telephony, the next step is to provide them access to digital services through links to education, entertainment, health, and e-Commerce services. At the heart of this shift is digital payments.
- Recently, use of mobile wallet and digital payments have accelerated, spurred on by COVID.
- Pakistan is in a good place today to scale up digitization. There is a huge uptake in telecom services. We see that in the number and value of transactions at Easy Paisa. Overall digital adaption has boomed. Driven by demand, there is great potential for shift to cashless
- At Telenor, five million customers used retail shops to top up their cards. In six months, about two million of them are doing so digitally.
- A recent study estimates that digitization could add USD 45 Billion to the GDP in five years.
- Transactions valuing Rs. 100 Billion is shifting from cash to e-Money every month. This data is for just two service providers, Easy Paisa and Jazz. How to build on this trend.
- There are some friction points. We find our incentives for interbank fund transfers do not reach the customer as retailers often levy their own fee. These charges are necessary for business sustainability.
- By improving the entire payment ecosystem, we could aim to bring 75 million non-banking people into the banking system and mobile banking and wallets could be their starting point.
- We may shift from NADRA's Know Your Customer requirements to equally robust and secure third party validation or telecom databases. Presence less system for entry accounts is key to meet our first goal of inclusion.



- Through tax and duty reduction, we can shift the over 50% non-internet cell phones entering the market each year to smartphones. More than a connectivity tool, this will stimulate financial and digital inclusion and spur growth.
- We must have an open ecosystem, whether its consumer protection or retailer transactions. Credit scoring and micro lending insurance will help scale up DFS. There is a good opportunity to scale up value added services.

### **Ehsan Saya, Managing Director, Daraz Pakistan:**

- Globally, e-Commerce is among the fastest growing business sectors. It has also fueled job growth. E-Commerce faces three challenges:
  1. Logistics infrastructure
  2. Customer trust
  3. Digital payments
- In e-Commerce prepaid customers bring turnover advantage. With such buyers, there is a 99% chance of successful delivery of product. It is unlikely that the product will be returned. With cash on delivery that success rate falls to 84%. This multiplies cost for the seller and the logistics companies. Also, with cash on delivery it takes much longer for the seller to get their money.
- Daraz has worked with banks and wallets to incentivize pre-paying customers, by offering discounts. Daraz also makes especial effort to educate the customer to use their cards. Such efforts have brought about a 100% YoY growth in digital payments. A big downside for customer is the cumbersome and delayed refund procedures, which is a deterrent to building customer trust. Often refunds take up to 45 days. This is not feasible, especially for big ticket purchase.
- Also, the transaction cost of using digital wallets is high for the customer. Digital transactions will grow if we reduce transaction cost. Cash payment can have zero cost.
- Another way to incentivize digital payments is to offer value added services, such as medical insurance. But that needs major infrastructure support from government, especially for financial institutions' inter-operability.
- Done right, digitization should enable the seller to receive their receipts quickly. The current time lag of 15 days places a working capital squeeze on the seller and restricts their ability to increase turnover.

## **Mick Wu, CEO FuiouPay (Pakistan):**

- The turnover of China's mobile payment was 40 trillion US Dollars in 2019.
- Payment tools are the point of start. Starting with Alibaba's Alipay, payment channels evolved in China. Now a myriad of apps and wallets from banks, telecom, e-Commerce, and chat platforms exist. The Chinese central bank has even begun a trial for digital currency. The consumer has a slew of mobile payment options.
- Gradually, this phenomenon is replicating in Pakistan where banks, telecoms, and third party providers are launching and expanding their own wallets and combining with a vast offline agent network. SBP and SECP's regulation is helping.
- To speed up this process, it is necessary for both payment and business digitalization to advance in tandem.
- The first step in business digitalization comes in the shape of POS machines. The point of sale is key no matter which payment tool is used. Whether it is e-wallets, bank cards, digital currency, fingerprints, face id, VR or AR devices, the POS must be able to accept it.
- This is where business digitalization comes in. Smart POS machines can also build customer data and form customer profiles. In a third step, the POS machine is a tool to issue coupons or promotion. Thus, the smart POS creates a unified management system for collection and marketing.
- For the firm, a major advantage from business digitalization is that human data is on a cloud server linked with all parts of the business. This creates efficiency and reliability. It brings certainty to the supply chain with predictable payment and receivable timeline and enhanced credit in the system so that payment can be guaranteed.
- At the firm level, it brings more working capital certainty, and turnover can grow. Extrapolated, the central bank can use these tools to plan at the industry level.
- Firm level digital payment systems often result in closed small systems that are not interconnected. That is a waste of social resources. The regulator can step in to establish a public platform for more connectedness and transparency.
- China's central bank has set up 2 state owned clearing institutions. They offer unified payment interfaces to all payment institutions. They also decide the tariff structure for different payment methods. The clearing institutions make especial effort to promote competition.

- The payment institution must provide data security, continuous service delivery and system stability. This is specially necessary in the early stage of digital payment development to build customer trust. In Pakistan, a major goal should be to improve hardware capacity.
- In China, enforcement and inspection by the central bank is very rigorous. Merchant reliability is another key responsibility of regulator and payment institutions.
- Given the importance attached to accelerated digitalization, China reviews these developments at top government levels, by the State Council.
- In addition to reliability and transparency, which are key, government should attract more digital payment users through fiscal incentives. Other than doing so at the sales tax stage, government may reduce import tariff for POS machine and infrastructure development for payment and business digitalization.

## Board of Directors

Mr. Humayun Akhtar Khan, Chairman & CEO

Mr. Akbar Khan

Mr. Haroon Akhtar Khan

Dr. Khalida Ghaus

Mr. Ghazi Akhtar Khan

Mr. Ashraf M. Hayat, Executive Director

## Board of Advisors

Lt. Gen (R) Sikander Afzal

Dr. Manzoor Ahmad

Mr. Syed Yawar Ali

Ms. Roshan Bharucha

Mr. Hussain Haroon

Dr. Iqrar Ahmad Khan

Mr. Tasneem Noorani

Mr. Tariq Parvez

Mr. Salman Raja

Dr. Atta-ur-Rehman

Dr. Abid Suleri

Mr. Abdullah Yousaf

4- Shami Road, Lahore Cantt, Pakistan

UAN:111-123-586

<http://ipr.org.pk>

<https://www.facebook.com/ipr.org.pk>

[https://twitter.com/IPR\\_Pakistan](https://twitter.com/IPR_Pakistan)

## Copyright

No part of this publication may be reproduced or transmitted in any form or by any means without permission in writing from the Institute for Policy Reforms