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The Philippines: A New Digital Hotspot in the Asia Pacific

Introduction

In these past two years, we've seen how the norm was challenged and how the unusual became the routine. This pandemic has indeed proven to be the great disruptor of recent times. This is not just in the medical front, but more so in the socio-economic and financial aspects. The implementation of the necessary health protocols and lockdowns has shaken up various industries and businesses on a global scale, limiting operations and restricting face-to-face transactions and interactions.

In the latest Digital Banking Maturity 2020 study conducted by Deloitte Digital, it was noted that 60 percent of legacy banks have either closed or shortened the operating hours of their physical branches, 11 percent have turned off specific account opening methods, and 6 percent chose to limit the access of new clients to particular products and services. The Philippines industry projections also reveal that 50 to 60 percent of branch-based over-the-counter transactions have disappeared and have shifted to digital platforms. These figures are just snapshots of two glaring reali-

ties that: 1) traditional brick-and-mortar banking falls short in the face of a global disruptor; and 2) digital transformation is the saving that financial institutions must embrace in order to be future-ready and pandemic-proof.

If there is one positive thing that this pandemic has forced industry leaders to do, it is to reexamine and even challenge traditional banking structures and processes. This will allow them to have a better understanding of where their institutions stand now and to determine effective strategies to employ moving forward. The situation demands newer business models and not just innovative, but intuitive solutions from financial institutions, to properly and promptly address the changing needs of the times and market. This would thus require the deconstruction of existing paradigms and mindsets making the radical shift from bricks to clicks. To move forward is to ride the wave of digitalization. And for financial institutions to survive, they must learn how to go with the flow.

Employing Game-Changing Reforms

In the Philippines, challenger banks and

new fintech players have started to reshape the country's financial ecosystem. To keep step with this influx, a number of milestone regulatory and enabling laws have been put in place at an accelerated pace. We saw the aggressive implementation of the Philippine Identification System Act (PhilSys), the National ID law, and the swift enactment of several legislative measures to further promote the Philippines' sustainable digital economy.

Priority economic measures enhancing the investment climate in the country have also been expedited. These include the amendment of various acts on foreign investments, public services, and retail trade liberalization law. The amended foreign investments act would now allow foreign nationals to own micro-, small and medium sized enterprises with a minimum paid-up capital of USD100,000, while the amended public services act allows up to 100 percent foreign ownership of such public services as telecommunications, railways, expressways, airports, and shipping industries. Under the amended retail trade liberalization law more foreign players will now be allowed in the retail market by lowering the minimum paid-up capital for foreign corporations.

On the regulatory front, the Bangko Sentral ng Pilipinas (BSP), the Philippines' central bank, has issued two landmark regulations: the digital bank licensing guidelines and the open finance framework. Their issue took place at the height of the pandemic, putting the BSP among the first central banks in ASEAN to quick-

ly issue licenses to six digital banks. Three are currently operational, while the rest are expected to go live before the end of 2022. Issuance of additional licenses for new digital banks and electronic money issuers has been suspended for three years to assess the performance of the current players. The regulator has also announced its planned central bank digital currency sandbox initiative with pilot participants within the year.

So far, we have seen two digital unicorns from the telecoms industry emerge during the hard lockdown period: Mynt's GCash and Voyager's Maya (formerly PayMaya). It is likely that two more digital players will join the elite list by 2024. This is driven by the growing interest and demand from an expanding market bolstered by the extensive financial inclusion efforts from both the government and the private sector. This is also anchored on the BSP's digital payments transformation roadmap with two strategic outcomes: first is transforming at least 50 percent of retail financial transactions to digital, and second, is onboarding 70 percent of adult Filipinos to have transactional accounts by end of 2023. Given the exponential growth in digital adoption, these goals are expected to be met even before the deadline. Meanwhile, interoperable payments through the country's national retail payments systems InstaPay and PESONet have registered unprecedented growth both in gross transaction volume and value. This was further boosted by Executive Order 170 (s2022) issued by President Duterte adopting digital payments for government disbursements and collections. This growth is expected to continue beyond the pandemic.

On the flip side, cybercrime and fraud have been on the rise. Concerted efforts by the industry to roll out massive financial education and digital literacy campaigns have been put in place to address these threats. To further promote trust and confidence among digital users, the BSP aggressively pushed Congress to quickly pass the financial products and services consumer protection act.

Enabling digital infrastructure would not be complete without giving attention to inadequate telecommunications and data provision especially in hard-to-reach areas. This awareness prompted the government to quickly implement Executive Order 127 (s2021) allowing satellite broadband in rural areas for better Internet connectivity and data network access. This order made way for the entry of Elon Musk's Starlink satellite broadband, which

made the Philippines the first country in the ASEAN region to have a facility with approximately 200 mbps capability specifically intended for Geographically Isolated and Disadvantaged Areas (GIDA).

Open Finance and Application Programming Interfaces

The open finance framework has accelerated the customer-centric product development cycle of digital finance solutions and platforms in the country by enabling banks, non-banks, fintechs, and other third-party providers to access financial data of consumers.

The digital disruption caused by a financial ecosystem largely driven by application programming interface (API) has cemented the place of digital challenger banks in this new banking landscape. The August 2020 *Banking Scene Report* reported that 480 million API calls were made in the United Kingdom for July 2020 alone, revealing the massive scale of third-party providers requesting access to a customer's bank account via APIs.

With the fast-changing financial landscape, there is no doubt that digital challenger banks are here to stay. They have emerged at the most opportune time when the confluence of technological advancement, evolving customer expectations and global disruptions have pushed the boundaries of traditional banking to new frontiers.

Generative Artificial Intelligence

Artificial intelligence (AI) has long been a cornerstone of any digital transformation. But as technology continues to evolve so does AI, which becomes smarter and more intuitive year after year. AI advancement has reached the point that it has become generative. With the wealth of data run-

ning in the cloud, it is now possible for industries to isolate, pluck out, and synthesize relevant data to come up with new products and services.

Generative AI now exposes the potential of how cloud-native data can be transformed to "synthetic data" and used to train other machine learning algorithms to customize inclusive digital products and services and even to detect fraud. Hence, AI may now identify patterns of consumer behavior, determine their pain points, and even tag suspicious digital transactions.

Moreover, generative AI has become more agile and can be scaled to perform its "policing task" even with multiple transactions happening at the same time. It is this generative function of AI that will prove useful for industries not only in addressing customer concerns almost in real-time, but also in strengthening cybersecurity measures.

Scaling of Digital Assets

Recognizing the agility and acceleration of digital payments, electronic money institutions (EMIs) and digital banks have started to venture in offering crypto investment services. Because of this, the BSP saw crypto transactions further spike in 2022 with the sustained increase in the use of virtual currencies in the payments and remittance domains as well as the delivery of other financial services. The developing positive attitude and consumer behavior of Filipinos toward digital transactions also reflect a strong indication of wider adoption of other digital financial services such as cryptocurrencies.

Based on the findings of the Philippines Fintech Report 2022, the country has also evolved as one of the "world's fastest adopters of cryptocurrency." Data from the BSP reveal that cryptocurrency transaction values booked a five-fold increase in 2020 mainly driven by the surge in the price of Bitcoins.

Moreover, a rise in crypto-friendly technology and blockchain developments has also created a dynamic and supportive environment for digital assets to flourish. This is complemented by the open mindset of regulators in understanding and, in

effect, facilitating the transforming nature of the country's digital finance landscape. The role of regulators is vital in ensuring investor protection and cybersecurity. This also instills confidence in the industry and system. In fact, Binance, the world's largest crypto exchange, will soon start operations in the Philippines. As of March 2021, the BSP has recognized 17 industry-compliant virtual currency exchanges. It also initiated collaboration with the Philippine Digital Asset Exchange (PDAX), the country's homegrown cryptocurrency exchange to start the development of a crypto regulatory sandbox.

Issuance of BSP Circular 1108 (s2021), which reiterates the regulation of Virtual Asset Service Providers (VASPs) operations in the country, redefined virtual currency exchange as virtual assets. This leads to the direct regulation of the use and exchange of cryptocurrencies or crypto assets.

Other government agency efforts have also focused on this. The Securities and Exchange Commission (SEC) is currently working on the guidelines for cryptocurrency trading in the country. With the spike of mass market interest in cryptocurrency exchange at the height of the pandemic, the SEC issued 33 advisories that inform and encourage the public to be more discerning in engaging with high-risk crypto activities to avoid scams. It also issued several cease-and-desist orders to noncompliant and unrecognized cryptocurrency operators in the country.

Keeping the digital finance industry aligned with the regulators is critical. The industry must remain supportive of the development of a crypto regulatory sandbox to better map out the future of cryptocurrency exchange in the country.

Decentralized Finance and Non-Fungible Tokens

Hand in hand with the emergence of blockchain technology is the rise of decentralized finance or DeFi. As DeFi solutions and applications continue to gain ground, the industry sees this digital revolution as another transformative driver of financial inclusion.

With decentralized finance solutions such as "smart contracts" established on

the blockchain, more traditional barriers to financial inclusion could be removed, opening more financial options and opportunities to ordinary Filipinos. This became more evident with the pandemic catalyzing the trend. As several businesses closed shop and many Filipinos lost their jobs, ordinary citizens started to see the value of non-fungible tokens (NFTs) as an investment and income-generating ventures. NFTs are virtual tokens that represent real-world items like music, art, in-game items and videos which are exchanged online using cryptocurrency. This "gold rush" in NFTs is mirrored by the sudden interest, especially in the mass market, to gamified NFT platforms like Axie Infinity.

In a report published by Business World (Lacsamana, 2022), the Philippines topped the list of 20 countries in NFT ownership. This is largely an effect of the pandemic that instantly displaced thousands of working Filipinos, including overseas Filipinos who lost their jobs, who turned to NFT-gaming platforms to earn income.

While many ordinary Filipinos still need to understand NFTs, the growing interest among the mass market suggests a bright prospect for DeFi solutions and platforms to thrive in the country.

Data Analytics for Customer-Centric Solutions

As the country moves forward with a highly interoperable financial ecosystem that mostly runs on the cloud, data generation grows exponentially. An article by Information Week reported that people generated 1.7MB of data every second in 2020. This corresponds to the flood of customer and user data available especially with the emergence of more digital banks, crypto currencies, e-wallets and e-commerce platforms. This shows that data is the new oil that can be tapped and monetized. It is high time every industry player incorporates open data in its strategies, whether for innovation or monetization, as data will only continue to be an important asset in the industry.

Data has played a big role in keeping Philippine financial institutions and other fintech players at the forefront of the inclusive digital finance push, despite the pan-

demic. In fact, the pandemic was the time when data was most valuable.

Given these technological disruptions, the whole digital finance industry realized that the most important aspects of customer-centric and inclusive digital finance always rely on the consumer's insight generated by a topnotch data analytics structure. Data analytics has enabled the digital finance ecosystem to identify the pain points of various market segments, and consequently develop tiered platforms that will specifically address customers' unique needs.

Communicating these innovations through data-driven content marketing became key to letting customers know that the technology they need to survive the pandemic and beyond is now more accessible. This is why the platforms have been contextualized, focusing on the specific journey of each customer for each market segment.

Addressing Challenges on Cybersecurity

Industry players who want the benefits of open finance and open data must also be accountable by responsibly building a sustainable ecosystem for it to flourish. This means investing in the infrastructure to make this possible. Infrastructure involves the technology, knowledge, and actual manpower needed to make open data credible, secure, and reliable.

An open-data ecosystem can only be effective with a certain level of trust among its participants. Without trust, market players and clients may opt out of the ecosystem altogether. Financial data are a particularly sensitive domain that involves a lot of regulations. This then brings to the fore the industry mandate to constantly strengthen cybersecurity measures.

To have a nimble and secure digital finance ecosystem means to invest in making the platforms and services cyber-resilient. This begins with the understanding of the current trends and technologies that will enable a more secure digital space.

A robust open-data financial ecosystem provides strong consumer protection and maintains data integrity and security across the ecosystem. It is also able to au-

tomatically detect and swiftly act on problematic or suspicious data in order to keep the ecosystem in check.

This should be complemented by a whole-of-institution approach that employs a “zero trust strategy.” This fortifies the operation of data systems and platforms in such a way that requires all users, whether within or outside the institution, to be authenticated and continuously verified before being authorized to access and use them. This includes cybersecurity drills, regular audit of devices and systems, and constant awareness campaigns on data privacy laws, compliance measures, and trends which are effective ways to safeguard financial institutions and the industry as a whole.

Depending on existing regulations that dictate the country’s level of data standardization and the breadth of data sharing, there is a lot of potential value from open data. When done right, open data will definitely take us a step closer to our goal of having sustainable inclusive digital finance and a more robust and cash-lite economy.

‘Innovation for the People’

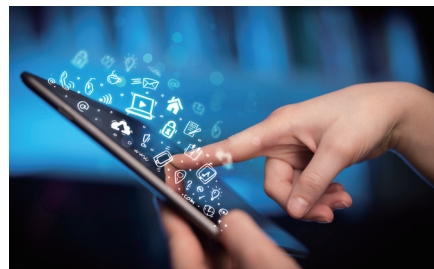
One can affirm that there is no stopping the Philippines from expanding its digital terrain and becoming one of the newest industry hotspots of competitive financial technology in the region. This is rooted in embracing an industry-wide culture that welcomes digital transformation.

By employing innovative technologies and strategies, the country has bolstered its cyber-resilient digital infrastructure. It has cultivated an encouraging financial landscape for consumers founded on trust and customer centricity. The Philippines has facilitated an enabling environment for financial institutions and other fintech players to continuously innovate and deliver hyper-personalized services that broaden the industry’s reach to the unbanked and underserved.

Ultimately, what makes the Philippines a new financial technology hotspot in the Asia-Pacific region can be summed up in one principle: “Making innovations work for the people.”

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Lito Villanueva is the Executive Vice President, Chief Innovation and Inclusion Officer of Rizal Commercial Banking Corporation (RCBC). Concurrently, he is the Chief Digital Transformation Advisor for the Yuchengco Group of Companies, one of the oldest conglomerates in Asia. He is also the founding chairman of Fintech Alliance.ph, the Philippines’ largest organization of digitally-enabled companies that generates over 90 percent of Fintech-initiated transactions volume in the country today.

Lito is the Philippines’ award-winning thought leader on digital transformation and inclusive digital finance. He has over 20 years of experience in banking, telecommunications, payments, development finance, advisory, RegTech, and Fintech. In his career, he has covered over 30 markets in Asia, Europe, Middle East, and Africa in various roles for The Economist, Land Bank of the Philippines, Philippine Long Distance Telephone Company (PLDT) -Smart Communications, Voyager Innovations, PayMaya, Inter-

national Finance Corporation of the World Bank Group, and Visa. He collaborated with regulators in promoting enabling regulations towards inclusive innovations and interoperability. As a digital inclusion and transformation advocate, he institutionalized the country’s first code of conduct and code of ethics, providing a wider industry framework towards greater consumer protection in partnership with all regulators.

Lito finished the Cambridge Intellect Leadership Programme on Digital Transformation by Design in 2019 at the University of Cambridge Judge Business School Executive Education in the United Kingdom. He also earned two graduate degrees: Master of Arts in public administration with magna cum laude honors from the University of Santo Tomas (UST) and Master in National Security Administration from the National Defense College of the Philippines as a state scholar, and its youngest graduate, thus far. His undergraduate degree is in political science also from UST.