

POLICY POINTER

August 2024 | ENG

Ensuring the Success of PAPSS - Overcoming Challenges for a Unified African Payment System

The Pan-African Payment and Settlement System (PAPSS) is a transformative initiative under the African Continental Free Trade Area (AfCFTA), designed to streamline cross-border payments and facilitate intra-African trade. PAPSS aims to reduce the continent's dependency on foreign currencies by allowing businesses to settle transactions in their local currencies. By doing so, it promises to reduce transaction costs, mitigate foreign exchange risks, and improve trade efficiency. Despite its potential, PAPSS faces numerous challenges that hinder its progress. These include governmental hesitancy, infrastructure fragmentation, currency volatility, and technological limitations. Additionally, businesses continue to prefer stable foreign currencies, further complicating PAPSS implementation. Unless strategic adaptations are made, PAPSS may struggle to achieve its full potential.

Key Challenges to PAPSS Implementation 1. Government Hesitancy and Policy Reluctance

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Governments across Africa are hesitant to fully adopt PAPSS due to concerns about relinquishing control over monetary policy. Central banks, in particular, are cautious about integrating their systems with PAPSS, for the fear that it may limit their capacity to manage inflation and currency volatility. This is especially relevant in countries with less stable currencies. There is a reluctance to surrender control of their financial systems, despite the potential benefits of increased trade efficiency. Additionally, regulatory differences among countries create obstacles for the harmonization of payment systems. Each nation has its own financial regulations, data privacy laws, and security standards. Harmonizing these the different financial regulations in the various countries under a unified payment system presents significant challenges. Ensuring compliance across borders is complicated and requires ongoing coordination, which has slowed down PAPSS adoption.





2. Currency Volatility and Business Preferences

African businesses remain cautious about conducting trade in local currencies. The high volatility of many African currencies, coupled with inflation concerns, makes businesses wary of using PAPSS for cross-border payments. Most prefer to trade in hard currencies, like the U.S. dollar or euro, which are globally accepted and perceived as more stable. Even with PAPSS, businesses are concerned about the risks associated with currency fluctuations and exchange rate instability, which could negatively impact profitability.

The lack of proper currency hedging mechanisms further compounds this problem. Without tools to protect businesses from exchange rate fluctuations, many companies are reluctant to embrace a system that requires them to settle transactions in local currencies. This creates a significant barrier to PAPSS adoption, especially for small and medium-sized enterprises (SMEs), which are particularly vulnerable to currency risk.



3. Technological and Infrastructure Gaps

The successful implementation of PAPSS requires robust digital infrastructure, which is unevenly developed across African countries. While some nations, such as South Africa and Kenya, have advanced financial technologies, others face substantial challenges in terms of internet penetration, digital literacy, and financial inclusion. Countries with underdeveloped digital infrastructure struggle to fully integrate with PAPSS, impeding the system's seamless adoption.

Moreover, the technological infrastructure supporting payment systems in many African countries is fragmented, making it difficult to harmonize different financial networks. Centralized payment systems and digital banking infrastructure vary widely across the continent. Limited access to reliable and affordable internet, especially in rural areas, further restricts the potential of PAPSS to reach its full scale.

4. Cybersecurity Concerns

As digital payment systems grow, so does the risk of cybersecurity threats. Many African countries are ill-equipped to defend their financial infrastructure from cyberattacks, making them vulnerable to disruptions. PAPSS, being a cross-border digital system, is exposed to potential cyber risks that could destabilize its operations. Without adequate cybersecurity protocols and investments in cyber defense, PAPSS faces a risk of data breaches, fraud, and disruptions that could erode trust in the system.



5. Complexity of Currency Conversion and Exchange Rate Risks

PAPSS allows transactions in local currencies, but managing the conversion between 42 African currencies is an inherently complex task. The differences in currency value, coupled with fluctuating exchange rates in the different countries, create complications for cross-border trade. Businesses are uncertain about the cost implications of converting their local currency to that of a trade partner, and the risk of sudden exchange rate shifts could impact profitability. Although PAPSS aims to mitigate these risks, the current absence of currency hedging solutions leaves businesses exposed to potential financial losses. Recommendations for Ensuring the Success of PAPSS



6. Foster Public-Private Partnerships (PPP)

Governments and PAPSS should work closely with private financial institutions, fintech companies, and industry stakeholders to accelerate the adoption of the system. Public-private partnerships can lead to innovative solutions, such as integrating trade finance, mobile banking, and peer-to-peer finance services that cater directly to the needs of African businesses. These partnerships can also expand PAPSS's reach by involving non-bank financial institutions, ensuring broader adoption and usability.

7. Incentivize the Use of Local Currencies

Governments must introduce incentives to encourage businesses to trade in local currencies. Financial incentives, such as reduced transaction fees, tax breaks, or regulatory exemptions, should be offered to businesses that use PAPSS for cross-border payments. Additionally, PAPSS should develop currency hedging mechanisms to protect businesses from the risks associated with currency fluctuations, making local currency transactions more attractive and secure.

8. Expand Education and Awareness Campaigns

Many businesses are still unaware of the potential benefits of using PAPSS. To address this, targeted education campaigns should inform businesses about the advantages of PAPSS, such as faster payment settlements and reduced reliance on foreign currencies. These campaigns should also address concerns about currency volatility and provide real-world examples of successful PAPSS transactions to build trust among businesses.

9. Enhance Cybersecurity and Data Governance

A major priority for PAPSS must be investing in cybersecurity infrastructure to protect the payment system against potential threats. Governments, in collaboration with the private sector, should implement robust data governance frameworks and cybersecurity protocols to secure PAPSS operations. By adopting international best practices for cybersecurity, PAPSS can build trust and encourage wider participation among businesses and financial institutions.



10. Develop a Phased Virtual African Currency

Over the long term, PAPSS could explore the development of a virtual African currency to facilitate cross-border payments and reduce reliance on foreign exchange. This digital currency could be introduced in phases, starting with regional digital currency zones, before moving towards a continent-wide currency. This phased approach would help PAPSS better address regional economic realities and establish a strong foundation for eventual continental integration.

11. Improve Technological Integration and Infrastructure Development

African governments, with support from international organizations and private partners, must invest in infrastructure development to bridge the digital divide and ensure all countries can participate in PAPSS. This includes upgrading internet connectivity, improving financial literacy, and expanding access to digital banking services, particularly in underdeveloped regions. These improvements are critical for increasing PAPSS's adoption across Africa. Finally, the successful implementation of PAPSS is critical to the realization of AfCFTA's full potential. By addressing the concerns of governments, businesses, and the wider financial community, PAPSS can become a transformative platform for African trade. However, this requires strategic adaptation, including building public-private partnerships, incentivizing the use of local currencies, and enhancing cybersecurity. With sustained efforts, PAPSS can overcome the challenges it faces and help Africa take a leading role in global trade by facilitating seamless, efficient, and low-cost cross-border payments.

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