Vietnam, Payments

Coming out of Hibernation

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Vietnam, a country in Southeast Asia with about 100 million people, where majority of the economy is driven by small businesses and substantial chunk of the population is still unbanked. Even though it is still relatively closed as an economy, it is on a path of strong integration with the Association of Southeast Asian Nations (ASEAN). The country has witnessed a push from the government to digitize its economy with its Vision 2025, which is almost coming to an end.

Substantial changes have occurred over the last five years, but what is next for the country's payments industry and broader digital economy?

The year is 2024, and it does seem like Payments industry in Vietnam have emerged from hibernation and entered a state of higher consciousness. It would be fair to say that Banks and non-banking financial technology institutions must prepare for the expected increase in the size of the digital economy.

The Payments Landscape in Vietnam leverages four major financial instruments: cash, cards, account-based payments through various digital applications and mobile wallets. This is essentially how individuals and businesses exchange money. The central bank runs the IBPS (Inter-Bank Electronic Payment System), which offers **RTGS and ACH and oversees NAPAS (National Payment Corporation of Vietnam).**

NAPAS runs instant payments, mobile switching, and ATM switch services, among others and has been instrumental in the growth of digital transactions. As more people are included in the official economy and the payments infrastructure improves, leading to improved adoption, the expectations from banks will change quickly. This change seems to be already in motion.

We believe Financial Institutions should consider the following aspects of their businesses to prepare:

1. Payments Regulatory compliance with domestic and international payments infrastructure.
2. Rebuild Technology Architecture and Operations for mid to long-term growth.
3. An approach with the broader Fintech ecosystem in Vietnam and across ASEAN

This document explores the challenges that banks and non-banking financial technology institutions face. It suggests an approach to prepare for the growth that the payments industry is expected to experience over the next half-decade.

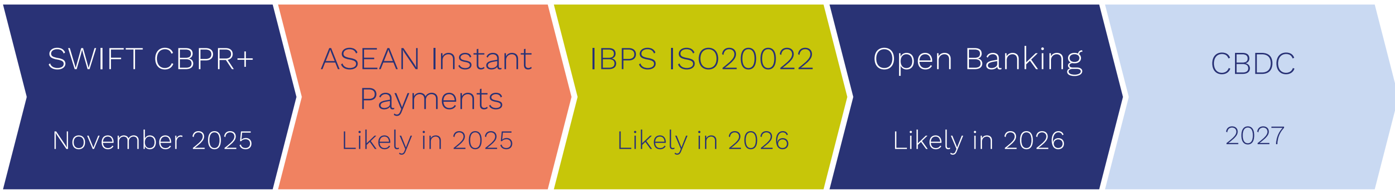
Payments Regulations Compliance; Domestic and International payments infrastructure

Compliance with regulations incurs substantial costs, and noncompliance could present risks at multiple levels for a bank, its brand, and regulators in the form of fines. Also, the cost of a potentially missed opportunity is difficult to gauge accurately.

The payments industry has become aggressive by nature - changes are relatively frequent and driven by a combination of regulators, competitors, and consumers. Hence, banks and non-banking financial technology institutions must react much faster to regulatory opportunities and leverage them to create products and services. **Orchestrating data and capabilities to create offerings positioning for growth is an asset that can differentiate a business model that generates revenue from one that just works.**

Payments regulations are fairly active both domestically and internationally. The image below describes an abstract view of the regulations that banks and non-banking financial institutions should consider regarding their payments business in Vietnam and ASEAN.

Payments regulations timelines over the next 24 months.



Regulations impacting international Payments business.

The SWIFT network is key to the global financial infrastructure; its dependency is unprecedented, and financial institutions in Vietnam are no different in this regard. SWIFT has set a deadline for banks to comply with a financial messaging standard based on a ISO20022 messaging framework. Compliance with SWIFT CBPR+ by November 2025 is probably the highest priority for FIs for their payments businesses.

SWIFT CBPR+ (Cross-Border Payments and Reporting), the term SWIFT, uses to market the change and offer an improved financial data set as part of the new messaging standard. This opens opportunities for more transparent services and possibilities of monetizing financial data with consumer consent.

Ironically, this push from SWIFT **presents an opportunity** to diversify the cross-border payments business across regional payment networks, such as the ASEAN cross-border initiative, and alternate global fintech networks, such as Thunes, Visa Direct, NIUM, and many more, that help optimize revenue margins.

There may seem to be enough time for FIs in Vietnam to comply with the SWIFT CBPR+ changes in 2024, but complying to deliver basic services and build applications to leverage the new data set will take time. Considering these factors, 15 months may not be enough, and FIs should consider moving immediately.

A more comprehensive financial data set translates to an opportunity to offer much more granular services to the FI's direct consumer base, exposing capabilities to a wider fintech ecosystem and enabling new revenue sources.

Applications are broad, from retail payments offering essential pre-validation services, credit decisioning for BNPL, data augmenting for improved trade financing, and better treasury decisions across business, commercial and corporate segments. A better data set also makes for a much better risk management infrastructure. As AI models across credit risk, AML, and anti-fraud gain transactions, a comprehensive data set would be a catalyst that can eventually be monetized. **FIs offering and processing better data sets would have an edge.**

ASEAN, Regional Instant Payments Network.

ASEAN is a strong economic block in Asia. It commands a combined nominal GDP of US $3.9 Trillion, driven by a population of 700 million. Most of the ASEAN countries run domestic instant payment clearing infrastructures that have positively impacted their economies.

The 43rd ASEAN Summit, held in September 2023 in Jakarta, resulted in an agreement to accelerate cross-border payments in ASEAN. QR payments, using Indonesian standards, Instant payments, and eventually real-time gross settlement services could accelerate cross-border transactions and trade across retail and commercial customer segments in the coming years. Vietnam officially joined the ASEAN cross-border initiative in 2023.

Financial institutions in Vietnam can probably open entirely new customer segments and business models leveraging the wider fintech ecosystem in ASEAN. This will open substantial opportunities across inclusion, retail, business, commercial and corporate segments, resulting in large transaction volumes, which would require operational capabilities for orchestration and revenue optimization. Potential business model innovation with financial technology players to distribute contextual banking services across accounts, payments, credit, investments and use cases unique to Vietnam and ASEAN are also possible.

There are two big challenges that the banks must solve. The first is a technology architecture that will allow them to collaborate at speed and offer granular data and payments, credit and accounts capabilities. The second is the ability to manage and orchestrate the payments volumes across all channels direct or through Fintechs to optimize revenue.

The fact is that most financial institutions, both banks and non-banks, in Vietnam are not ready for this opportunity, but the FIs who are ready are likely to experience a major growth spurt in the coming years.

Reference - ASEAN website

Preparing for Domestic Payments Regulations in Vietnam.

State bank of Vietnam governed (SBV), Inter-Bank Electronic Payment System (IBPS) with high value RTGS, low value file-based clearings and NAPAS driven instant payments services are the major drivers of accounts-based payments in the country. These cut across almost all segments of the economy. Transaction volumes from cash use and some from cards is expected to move to accounts as QR payments with NAPAS are adopted further.

The SBV governed domestic payments schemes still runs with legacy financial messaging standards and complex closed processing flows. It works but is not really equipped for a world where leveraging data is considered a revenue strategy.

We believe the country is ripe for a domestic large-value payments infrastructure modernization and this is likely to occur over the next 18 months. This aligns with Vietnam's vision of a largely digital economy.

Vietnam does not have official open banking regulations or an open banking framework, but even a vague set of guidelines that help reduce barriers to entry for new players has spawned multi-billion US-dollar industries in other countries. Europe, the UK, Saudi Arabia, and India are examples of this approach, and it is the first and a very critical step to more embedded financial services in the economy. We believe regulators in Vietnam might be considering this in some form.

Central Bank Digital Currencies (CBDCs) are seen as a natural evolution to a physical fiat currency in a country, and Vietnam has been exploring the idea since 2021. As the world moves towards tokenization of assets, both physical and digital, a currency that can keep up with these changes is essential for a country. CBDC seems to be the promise and it seems to feature in the countries' long term digital strategy.

China, India, Indonesia and many other countries in Asia are pioneering the technology and application of CBDCs. Vietnam will have the opportunity to choose what works for her. Payments using CBDC will have to be run on a very different tech stack, one that understands an encrypted currency stored as a token and can run on a distributed ledger but also has capabilities to be interoperable with traditional fiat-based infrastructure in the short to midterm. The applications are spread across retail and wholesale use cases, depending on the priority of the country and have the potential to impact domestic and international trade.

Open banking regulations is a term that loosely refers to a framework of exposing customer data with consent and payments initiation capabilities to external fintech ecosystem (and other players), that aids innovation and better, transparent more convenient services for customers. Vietnam has a vibrant digital wallet ecosystem which is growing well but integration into the official banking industry is limited.

Rebuild Technology Architecture and Operations for Growth.

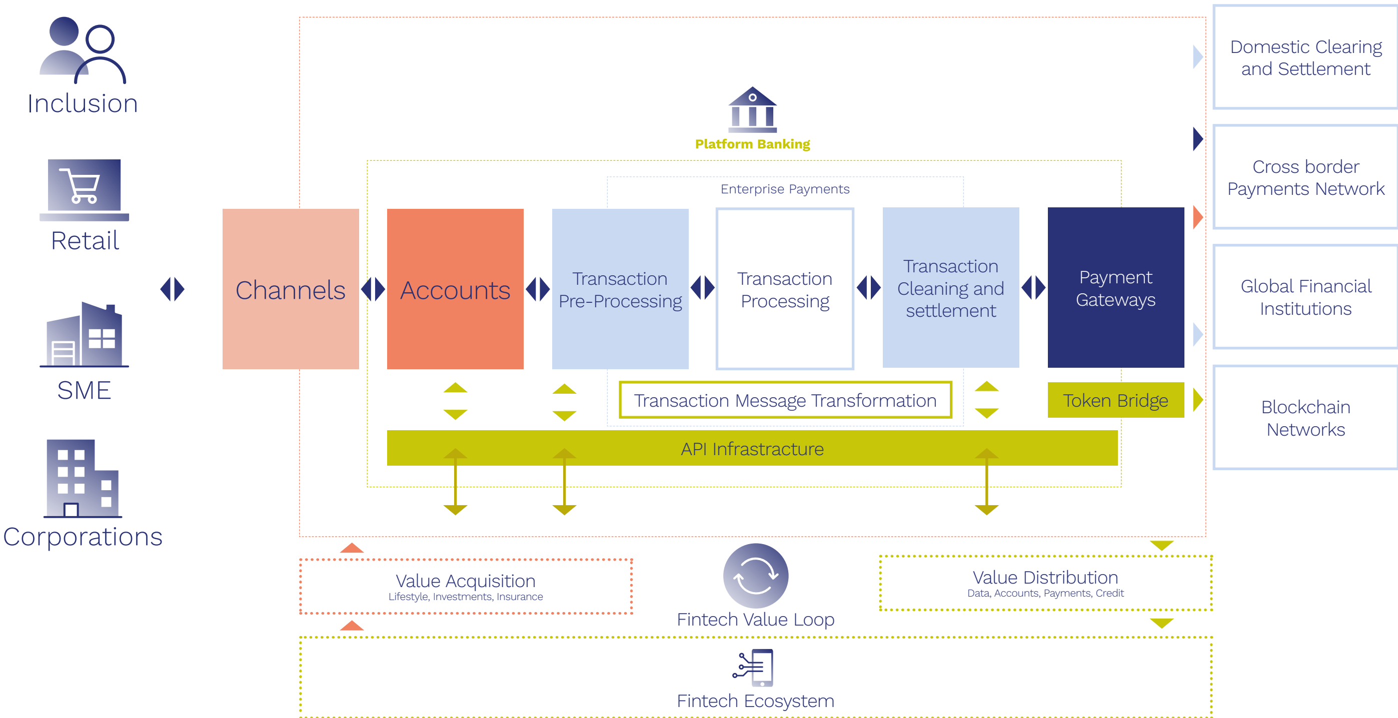
Most of the banking industry in Vietnam runs on legacy payments processing technology *(as observed in year 2024),* at least a decade old if not older. This poses a substantial risk for banks to leverage current and upcoming opportunities driven by either regulations, competition or customers expectations.

The shift in customer segments between people moving from financial inclusion into traditional retail, business and commercial segments is eminent with government initiatives and economic growth. This would mean higher transaction volumes, much more complex operational needs, and faster reaction time for collaborations with external fintech ecosystem. It is believed that some banks in the country take about one second to process a transaction. Considering that the processing standards in the digital world are high, with processing speeds of 250 transactions per second, considered slow. FIs in Vietnam probably are losing a lot of revenue due to technology architecture and operational complexities.
Transaction processing capabilities need to be strengthened to accommodate changes faster in terms of minutes and hours instead of months and quarters. Flexibility to leverage data elements and capabilities to make business decisions and offer services, embedded or direct, is essential to the survival and growth of FIs.

The speed and cost of making these changes have proven to impact revenue margins on each transaction and could mean the difference between a healthy balance sheet and a stressed transaction banking business.

The technology stack of well-run banks looks more like a platform than a set of basic banking applications. It is heavy on APIs, leveraging the smallest of data elements to create curated product and services that have the potential to generate revenue on their own. The platform stacks are capable of processing huge transaction volumes, scaling quickly across existing and new customer segments. Transaction volumes in Vietnam are likely to double over the next few years, with customers moving between various segments, and banks will have to be able to cater to this growth and cross flow within the customer segments. Financial institutions will have to navigate the complexities of building a technology and operational infrastructure to support a varied set of payments systems across various business needs, speed, and cost to market building a potential differentiation.

An appropriate approach is to consider a model where FIs start to build a Platform architecture that works as an enabler to its direct customer and a wider financial technology ecosystem.

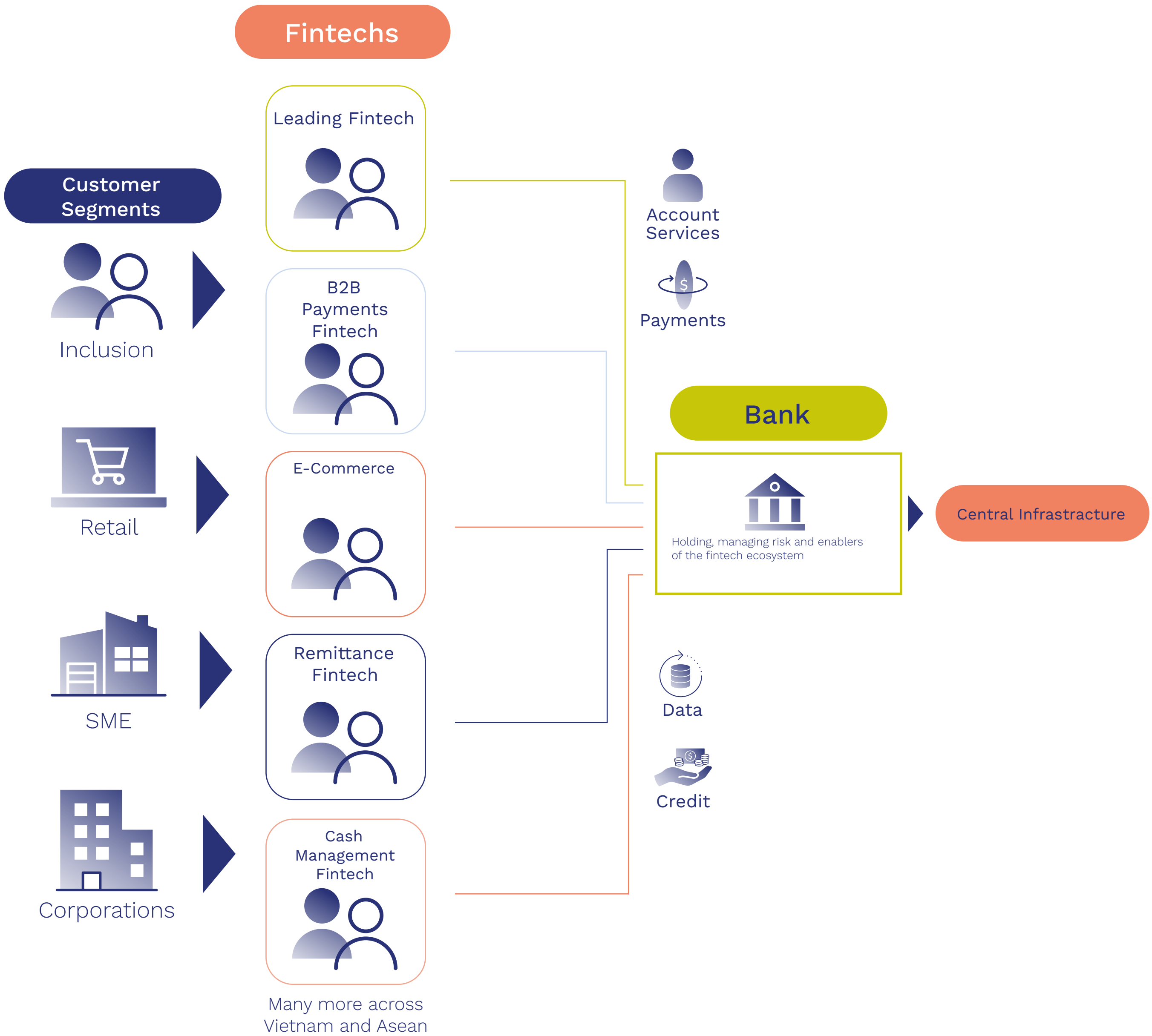


An Approach for Growth with the wider Fintech ecosystem in Vietnam and across ASEAN

Financial institution will have become Platforms that will eventually be the holders of the risk and enablers of the financial services, the distribution of these services will move towards the Fintechs. This sentiment has been getting stronger across the world and the regulators and FIs are budling and preparing in this direction.

Banks will have to be able to offer capabilities for account, payments, credit needs across various customer segments. Embedding these services within customer journey either distributing directly in a conscious banking model where the bank is visible in the journey or in a contextual banking model where distribution is through Fintech, and other players and banks are not visible to the consumer.

These varied models will allow banks to acquire transaction volumes from indirect channels, eventually impacting the bottom line. An approach with Fintechs as a distribution channel represents substantial growth opportunities for FIs across Vietnam and ASEAN.



Conclusion

The payment transaction volume that a bank processes is tightly linked to the revenue it generates, either directly through fees and surcharge, or an exceptional consumer experience that impacts the overall revenue per customer or even through fintechs which provide access to entirely new revenue models.

Payments is mission critical for the banking business and Enterprise Payments Processing takes major investments from Operations, Technology, Regulatory Compliance and Business teams at the bank for it to be effective for growth. Retail, Business (SME) and Corporate banking have led the focus for payments, but as banking evolves, we see a new consumer segment that banks must cater to Fintechs; combining that with the capabilities that these fintechs can offer to banks creates what we call a The Fintech Value Loop.

Temenos Payments can contribute to financial institution's build across regulations, operations, technology, and fintech strategies for mid to long-term growth. Reach out for more.

About Temenos
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