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# Towards a highway for money

**There are unseen costs to economies heavily reliant on cash. Today, there are choices to reduce this dependence**

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Ever since cash replaced the barter system of trade, it has been the most preferred mode of transaction. It is convenient, simple, quick to use and leaves no audit trail. However, like any other payment instrument, cash has multiple costs—that of cash handling, infrastructure as well as risks of fraud and counterfeits. Cash also fuels the "shadow" economy, i.e., commerce outside the tax net, a key concern for governments.

Globally, governments have created "electronification" charters and are at various stages of implementing solutions to tackle this problem. The challenge is to create awareness on the true costs of cash in the economy and pave the way for more convenient, cost-effective and efficient electronic payment solutions.

As part of its electronification charter, India has implemented several initiatives to popularize card payments. While the National Payments Council has been established, the UID-Aadhaar project targets the entire population of India for "formal" identification, leading to financial inclusion. The Reserve Bank of India has enacted several progressive policies that aim to create a governance model and operating framework for a robust electronic payment network essential for rapid electronification.

What are the benefits of electronification? It lowers cost of printing and managing currency, increases transparency in commerce by nipping money laundering in the bud, eliminates the parallel economy, leading to higher tax revenues and plugs leakage to final recipients of subsidies. E-payments will increase the utilization of many subsidy schemes.

Governments can target multiple electronic channels to pursue their electronification strategy. Some of these are cheques, electronic fund transfers, pre-instructions for recurring payments, payment cards—prepaid, debit and credit cards. A pragmatic electronification strategy combines all these modes to drive financial inclusion in a secure and suitable way.

Cards are the most popular and are preferred by consumers. In India, card payments account for less than 2% of the gross domestic product (GDP). Even if other electronic fund transfer modes are taken into account, the share is at best 5-6%. In the US, debit and credit card purchases represent 30%-plus of GDP. India's penetration in electronic payment for utilities is negligible whereas in countries such as Australia and Singapore it is 24% and 4%, respectively. Similarly, insurance payments are negligible in India compared with Australia (35%) and Singapore (4%).

Why hasn't card payment become more popular? Primarily, it's a combination of inadequate card penetration (India is at 0.15 per capita penetration on credit cards vis-à-vis the US at 2.53 and the UK at 1.35) and inadequate acceptance infrastructure (India has a 0.05 point of sale (POS) per capita vis-à-vis 20 in the US and 1.95 in Brazil). Low awareness of debit card usage at POS, high costs of transactions, security concerns and tax issues too have played a dampener.

India needs to focus on areas of enhancing card penetration like growing acceptance infrastructure, mitigating security concerns and increasing awareness levels on the benefits of card payments. The Indian banking industry, as custodians of the consumers' financial relationship, must play a critical role in implementing these objectives and evolve an efficient, cost-effective, secure and convenient model that achieves national electronification objectives and is commercially viable for everyone.

But who will invest in increased terminalization? What are the economics of an electronic transaction covering all costs in the payment ecosystem? How can we encourage merchants to demand more payments through plastic? How will we educate customers on benefits of plastic use?

No single model will succeed in every country. Hence, markets will have to evolve their own strategies on the basis of ground realities. However, there are important lessons to be drawn from countries with similar payment behaviour.

The South Korean government gave fiscal incentives to consumers and merchants for increased usage and acceptance of cards (20% of credit card expenditure could be deducted from the credit card user's taxable income). Result: Card usage as a percentage of personal consumption expenditure increased from 15% to 65% between 1997 and 2010. South Korea now has more than two million POS terminals compared with India's 600,000. In Argentina, the government introduced a VAT rebate in 2001 for consumers paying through cards, initially for a two-year period. An outstanding success, the scheme was consequently extended.

For India, a possible multi-pronged approach could be: a) to increase card acceptance, incentivize banks to invest in rapid terminalization, especially in deep geographies, utilities, *mandis*, etc., give tax breaks to merchants to accept card payment and reduce POS terminal pricing; b) to increase card penetration, offer sops to consumers using cards and build robust risk systems; c) finally, tweaking network and transaction costs. Since interchange is a key source of revenue for banks to invest in promoting card payment programmes, we may leave this part unchanged in large cities. However, to develop electronic payment in underdeveloped markets, we can look at a lower interchange for smaller payments (<₹500), and small merchants (monthly turnover of ₹50,000-1 lakh), a differential interchange and network fee in targeted segments, business-to-business (procurement, vendor payments, supply chain disbursements, etc.) and business to government (direct and indirect taxes, octroi, VAT, service tax, utilities, etc.). To augment these steps, the government may look at implementing subsidies/schemes through cards.

Ultimately, a combination of all these would encourage rapid adoption of payment instruments, drive card activation and increase usage volume—all critical to realizing the national electronification dream.

*Comments are welcome at theirview@livemint.com*