GLOBAL PAYMENT INFRASTRUCTURES AND CROSS-BORDER PAYMENTS

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Using metrics to navigate the fragmented seas of cross-border payments

Fragmentation of the payment ecosystem is looming large following the rise of geopolitical tensions, stressing the need for cheaper, faster, more transparent and more accessible cross-border payments to support international trade, economic growth and financial inclusion.

Three years ago, the G20 established an ambitious plan – the Roadmap – and set high-level quantitative goals to be achieved by end-2027. These goals represented a foundational step of the Roadmap, to define its ambition, provide accountability and, importantly, to steer actions and improvements under the overall programme[1].

Huge work has been accomplished since then; analyses and public-private cooperation have provided key insights and useful tools to impulse change in a coordinated manner. We now stand at a tipping point where concrete implementation is required in order to achieve meaningful results, including on remittances.

The identification of data sources and the definition of KPIs was a key starting point to allow for fact-finding, at a granular level whenever possible (by use case, by region) and for a good understanding of the challenges. The methodology is now in place and we look forward to the forthcoming baseline estimates of market performance[2] to better understand the complexity and heterogeneity of the payment ecosystem, disentangling the aggregates to understand the specifics, to steer the G20 programme toward the most impactful initiatives.

Besides the quantitative and qualitative monitoring, a public-private consensus has already developed around what the main areas of focus should be: legal, regulatory and supervisory frameworks; payment systems interoperability and extension; data exchange and message standards. Among the identified priority actions, the interlinking of fast payment systems (FPS) carries a huge potential to increase both the speed of and access to cross-border payments, with additional impacts on competition and prices where those systems are open to innovative actors. Actions around the harmonised implementation of international standards – such as the ISO20022 norm – and the sharing of experiences among public and private actors, including around the governance and oversight of interlinking arrangements, are key enablers for the success of interlinking projects. In Europe, the Eurosystem is pursuing reflections around the interlinking of the European FPS, TIPS, in order to foster European integration and ease cross-currency instant payments.

We now need to make concrete and lasting changes to bring decisive improvements. I see three levers for that. First, we need to maintain momentum, as only a resolute political commitment at the highest level can allow the roadmap to keep the traction and adapt to new challenges as we bring the work forward. Such commitment is key also to promote public-private partnerships and should rely on local outreach by national central banks. Second, the programme needs to reach a large number of jurisdictions, including beyond the remit of the G20 where frictions are more acute. The IMF and the World Bank have a key role to play, through the setup of technical assistance programmes. Finally, more exploratory work in the field of cross-border payments should be pursued with a longer-term view. This includes increased efforts to define common standards to avoid the emergence of technological silos and the resulting fragmentation of liquidity. To this end, it is essential to focus on the interoperability between our existing infrastructures while keeping in mind their potential interlinking with DLT-based infrastructures in the future.

Disentangling the aggregates to understand the specifics, to steer the G20 programme.

Keeping the momentum on experiments is crucial to advance the analysis on the potential of multiple CBDC (mCBDC) arrangements. It is the aim of the Mariana Project[3] conducted by the Banque de France, the BIS IH, the MAS and the SNB, to explore novel options for tokenised FX trading and settlement between multiple wholesale CBDCs. This learning by doing approach will contribute to feed concrete input in the design of a single platform, as envisaged by the BIS with the concept of a *unified ledger*[4], or by the IMF with the concept of *XC platforms*[5].

1. *Denis Beau (2021), Shaping the future of cross-border payments, The EUROFI Magazine.*
2. *Following G20 approval, the KPI monitoring report will be published in parallel with the FSB's annual progress monitoring report in October 2023.*
3. *Project Mariana: Interim report, BIS, 2023.*
4. *Annual Economic Report, Section 3, BIS, 2023.*
5. *A multi-currency exchange and contracting platform, IMF, 2022; The rise of payment and contracting platforms, IMF, 2023.*

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Moving towards instant and frictionless: the G20 goals for cross-border payments

In 2020, the G20 made enhancing cross-border payments a priority. The group stated that "*making cross-border payments - including remittances - faster, cheaper, and more transparent and inclusive, while maintaining their safety and security, would have widespread benefits for citizens, businesses, and economies worldwide, supporting economic growth, international trade, global development, and financial inclusion*".

Discourse around how an efficient global payments ecosystem can foster socioeconomic benefits has been ongoing for years. But the financial services industry is now at a point where commitment to enhancing cross-border payments has never been more pressing.

The pace of change

Since the roadmap's inception, the world has undergone unprecedented transformation. Against a backdrop of rapid globalisation and shifting geopolitical realities, the need for a frictionless and inclusive international payments system has come to the fore and cemented the importance of the G20's work.

Investment in emerging technologies is also no longer seen as a choice, but a necessary step in preparing for the future. When it comes to payments, we are at a turning point. The metamorphosis of money as we know it is at an exciting juncture, and its digital form could create a more inclusive, connected financial ecosystem. Alongside the emergence of CBDCs and digital assets, we are seeing digitisation at all stages of the payments lifecycle to power this new generation of money.

Measurable objectives

The roadmap marks an inaugural step in recognising global payments as the crucial socioeconomic enabler that they are. Driving this forward is the work of the Financial Stability Board (FSB), which set global quantitative targets for addressing the challenges of cost, speed, transparency and access faced by cross-border payments. These targets play an important role in defining the ambition of the roadmap, and five key areas of focus were identified:

- Committing to a joint public and private sector vision to enhance cross-border payments.
- Coordinating on regulatory, supervisory and oversight frameworks.
- Improving existing payment infrastructures and arrangements to support the requirements of the cross-border payments market.
- Increasing data quality and straight-through processing by enhancing data and market practices.
- Exploring the potential role of new payment infrastructures and arrangements.

The road ahead

Now in its third year, the Roadmap for Enhancing Cross-border Payments continues to be a priority initiative of the G20. The foundational work done during 2020-2021 is moving to practical application of KPIs, working to make the 19 building blocks outlined by the CPMI a reality. The key enabler in realising this will be interoperability and partnership, supported by responsible innovation.

In furthering the G20 goals, institutions need to become more efficient to be able to pass their cost savings to end users by the means of competitive fees and terms. To achieve this, cost mutualisation across industry players is key. Investing in making payments more transparent and simpler should also be considered, linking them to the backend engines to expose payments terms upfront and in a clear way to end users.

When it comes to speed, it's not just about using the fastest rails, but service level agreements with other actors in the payment chain. As for cost and transparency, collaboration is the enabler to making this a reality for a global network of disparate payment systems.

The importance of partnerships

Industry-led initiatives will only be as effective as the cooperation and gravity they are afforded by market participants. Regular, transparent engagement between the public and private space will be the linchpin to guarantee the success of the roadmap's objectives. This can be encouraged by proactive engagement from certain entities that form the building blocks of cross-border payments. Payment systems, regulating bodies, and key industry participants can all help command a commitment to responsible innovation across payments, in turn fostering public-private collaboration.

Payment providers should look to the g20 agenda in the drive to enhance cross-border payments.

This need for interoperability and partnership will also be crucial in ensuring the successful implementation of many innovation projects that are taking shape across payments. Indeed, accelerating innovation and interoperability go hand in hand in an increasingly complex and fragmented world.

Public consultation, a pipeline of milestones, and ongoing progress review will arm the payments industry with the knowledge to know how far we've come, and what more needs to be done in bringing the G20 roadmap to realisation. Crucial to making this happen will be collaboration from industry participants. They are, after all, the ones that will be effecting change day-to-day for people who make payments around the world: everyone.

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Demystifying settlement risk to support the FSB Roadmap

In October of this year, it will be three years since the Financial Stability Board (FSB) published the G20 Roadmap for Enhancing Cross-Border Payments (FSB Roadmap). The initiative has made significant progress in addressing certain challenges in cross-border payments, moving from foundational elements to practical actions that will improve existing arrangements and help establish new ones.

The FSB Roadmap is based on the premise that cross-border payments need to be faster, cheaper, more transparent and more inclusive. Its remit is quite broad, and it is important to recognize that different market segments of cross-border payments face unique challenges. For example, while the remittance business may need to address speed and transparency, this is not necessarily the case in other areas such as wholesale FX settlement.

Building Block 9 of the FSB Roadmap specifically addresses a key challenge for the wholesale market – mitigating FX settlement risk for cross-border payments by encouraging increased adoption of payment-versus-payment (PvP) arrangements. This element of the FSB Roadmap is supported further by the FX Global Code – a set of global principles of good practice for the FX market. Principle 50 encourages FX market participants to reduce their settlement risk by channelling FX transactions through services that provide PvP settlement.

To facilitate progress and increase transparency in this area, CLS worked with a subset of its settlement members, analyzing trading activity to determine how their trades were settled. The analysis showed that of the FX transactions eligible for CLSSettlement (which currently comprise around 80% of all FX transactions),[1] on average 51% of the traded notional is settled through CLSSettlement. This confirms the key role CLS plays as the settlement backbone of the FX ecosystem.

Much of the remainder of the FX transactions comprises inter-branch and inter-affiliate trades (35%) or trades where settlement occurs via a single currency cashflow or over accounts within the banks' direct control (together, 8%), which leaves approximately 6% of trades exposed to settlement risk that could be settled via PvP in CLSSettlement.[2] Tackling these transactions and expanding participation in CLSSettlement remains a high priority for CLS.

Another important aspect of increasing PvP adoption is finding alternative mechanisms for non-CLSSettlement eligible currencies, including emerging market (EM) currencies. There has been a significant increase in EM currency trading volumes in recent years, and this is where the majority of settlement risk lies. Public policy makers have repeatedly emphasized the need to mitigate settlement risk for these currencies.

CLS's public-private approach has achieved success in capturing FX transactions for PvP settlement.

CLS has been actively working with the industry to explore alternative PvP mechanisms for EM currencies and has received strong support in these efforts. However, progress in this area must overcome regulatory and geopolitical challenges and will require public and private sector stakeholders to closely collaborate and actively contribute to an industry solution. CLS strongly believes in the power of public-private sector partnerships, as demonstrated by its creation in 2002 as a private sector response to public sector calls to mitigate settlement risk for FX transactions.

Due to the current challenges in developing alternative PvP mechanisms, for now CLS is focusing on growing CLSNet, its automated bilateral payment netting calculation service for approximately 120 currencies. CLSNet helps to mitigate operational risk associated with trading EM currencies.

By standardizing and automating the netting calculation process, it supports the subsequent netting of payments to reduce the payment obligations exposed to settlement risk while improving operational and liquidity efficiencies. Crucially, a significant portion of the interbank transaction flow through CLSNet is in the deliverable EM currencies that pose the most settlement risk for CLS members.

The FSB Roadmap recognizes the importance of PvP in mitigating risk in wholesale markets, and the continued support of the public sector is critical in achieving this. As a financial market infrastructure at the center of the FX ecosystem, CLS's public-private approach has been successful in capturing eligible FX transactions for PvP settlement. However, due to the current legal and regulatory constraints, bilateral netting appears to remain the most effective way to mitigate risk and increase operational efficiency for EM currencies.

1. *Calculations can be found here: cls-group.com/insights/shaping-fx-ecosystem/shaping-fx-01-taking-a-central-role-cause-and-fx/*
2. *cls-group.com/insights/shaping-fx-ecosystem/shaping-fx-02-fx-settlement-risk-to-pvp-or-not-to-pvp/*

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Public-private partnership remains critical to improving cross-border payments

Cross-border payments are critical to the global economy, with nearly €9.7 trillion in annual transaction volume fuelling international commerce. However, cross-border payments are inherently more complicated than domestic payments, sometimes leading to challenges with cost, speed, transparency, and access.

Given this complex, fragmented landscape, the G20 Roadmap for Enhancing Cross-border Payments is bringing together stakeholders from around the world to identify challenges and solutions. This work has significant implications for Europe, especially future efforts to further harmonise payments within the single market. A key characteristic of the roadmap's approach has been a commitment to public-private partnership. We see tremendous value in this partnership and believe it is the single most important factor in the success of the G20's work.

To better understand why this partnership is so important, it is worth spending a bit of time outlining the public and private sectors' respective roles and responsibilities in improving cross-border payments. Let us start with the private sector.

First and foremost, the private sector excels in meeting end users' needs in making and receiving cross-border payments. These needs are ever evolving and vary depending on the use case. For instance, someone making a payment to book a vacation abroad likely has different needs than a migrant worker sending money back home to their family.

We should keep business needs in mind too: for instance, a small business' cross-border payment needs will differ significantly from those of large multinational corporates. As we have written about recently, private sector firms solve for these different use cases with customised solutions, all of which require different considerations in the roadmap.

Addressing user needs also requires that the private sector make continuous investments in innovation. Despite the complexities and pain points facing cross-border payments, Visa and others in the industry are developing innovative technologies and services to drive down costs and make payments faster, safer, and more transparent. Over the last five years, Visa invested over €9 billion to secure and enhance our technology platforms, preventing roughly €24.5 billion in global fraud every year with incidents of fraud occurring in less than 0.1% of transactions.

Public-private partnership is the single most important factor in the success of the G20's work.

We are also committed to streamlining cross-border payments with our global money movement platform Visa Direct, which enables nearly 30 new types of payment flows, including remittances, merchant settlement, and employee pay-outs with real-time capabilities across 190 countries. For business-to-business payments, Visa B2B Connect enables same-day payment services and a seamless cross-border experience by removing some of the frictions associated with correspondent banking.

Even with these investments, the private sector's role is only half the story: the public sector plays an equally important role, especially in addressing today's biggest issues. In looking at the G20 work itself, an obvious and defining role for the public sector is that of convener. Intergovernmental organisations like the Bank for International Settlements (BIS) and the Financial Stability Board (FSB) embody this role on a global stage, bringing many stakeholders together to find real solutions. This same approach has been especially important in Europe, where stakeholder inclusion is an essential part of the policymaking experience.

The public sector also plays a critical role in establishing frameworks and rules for the system, which protects consumers, encourages fair competition, and maintains financial system integrity. This is perhaps the single most important role in cross-border payments – without rules, end users would lose trust in the system. Here, European policymakers have played a particularly important role as first movers in protecting consumers and harmonising standards and regulations across multiple markets.

Of course, some rules occasionally do more harm than good, especially when rules vary widely across corridors and increase payment friction. Here, we see tremendous potential to improve end user experiences by streamlining regulatory requirements. This is also something the public sector widely recognises and is seeking to address with the G20 work, particularly through the FSB's taskforce on legal, regulatory, and supervisory matters.

The public and private sectors each have their respective strengths and responsibilities when it comes to improving cross-border payments, but neither can do it alone. As the G20 Roadmap progresses, we are encouraged to see that public-private partnership remains at the core of this work, and we commend the leadership of the FSB, BIS, World Bank, and other public institutions driving this work.

At Visa, we remain committed to improving cross-border payments by meeting end user needs and maintaining productive partnerships with governments around the world.