

THE IMPACT OF DIGITAL PAYMENTS ON THE GROWTH OF CASHLESS PAYMENTS AND THE FACTORS LIMITING ACCESS TO FINANCIAL SERVICES

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***Abstract.** Most countries worldwide are undergoing digitalization, with the adoption of non-cash payment methods accelerating. In recent years, the population and economic entities in our country have readily embraced the use of digital technologies. Organizing new methods of innovation is a key priority in the pursuit of strengthening the financial stability of the banking system. The introduction of new technologies serves as an effective tool for improving production potential, providing financial support, and stimulating entrepreneurship. Ensuring the reliability and security of the payment system, enhancing the efficiency and speed of payment operations, expanding financial inclusion by providing the population with access to payment services, minimizing the volume of cash circulation, and organizing and promoting new methods of innovation in the payment market. The application of financial technologies, especially in payment services, enables market participants to conduct their payments conveniently, safely, and at low cost. It allows for a broader involvement of economic cycles in the banking sector, limits the informal economy, and increases banks' credit resources and financial intermediation.*

***Keywords:** banking sector, digital payment, financial services, financial intermediation, payment cards.*

INTRODUCTION

In recent years, a number of serious steps have been taken in Azerbaijan in the direction of maintaining macroeconomic stability, forming a favorable business environment and developing non-oil sectors, and reforms have been continued. Strategic roadmaps for the national economy and the main sectors of the economy, many state programs have been adopted, economic development goals for the near, medium and long-term perspective have been defined. Building a digital economy takes an important place among these goals. The development of the digital economy will lead to wider involvement of economic cycles in the banking sector and will multiply the investment and lending opportunities of the sector, and provide access to sources of financing. Renewal of production capacity, increase of fixed capital, finding new forms and mechanisms of investment attraction for modernization of production, will stimulate growth of economic activity and investment opportunities. The deep reforms initiated in the economy have created a favorable opportunity for the formation of a new development model and the achievement of sustainable economic growth. In such circumstances, ensuring the transition from the “capital accumulation” based model to the “effective” based growth model (Azerbaijani Government, 2016) is considered the most important strategic challenge of the new era.

The historical services of the Great Leader Heydar Aliyev, who has independent organization, management skills and phenomenal analytical thinking, are invaluable. The

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National Economic Development Strategy, which was founded by Heydar Aliyev, is successfully continued by Ilham Aliyev. The follower of H. Aliyev's policy, political heir, courageous and heroic statesman, President of the Republic of Azerbaijan Commander-in-Chief Ilham Aliyev played an unparalleled role in the formation and establishment of the Oil Strategy. In the last 20 years, the strategic goals set by the President of the country, Ilham Aliyev, have been achieved. During this period, the economy of Azerbaijan increased by 4 times, the non-oil sector by 2.8 times, and the non-oil export by 4.1 times. Strategic currency reserves exceeded 65 billion dollars as of 01.06.2023. The main purpose of the Digital Payment System is to ensure continuity of the payment service. Most countries of the world are moving towards digitalization, the use of non-cash payment methods is spreading faster. The changes in the digital payment system, the availability of non-cash payments in the payment system to the financial services of the population and enterprises, increase the relevance in the financial sector. The COVID-19 pandemic has spurred the adoption of digital payments internationally. In recent years, the population and economic entities in our country have readily embraced the use of digital technologies. Electronic money is considered safer and more convenient than physical currency, facilitating quick and efficient financial transactions. This approach aims to minimize the risks associated with banking transactions, ensuring the reliability of the payment system and the security of non-cash payment instruments. Additionally, it seeks to enhance the efficiency and speed of payment transactions by reducing associated costs, promoting financial inclusion by ensuring widespread access to payment services, and fostering innovation in the payment market within the digital economy.

The establishment of a digital economy holds a significant role in fortifying the financial stability of the banking system. The application of digital technologies in payment services enables market participants to conduct their payments securely and conveniently. This, in turn, contributes to broader involvement in economic cycles within the banking sector, restricts informal economic activities, and augments banks' credit resources and financial intermediation. In Azerbaijan, several legislative acts have been enacted in recent years to expand non-cash payments and enhance transparency in the economy. The implementation of new laws in this direction creates fresh opportunities. Key objectives include expanding the non-cash payment environment among the population and business entities, as well as state structures, while simultaneously minimizing the volume of cash circulation.

Overall, these initiatives underscore the commitment to embracing digital advancements, fostering financial stability, and driving economic growth through a more efficient and transparent payment ecosystem. The application and expansion of digital payment technology will lead to a reduction in cash-related costs, a systematic provision of the tax base, as well as access to financial services for market subjects, an increase in investment and credit opportunities for the banking sector in general, and ultimately economic growth.

Within the framework of the State Program, the range and volume of electronic banking operations will expand, the proportion of the population using electronic banking will increase, and the growth of the volume of electronic commerce will accelerate the de-cashing of the economy. This will significantly contribute to the increase of budget revenues and the standard of living of the population. It should be noted that banking services are the central link in the financial system and reflect the processes taking place in the economy as a whole, including in

individual areas, in providing the material and technical base of reproduction. The limitation of banking services restricts the participation of legal and natural persons in the reproduction process, as a result of which the chain of transmission of the product produced in the real sector to the final consumer loses its effectiveness.

RESEARCH METHODOLOGY

Creating a stable system in the banking services market and strengthening its integration into the real sector are considered among the main challenges facing the economy of Azerbaijan. One of the critical factors for ensuring the development of the non-oil sector in Azerbaijan is the availability of investment sources. This, in turn, necessitates efficient operations in the banking sector. A key indicator of the successful functioning of the banking sector is the level of access to financial sources among the population. Thus, increasing financial inclusiveness among the population and lending substantial amounts of funds circulating in the economy to the real sector are directly possible as a result of the effective functioning of the banking sector.

The rapid adoption of modern technologies in financial payment services creates conditions for market participants to make their payments comfortably and safely, enabling a broader involvement of economic cycles in the banking sector and an increase in banks' credit facilities. Limited access to financial resources – on one hand, causes the banking sector to be deprived of sufficient funds circulating in the economy, and on the other hand, does not allow the revitalization of the non-oil sector. The size of the amount of cash in circulation limits not only the country's economy but also the financial intermediation of the banking sector to a large extent. In the last 15 years, special importance has been given to the intensive use of the possibilities of the National Payment System (NPS) among businesses and the population. In 2022, the total volume of payments made through the Real-time Interbank Settlement System (AZIPS) and the Small Payments Settlement Clearing System (XOXKC), which are the main components of the system, reached 341.9 billion Manat (2.6 times of GDP). The number of payments in 2022 was 97.2 million, representing an increase of 37% in the number and 57% in the volume of bank transfers compared to 2021.

In AZIPS, the total volume in 2022 was 300.1 billion Manat, with 1358.6 thousand payment documents processed, amounting to AZN. Compared to the previous year, the volume of operations increased by 63.3% (116.3 billion manats), and the number increased by 22% (245.6 thousand units). The average amount of each payment document processed by the system was 220.9 thousand manats. In XOHKS, an important component of the payment system, 95,896 thousand payment documents with a total volume of 41.9 billion manats were processed. Compared to the previous year, the number of transactions increased by 37.7% (26,257.6 thousand pieces), and the volume of transactions was 8.0 billion manats. There was an increase, and the average amount of each processed payment document was 437.3 manats.

DISCUSSION

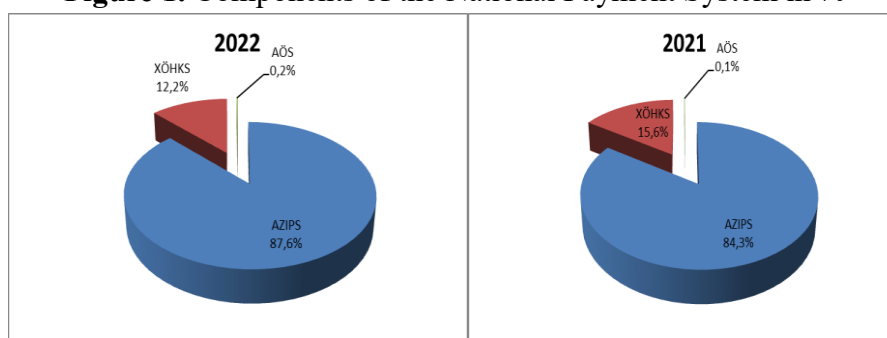
In recent years, one of the modern payment trends, the Instant Payment System (IOS) and the blockchain-based Digital Identification System have been created, the card infrastructure has been improved, and the possibilities of non-cash payments have been increased. For the first time in the country, “smart student cards” with payment functionality

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have been issued to students in the education system. The implementation of this mechanism allows to expand of infrastructure capabilities and offers innovative payments to customers. As a result of the convenience and safety of non-cash payments, the radical change in the financial behavior of the population, the emergence and application of modern innovative payment channels, realizes the possibility of rapid growth in the dynamics of digital payments.

337.3 thousand payment documents with a total volume of 549.6 million manats were processed in the Instant Payment System (ISP) launched on 01.01.2023. Compared to 2021, the number of operations has increased by 2.9 times (220.3 thousand units). In the total volume of payment documents processed in the payment system for 2022, AZIPS had a special weight of 87.6%, XÖHKS 12.2%, and AÖS 0.2%

Figure 1. Components of the National Payment System in %

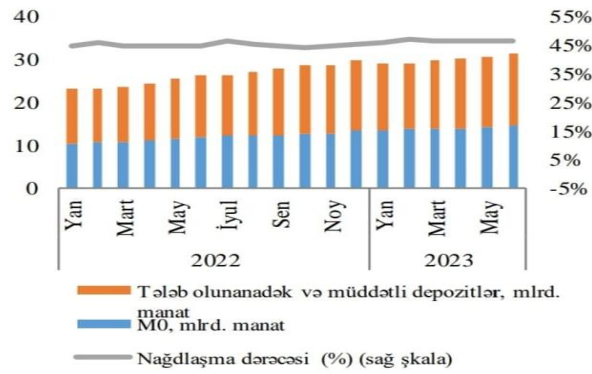


Source: Prepared by the author based on Central Bank Statistics

As a result of the work done in the direction of the development of cashless payments, the pace of development during 2022 was higher than in previous years. As of 01.01.2023, the number of payment cards in circulation is 13.6 million. Units, the number of ATMs was 3 thousand, and the number of POS-terminals was 79.8 thousand. During the reporting period, the volume of non-cash transactions with payment cards within the country increased by 2.1 times to 24.4 billion. Formed manat. The number of e-commerce transactions in the country has increased by 2.4 times and its volume by 2.5 times compared to 2021. The specific weight of non-cash payments made with payment cards in the country increased by 11.4 percentage points compared to last year and was equal to 43.2%. During the reporting period, the volume of transactions carried out through internet banking services increased by 50% compared to 2021, and the volume of mobile banking transactions increased by 3 times. (CBAR, 2022)

One of the main problems of the banking sector is the lack of alternative financial institutions in order to eliminate the limitation of financial inclusion among the population. In the world experience, the creation of alternative financial institutions to traditional banks is encouraged to involve the population in the financial-banking system and, in parallel, to diversify the banking sector and the economy. Although such organizations differ according to the characteristics of the countries, they are essentially the same and aim to include large amounts of money flows outside the banking sector into the general financial system of the country and provide cheaper loans to the real sector by providing access to financial services for the population (Zeynalov, 2021). The intensity of access to financial services has a positive effect on the demand for banking services and economic activity along with the improvement of the population's well-being.

Figure 2. Cash flow (M0/M2)



Source: Central Bank Monetary Policy Review 2023 January – June

The specific weight of cash money (M0) in manat broad money (M2) was 46.3% by the end of the period (CBAR, 2023). Due to the convenience and speed of non-cash payments, radical changes have taken place in the socio-economic landscape of cash in several countries.

With the advent of mobile phones and innovative payment channels, the dynamics of digital payments are rapidly increasing. According to the 2020 edition of the World Payments Report (World Payments Report 2020), "over the last year, the volume of non-cash payments made via the Internet increased by 14.1%, and the volume of payments made by mobile phone increased by 8.1%. At the same time, in 2020, although the size of the world economy shrank due to the COVID-19 pandemic, the volume of cashless payments made through electronic commerce increased significantly. Thus, a 62.4% increase in the volume of credit card transactions and a 52.7% increase in debit card transactions were observed in electronic commerce" (CBAR, 2023).

The low level of financial literacy among the population and lack of knowledge about the advantages of digital payments have a negative impact on the use of these services. A study conducted by the World Bank shows that "interest in opening bank accounts in Azerbaijan is significantly less. Financial literacy is lower in regions and rural areas, especially among housewives and elderly population groups" (CBAR, 2023). The weak competitive environment and low level of financial literacy in the digital payment system, high cash circulation outside banks ($M0/M2=46.3\%$), and the rapid expansion trend of the monetary base (2 times in the last 5 years) are factors limiting the development of cashless payments and access to financial services. (Zeynalov, 2021).

At the same time, the weak development of financial markets, the high cost of digital payments, poor use of payment facilities by business entities and population groups, and a number of other factors significantly impact the volume of digital payments. Cyberattacks and money laundering also pose serious risks when using electronic money. It is crucial to continuously implement various projects aimed at increasing access to cheap and convenient financial services for the population and businesses in the country and increasing the volume of non-cash payments. For the diversification of the banking sector and the economy, the creation of alternative financial institutions to traditional banks will create the possibility of attracting large amounts of financial flows outside the banking sector to the banking circulation and providing cheaper loans to the real sector by ensuring the population's access to financial services.

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CONCLUSIONS

In conclusion, the application of new technologies emerges as a powerful tool for enhancing the qualitative aspects and increasing the production potential of a nation. By extending innovative payment services to customers, there is a positive impact on mobilizing internal financial resources and reducing the high cost of credit resources within the banking sector. Furthermore, the improvement of economic management mechanisms, with a heightened focus on formulating sectoral development strategies grounded in the economic and labor potential of distinct regions, stands out as a priority issue. The overarching goal is to foster economic growth and entrepreneurship stimulation. Addressing the pressing matter of financial accessibility for both businesses and households is paramount. Establishing a robust connection between the real and banking sectors requires concerted efforts, including collaboration with international financial institutions such as the International Monetary Fund and the World Bank.

Urgent monetary reforms are essential in this context. To expand financial inclusion in the banking services market and deepen financial intermediation, building trust in the financial sector and ensuring transparency are foundational. Measures to develop the capital market play a crucial role in this endeavor. The organization and promotion of innovative methods in the payment market, especially those facilitating access to non-cash payments, represent a key priority. This involves fostering confidence, transparency, and regulatory frameworks covering the legal and security aspects of digital payments to ensure the stability and security of the payment system. Creating a stable system in the banking services market and reinforcing its integration into the real sector are imperative. Diversifying investment sources becomes a strategic approach for the banking sector to minimize risks effectively. Lastly, the rapid, efficient, and secure adoption of innovative innovations in digital payments and electronic banking services necessitates ongoing efforts to educate the population and enhance financial literacy periodically. This holistic approach ensures the sustainable growth of the economy, supported by a well-functioning and resilient financial ecosystem.

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