

Policy Briefing

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PAPSS – What Is It Good For? Probably Plenty

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Recommendations

- Central banks, Afreximbank and the AfCFTA Secretariat should foster transparent collaboration and advocacy to increase PAPSS adoption.
- AU member states and RECs should accelerate initiatives to harmonise regulations across African countries to facilitate smoother cross-border transactions.
- AU member states in collaboration with the private sector must invest in digital infrastructure to ensure broader access to PAPSS, particularly in underserved areas.
- AU member states and RECs must address currency conversion challenges by promoting monetary convergence and transparent exchange rate mechanisms.
- Robust cybersecurity and risk management practices should be implemented to secure PAPSS transactions.

Executive summary

The Pan-African Payment and Settlement System (PAPSS) is an innovative financial infrastructure designed to streamline cross-border payments across Africa using local currencies. Spearheaded by Afreximbank and supported by the African Continental Free Trade Area (AfCFTA) Secretariat, PAPSS aims to enhance intra-African trade by reducing reliance on foreign currencies, lowering transaction costs and increasing financial inclusion. Despite its promising potential, PAPSS faces challenges, including interoperability issues, low awareness and varying regulatory frameworks across countries. Addressing these issues through harmonised regulations, digital infrastructure development and robust cybersecurity measures is essential for the system's widespread adoption. PAPSS offers opportunities for greater economic integration, transparency in trade transactions and access to new markets, especially for small and medium-sized enterprises. However, successful implementation will require sustained collaboration between central banks, Afreximbank and regional economic communities to foster a harmonised financial ecosystem. Enhanced advocacy, transparency in transaction data and stronger risk management practices are also critical to unlocking PAPSS's full potential for driving Africa's economic growth.

Introduction

In the intricate web of modern finance, payment and settlement systems form the backbone of economic activity, ensuring smooth fund transfers and market stability. Historically, these systems have evolved to support various transactions, from individual purchases to large corporate trades, with banks playing a central role as intermediaries. Banks facilitate the exchange of funds, manage risks and provide the infrastructure necessary for secure and reliable transactions, thereby maintaining the integrity and efficiency of financial markets. The Bank for International Settlements and the Financial Stability Board (FSB) underscore the critical role of banks in these processes.

In Africa, payment systems are primarily overseen by the Association of African Central Banks (AACB), which plays a key role in coordinating and harmonising these systems across the continent. Despite this oversight, cross-border payments in Africa have traditionally faced significant challenges, including high transaction costs, slow processing times, limited access and a lack of transparency. Addressing these issues by implementing faster, cheaper, more transparent and inclusive payment solutions could significantly enhance economic growth, boost intra-African trade and promote development and financial inclusion across the continent.¹ According to the FSB, cross-border payments sit at the heart of international trade and economic activity.²

1 FSB, 'Cross-border Payments.'

2 FSB, 'Cross-border Payments.'

The motivation and necessity for, and intended impact of, PAPSS

Intra-African trade holds much potential, with digital trade and e-commerce, for example, constituting important opportunity areas. However, trade among African countries faces many traditional impediments, such as logistical shortcomings, low internet penetration rates, limited access to finance and weak data management and governance. Africa also faces challenges with the interoperability of payments, including fragmentation of payment systems across different countries and regions, a lack of standardisation and harmonisation in legal and regulatory frameworks, and limited availability of digital infrastructure, such as broadband connectivity and mobile networks. Addressing these challenges could help to enhance intra-African trade.

Interoperability in the context of payments refers to the ability of different products or systems to work together without encountering obstacles. Specifically, in payments, interoperability enables users to conduct electronic payment transactions conveniently, affordably, swiftly, seamlessly and securely. Fundamentally, interoperable payment systems facilitate smooth interaction between two or more proprietary platforms, allowing providers to exchange payment transactions. This ensures that users can access and utilise payment services efficiently across various platforms, enhancing convenience and accessibility in the payments landscape.³

There are various initiatives, such as the regional payment and settlement systems implemented at a regional economic community (REC) level, which aim to address the interoperability challenges in African regions. PAPSS aims to facilitate interoperability among these regional systems. In October 2023, a multi-sector focus group, hosted by Tutwa Consulting Group under a USAID-funded Africa Trade and Investment Program, explored the challenges and opportunities related to interoperability in cross-border payments, particularly within the context of PAPSS.⁴ Overall, the programme underscored the importance of harmonised and standardised payment systems across the continent to benefit from digital trade and e-commerce under the AfCFTA.

PAPSS is a financial market infrastructure (FMI) that enables instant payments across Africa, in local currency. Led by the African Export and Import Bank (Afreximbank) and supported by the AfCFTA Secretariat, PAPSS is expected to boost intra-African trade through the transformation and facilitation of payments, clearing and settlement for cross-border transactions.⁵ PAPSS launched its pilot phase in the West African Monetary Zone (WAMZ) in 2022 and is expected to be fully operational by 2025. However, concerns

3 Roger Tafotie, 'The Pan-African Payment and Settlement System (PAPSS),' *Interoperability in Fast Payment Systems* (Focus note, World Bank, Washington, DC, 2021).

4 Hosted by Tutwa Consulting Group under the Africa Trade and Investment Program funded by USAID.

5 Afreximbank, 'Pan-African Payment and Settlement System Launched by President Akufo-Addo Foreseeing \$5 billion Annual Savings for Africa,' press release, January 13, 2022.

about the feasibility of the proposed PAPSS timeline have arisen due to what has been called a premature launch without a functioning system and the lack of a demo during the WAMZ pilot, which relied on limited PowerPoint presentations and failed to motivate stakeholders.⁶

PAPSS was inspired by the desire to enhance intra-African trade by addressing the challenges related to cross-border payments. Traditionally, transactions between African countries have been undertaken in US dollars and Euros, thereby requiring central and commercial banks to hold (excess) reserves of these foreign currencies. In contrast to global trade, intra-African transaction costs are higher and processing times longer. This is sometimes attributed to a reliance on financial policies and systems outside the continent.⁷ PAPSS aims to streamline intra-African transactions by allowing payments to be made in local (African) currencies. This has the potential to compete with international payment systems and close the gap in transaction costs between global and continental trade.⁸ Since PAPSS makes payments in local currencies, there is a case to be made for commercial banks being able to reduce their reserve holdings. Nonetheless, central banks will still bear the risks and costs of exchange rate depreciation against major (non-African) trading partners.⁹

PAPSS is a crucial intervention to support the AfCFTA, as it encourages African countries to trade more with each other – assuming lower transaction costs. The potential value that will be unlocked by PAPSS includes increased trade volumes, greater economic integration and enhanced financial inclusion. In addition, it may open new market opportunities for small, medium and micro enterprises (SMMEs), including informal, cross-border traders. PAPSS also helps to improve liquidity management for commercial banks and provides better oversight and transparency in cross-border trade, assisting policymakers to track small-scale transactions that often go unrecorded.¹⁰ Through these mechanisms, PAPSS could play an important role in driving economic growth and development across the continent.

While PAPSS presents a key initiative to address various interoperability issues facing the continent, more needs to be done in terms of advocacy and sensitisation on the initiative. Efforts are being made by various stakeholders, including governments, central banks, commercial banks, payment service providers, corporates, SMMEs and traders involved in cross-border transactions, to address the issues related to interoperability and payment systems. The AfCFTA market would benefit greatly from harmonisation of these efforts, resulting in easier, more consistent trading processes.

6 Interview with digital infrastructure official, June 10, 2024.

7 PAPSS, 'Connecting Payments. Accelerating Africa's Trade'; International Trade Administration, 'Pan-African Payment and Settlement System,' press release, May 11, 2022.

8 'New Payment System Could Boost Intra-African Trade by Billions of Dollars,' *International Institute for Sustainable Development*, February 14, 2022.

9 Interview with central bank official.

10 Brookings, *Foresight Africa 2024*, Top Priorities for the Continent in 2022.

Institutional frameworks supporting the implementation of PAPSS

PAPSS is underpinned by several key institutional frameworks and agreements designed to facilitate its adoption and integration across Africa. These frameworks are crucial for ensuring the system's effective operation and broad acceptance by financial institutions and businesses.¹¹

AfCFTA Agreement

The primary institutional framework supporting PAPSS is the AfCFTA. Afreximbank and the African Union (AU) have announced PAPSS as a key instrument for implementing the AfCFTA Agreement. The AU Assembly has instructed Afreximbank and the AfCFTA Secretariat to finalise and implement PAPSS, recognising its importance in enhancing trade and economic integration within Africa. These agreements provide a solid foundation for the adoption and utilisation of PAPSS across the continent.¹²

The AU

The AU has been instrumental in endorsing and promoting PAPSS. The high-level endorsement from the AU encourages member states to adopt and integrate PAPSS, reinforcing its significance as a tool for facilitating intra-African trade. PAPSS supports the AfCFTA by addressing the issue of fragmentation of African payment systems. Notably, the AU has indicated the need to address the continent's overreliance on external finance, emphasising the need for Africa's financial self-reliance.¹³ PAPSS could help deliver this aspiration as local currencies are used in cross-border payments.

Central bank collaboration

A guiding agreement among African central banks facilitates the use of PAPSS. The system is designed to use central banks or commercial banks as settlement agents, ensuring the efficient and secure flow of money across borders. This arrangement ensures the smooth operation and effectiveness of PAPSS, providing the necessary regulatory support and infrastructure for its success. The expectation is that the African banking and financial systems will be further strengthened in their infrastructure, compliance and capacity through the adoption of this system.

¹¹ Afreximbank, 'Afreximbank and AfCFTA announce the Operational Roll-out of the Pan-African Payment and Settlement System (PAPSS),' press release, September 28, 2021.

¹² Afreximbank, 'Afreximbank and AfCFTA.'

¹³ AU, 'Africa's financial self-reliance is not self-isolation, but a commitment to base development on own resources: Ministers of Finance,' press release, June 22, 2022.

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