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Future of Payments in the Middle East and North Africa (MENA)

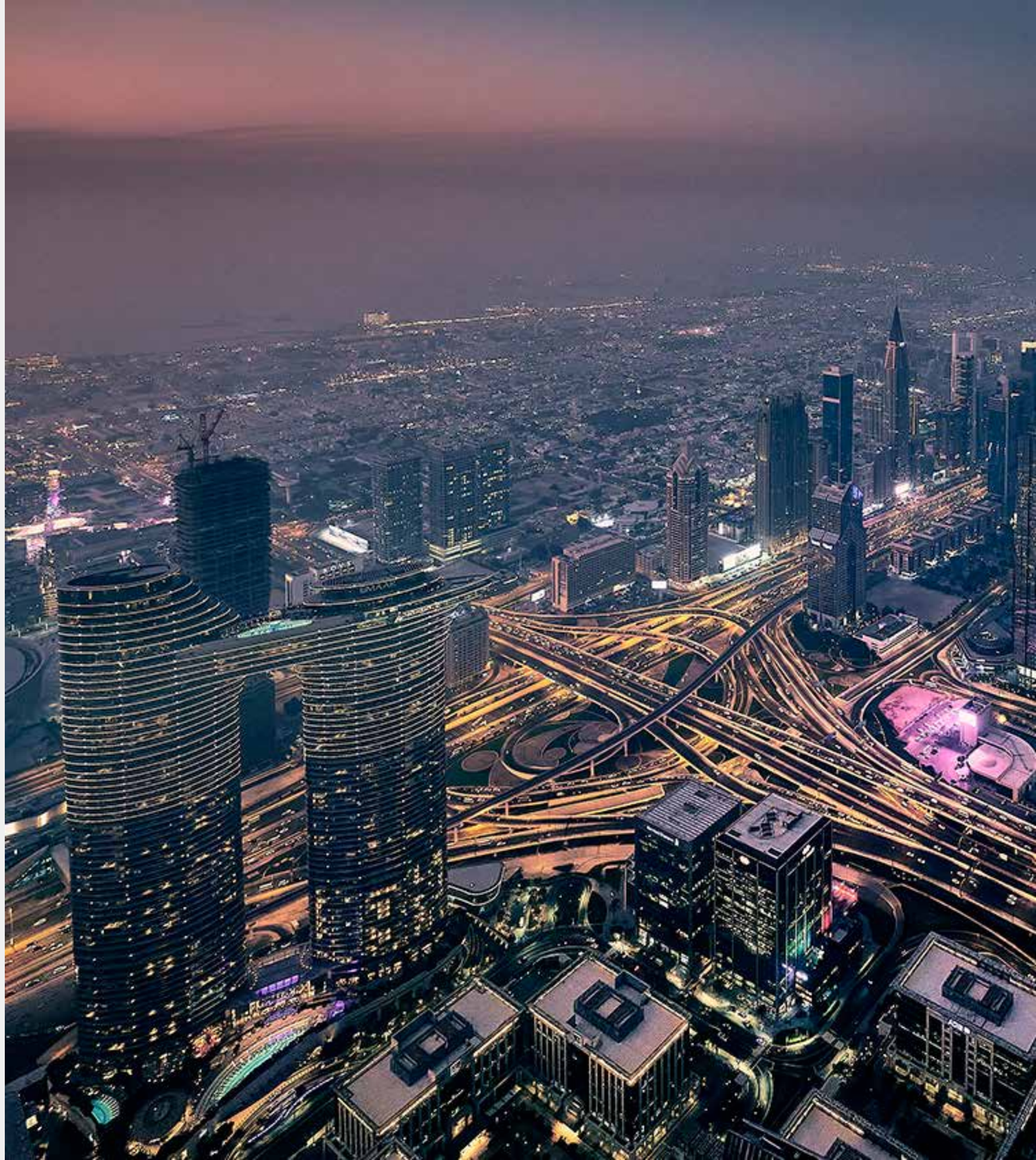
September 2022

Foreword

The MENA region is on the brink of an important financial payments reform. The inconsistency between the high numbers of digitally savvy population and the low percentages of the digital payments transactions was acknowledged and the necessary initiatives were taken by the governments both in terms of the infrastructure and the regulation. The global pandemic and its push towards a cashless society was another important driver of the alteration in the payments industry in the Middle East towards digitalization. The anticipation is that digital payments will dominate the future of payments in the MENA and be the permanent custom rather than a trend.

This whitepaper elaborates on how the improvements in the digital payments industry affect the financial environment in the MENA region and what kind of payment-related evolutions are expected to take place with the contribution of the COVID-19's financial reflactions. Following the incremental growth in digital adoption, the developments in the consumer preferences and open banking, the move upwards in the number of fintechs and non-banks, the reduction in the fees, and the increased cooperation and connection in cross-border and inner parts of the payments industry are among the most prominent shifts that are to prevail in the Middle East and North Africa in the foreseeable future.

Ahmet Vefik Dinçer, CEO



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This whitepaper explores the changes that are expected to happen in the payments industry in the MENA region even though the region by nature is fond of cash and there is an insufficiency in the digital payment infrastructures. The regulatory and digital initiatives in the area along with the acceleration trend in the digital payments as one of the consequences of the COVID-19 pandemic, the payments industry in the MENA region is expected to go through a set of alterations: upswing in digital adoption, shift in the payment preferences, nonbanks outnumbering, expansion of open banking, cross-border payments getting more interconnected, decrease in the payment fees and integration in some parts of the payments industry.

Future of Payments in the Middle East and North Africa (MENA)

The Smartphone penetration is almost 90% in big markets within the region and still only about 30 percent of the retail transactions are completed digitally.

The arrival of digitalization in the financial industry has paved the way to countless improvements in the payment services within a very short period of time. With the turmoil of the COVID-19 starting to go down as we completed the first half of 2022, it is possible to see and analyze the outcomes of the pandemic more clearly in the financial sector. The tendency to use digital payment services has seen a dramatic acceleration during the global pandemic since society has become more in favor of the contactless and cashless transactions. Even in the regions such as MENA (Middle East and North Africa) where there was a discrepancy between the rates of the digital inclusion and the use of digital payments, the latest surveys and data demonstrate that the digital payment transactions are showing an incremental growth.

In the Middle East, even though the population is highly fond of digital solutions, due to several reasons such as insufficiently developed infrastructure of digital payments, cultural tendency to use cash, and consumers' preference of remaining underbanked, the digital payment transactions remained lower than expected. The penetration of smartphones is almost 90 percent in big markets within the region and still only about 30 percent of the retail transactions are completed digitally according to the survey conducted by McKinsey & Company in August 2021. Nevertheless, new regulatory and digital initiatives within the area along with the COVID-19 pandemic have accelerated the transformation in payments and a trend of change was initiated moving at a high speed.

In MENA region, the alterations in the financial industry that are expected to happen in the upcoming years are as follows: boost in digital payments transformation, change in consumer payment preferences, dominance of nonbanks in the market, growth in open banking, more connected cross-border payments environment, adjustments in the transaction fees, and consolidation in the industry up to some degree.

Boost in digital payment transformation

It is a fact that the digital transformation in the payments field has already had a certain pace prior to the pandemic. Data show that between the years 2014 and 2019, the annual growth rate of the digital payments transactions in the United Arab Emirates (UAE) was more than 9 percent in comparison to 4 to 5 percent rate of Europe's (McKinsey & Company, 2021). The global pandemic has pushed these growth rates even further. It is expected that cashless payments are to arise up to 20 percent in the MENA region as one of the outcomes of the pandemic. As the contactless digital solutions have become what is sought by the consumers, the financial institutions focused on creating solutions to answer to this demand. It seems highly possible that digitalization will remain as a permanent custom in the financial industry rather than a simple trend.

9%
United Arab Emirates

4-5%
Europe

Change in consumer payment preferences

The payment preferences of the consumers do not stay the same as we move towards a more cashless society. The digital wallets and contactless card payments are expected to dominate the MENA market in the very near future according to the payments practitioners in the Middle East surveyed by McKinsey. Supporting this estimation, the majority of the consumers in the Middle East are in favor of digital payment methods (58%) in comparison to the small minority of 10 percent who prefers to use cash in their transactions.

Only a small minority of 10 percent prefers to use cash in their transactions.

Dominance of Nonbanks

Half of the population in the Middle East region is young-adults. There are potentially 200 million tech-savvy customers seeking new and smart financial technologies to ease their everyday lives.

As a natural outcome of the digitalization trend in the payments market and the regulatory changes, new financial payments players other than the banks have emerged in the MENA region. The presence of Fintechs, Regtechs, technology and telecom providers and many other nonbanks has been felt more and more with an increasing growth rate of 30% annually. Almost half of the population in the Middle East region is young-adults which means that there are potentially 200 million tech-savvy customers seeking new and smart financial technologies to ease their everyday lives. Therefore, the Middle East is a region of many possibilities for the growth of digital payments solution innovators.

In terms of merchandising, accelerated by the lockdowns of COVID-19, online shopping has reached its peak since 2020. Occasionally, merchants started to look for the means to create an online presence. According to the research of McKinsey & Company, the 2 most effective entities (with 40% each) that can help merchants to sell online are the e-commerce marketplaces and fintech companies. As the percentage of the banks remains at 7%, it suggests that SMEs (small and medium-size enterprises) are looking for new methods to offer services to their customers rather than simply payments. The advantages of partnering with an e-commerce platform include both processing digital payments and creating online sales. One important disadvantage of the e-commerce marketplaces is their commission rates which may rise up to 35% and cause merchants to invest in a solution offered by Fintechs that is more cost-friendly in the long term and gives more freedom to merchants in controlling their online sales activities.

At this point, it is essential to highlight that although the Fintech solutions have started to gain a momentum to no less a degree, the traditional banks are not to be displaced. Many of the embedded finance solutions still depend on the infrastructures of the banks. On the other hand, banks make use of the data collected by the embedded finance solutions.

Growth in open banking

Open banking refers to a regulatory improvement that enables banks, third-parties and technical providers to exchange the financial data of their customers with each other easily and securely. It is also called “open financial data” and the system offers a trusted framework for cooperation among different financial institutions for them to provide better and more innovative financial services to their customers. Middle Eastern countries have started to adopt the open banking developments regarding data sharing among financial institutions. In 2018, Bahrain put open banking rules into effect and two years later, in 2020 published guidelines on the exchange, sharing and managing data. In early 2022, the project of launching open banking in Saudi Arabia was announced. Such regulatory initiatives of the governments towards the amelioration of the digital payments environment in terms of security and user-friendliness create a positive effect in the consumers for embracing digital payment transactions.

2018
Bahrain declared Open Banking Rules

2019

2020
Guidelines for exchange, sharing and managing data

2021

2022
Saudi Arabia announced open banking project

More connected cross-border payments environment

$78
BILLION

UAE and Saudi Arabia operated $78 billion only in 2020 which accounts for the 7 percent of the total GDP of both countries.

As the United Arab Emirates (UAE) and Saudi Arabia own the two biggest payment corridors in the world, it is no surprise that cross-border payments are highly crucial in the Middle East region. Together, they operated $78 billion only in 2020 which accounts for the 7 percent of the total GDP (gross domestic product) of both countries. Improving the real-time settlements and enlarging the scope of the digital money transfers have become more important than ever. The success of this depends on a more connected global payments ecosystem which can be achieved with special agreements between and among countries. In the MENA region, a couple of projects have been initiated to this end which are the Project Aber which is based on a mutual digital currency between Saudi Arabia and the United Arab Emirates (UAE); the Buna payment platform that enables the members of the Arab Monetary Fund to operate transactions in different currencies; and the AFAQ system that brings together the RTGS (Real-Time Gross Settlement) systems of the Gulf Cooperation Council (GCC) countries.

The use of CDBC (central bank digital currency) as a new way of payment was a rising trend among some Middle East countries such as Saudi Arabia and the UAE. The CDBC gives the countries a chance to prolong their regulatory power while at the same time they can remain up to date regarding the fast-moving digital economy trends. Pursuant thereto, an important digital initiative is taken by the UAE Central Bank. The multiple CBDC Bridge (mBridge) project emerged as a multiple central bank digital currency (CBDC) platform and aims to improve cross-border payments experience by offering solutions to the challenges in the traditional payment methods. The most problematic issues of the cross-border payments and settlements which are timing, cost and security are targeted and to serve this purpose, the distributed ledger technology (DLT) is used as the basis of the project. The ultimate purpose is to create a cross-border payments and trade settlement platform using CBDCs (Central Bank Digital Currencies).

In addition to the UAE Central Bank, the project involves the Digital Currency Institute of the People's Bank of China, the Bank of International Settlements Innovation Hub in Hong Kong, the Hong Kong Monetary Authority and the Bank of Thailand.

The mBridge platform is tested across 11 industries including medical equipment, semiconductors and clothing, and 4 jurisdictions with several sample trade settlement transactions. In 2022, the target is to prepare the system to become production-ready for supporting the whole procedure of cross-border trade settlements and similar potential use scenarios.

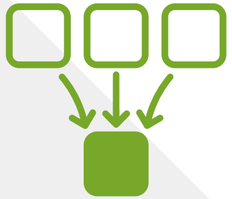
Adjustments in the transaction fees

As a natural consequence of the intensifying competition among the financial institutions and the demanding regulatory changes, the payment fees have faced either a stillness as in the case of the MDRs (merchant discount rates) or a drop recently. The declining tendency is expected by the experts to continue in the upcoming years as well. According to the survey of McKinsey & Company, the majority of the payments practitioners in the Middle East expect that the decline in the payment fees will reach to 10 percent in the next five years while 13 percent of the respondents is expecting a drop between 10 to 20 percent and finally 17 percent of them said that their expectation is more than 20 percent of a decline in the payment fees. If the expectations will turn into reality, the financial institutions and networks will have to come up with new methods to gain profit from the payment transactions.

According to the survey the majority of the payments practitioners in the Middle East expect that the decline in the payment fees will reach to 10 percent in the next five years.

Consolidation in the payments industry

One another estimation concerning the future of the payments in the Middle East and North Africa is the consolidation in the industry up to some extent. Consolidation is expected within the specific parts of the value chain and in the form of an integration. The Middle East can play an important role in achieving consolidation among financial providers in the region. One of the possible areas for the Middle East to act as a foothold for the international actors who are looking for local solutions to reach local targets is the payment gateways. These international actors may also benefit from the improvement opportunities in the Middle East area and use the geographical advantage of the region to reach Africa.



The Middle East can play an important role in achieving consolidation among financial providers in the region.

Conclusion

The most preferred payment method will be digital wallets by 60%.

Will be followed by credit and debit cards by 27%.

The Middle East was a region generally known with its dependency on cash payments until recently. The shift towards digital payments which started before the global pandemic and accelerated with the COVID-19, is moving drastically fast along with the support of the government initiatives. It is estimated that the use of digital payments will be more than a mere trend and turn into a habit in the region. As the study of the McKinsey & Company suggests, in the MENA region, the most preferred payment method will be digital wallets (60%) followed by credit and debit cards (27%). In addition to the high rates of digital payment transformation, shifts in the payment preferences, uptrend of the FinTechs and other nonbanks, developments in the open banking, higher connection in the cross-border payments ecosystem, lessening of the payment fees and finally consolidation up to some extent in the payments industry are among the future expectations for the MENA.

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About Us

Milestones
Fineksus was founded in Istanbul, Turkey in 2002 as a software and professional service provider to deliver technical consultancy, outsourcing services, standalone / SaaS AML and payment software solutions for banks, brokers and corporations. In the beginning of 2013, Fineksus started managing its ongoing GCC Region operations at its new office in Dubai, UAE.

Fineksus is the market leader of compliance and financial messaging solutions in Turkey by providing its products and services for more than 95% of the banking industry, and aims to expand its offerings global wide which makes the company at the forefront for providing AML solutions and financial messaging tools.

PayGate™ Financial Messaging Suite
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o PayGate™ Search
o PayGate™ Reconciliation
o PayGate™ Analytics
o PayGate™ Message SDK
o PayGate™ Converter

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