Prosegur response to the RBA's Review of Banknote Distribution Arrangements: Issues Paper

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Executive Summary

Prosegur Australia welcomes the Reserve Bank of Australia's review of banknote distribution arrangements and the wholesale banknote system. The changing landscape of cash usage and physical banking infrastructure means the model that has worked for decades is challenged, and we need to address the new landscape.

One quarter of all transactions are cash. Our community relies on cash, and therefore on physical banking. This reliance comes in two forms:

- widespread, modest reliance across the majority of the community – with most people typically needing cash for certain activities
- concentrated reliance in specific parts of the community – with these people typically having a very high reliance on cash services.

Australia's cash system must ensure financial inclusion, equality and choice. And it must support businesses and communities.

Making cash available and efficient is fundamental to these objectives. This requires an efficient and accessible banknote distribution system.

Our response is in two parts. The 'Introduction and background' discusses important industry matters that have a bearing on the issues raised by the RBA. The second part responds to the questions raised in the RBA's issues paper.

Cash-in-transit (CIT) companies undertake every physical activity in the banknote distribution Agreement (BDA), are the cash supplier to the 70% of the market that are not BDA participants, and bear the cost of BDA compliance and banknote distribution.

This critical role of major CIT companies in the BDA should be formally recognised. They should have a seat at the table and deal directly with the RBA.

Wholesale cash access should not be a competitive advantage. The current structure has resulted in only one BDA participant offering wholesale cash access. It needs to be restructured to allow direct access for major CIT companies and be competitively neutral.

We believe that the public sector should have greater involvement in the CIT industry. This is necessary to satisfy the safety and efficiency of the changing payments system. Industry standards for note quality, safety and security need to be maintained and, as a minimum, all market participants should ensure compliance with the Cash-in-Transit Code of Practice.

We have recommended a more efficient solution for managing banknotes. There needs to be different solutions for different challenges, such as the challenges posed by regional and remote areas. Utility models, shared models, and other collaborative approaches, should be investigated to ensure cost-efficient banknote supply. Future solutions should also promote and incentivise activity that contributes to the conservation and protection of the environment including reducing the industry's carbon footprint.

We believe the BDA should be segmented and that certain financial aspects be reviewed to allow greater participation.

The CIT industry is a scale industry. Declining cash volumes have made this challenging. In our response we discuss the opportunity to review other models. This challenge is not unique to Australia and there are international solutions that can be considered.

Solutions to the changing physical landscape are coming from non-traditional sources. Independent forums or environments should be created to engage with these parties. Participants and communities should be incentivised to use new solutions that promote banknote efficiency. We have suggested some options below.

Australia has always had a CIT sector that has invested and supported industry initiatives. The major CIT companies have previously supported Australia through crises such as the GFC and COVID pandemic. Australia needs a strong CIT industry to support the cash supply system, innovate and invest in future solutions for the changed cash landscape – solutions supporting cash access for all.

We thank the RBA for the opportunity to provide a response and would welcome further discussion and engagement.

Introduction and background

The ongoing delivery of services to all parts of Australian society, including regional and remote communities, is a priority for the Government. A key component of these services is banking, and ongoing access to physical banking services – branches and ATMs – is an important feature of the service landscape.

The challenge is achieving equality of access to payment systems in an efficient way.

In this section we will expand on some of the points raised in the RBA's *Review of Banknote Distribution Arrangements: Issues Paper*.

Banknote distribution and access to wholesale cash are cornerstones of the physical payments system. We believe that to address the banknote distribution arrangements and plan for the future, the review must dig deeper into the physical landscape of payments and banking in Australia.

Changes in the landscape of physical banking

Key points

- Physical bank access points have been reducing for many years
- There is a growing number of demographic groups and regional communities that have limited or no access to bank branches

The reasons for the changes in physical networks include:

- **Shifts away from physical channels in favour of digital channels**. Internet banking began in Australia in December 1995. Since that time there has been a continued move toward digital channels. Digital channels generally provide consumers and businesses with convenience, consistency and reliability. While important parts of the business and private communities continue to rely on physical channels, the importance of digital is central to the future of banking.
- **Acceleration of the physical-to-digital shift as a result of the COVID-19 pandemic**. While the long-term effects of the pandemic are unknown, and in particular how society will preference physical vs online interactions, the pandemic has driven a short-term acceleration of movement toward digital channels.
- **Changing demographics across the community**. Over a longer horizon, changes in demographics will continue to influence needs across the various banking channels, and the banking industry response to those needs. Key demographics in local communities include age profiles, international migration profiles (particularly from non-English speaking backgrounds) and socioeconomic profiles. The industry should consider these demographic shifts in the ongoing evaluation of physical footprints.
- **Cost considerations within the banking industry**. Operating branch and ATM networks comes at significant cost. Banks constantly evaluate this cost, and the

perceived benefits for customers, both in an absolute sense and relative to other services that can be delivered with an equivalent spend.

The Issues Paper references the changes in the physical banking landscape in Australia:

- Between 2017 and 2021, bank branch numbers declined by more than 20%. In general, this reduction has been evenly distributed, though regional and remote Australia has seen a slightly greater reduction of 24.6%.
- The number of ATMs has declined by around 20%. This reduction is more varied geographically

It is unlikely there is one solution for all these challenges.

Changes in cash usage

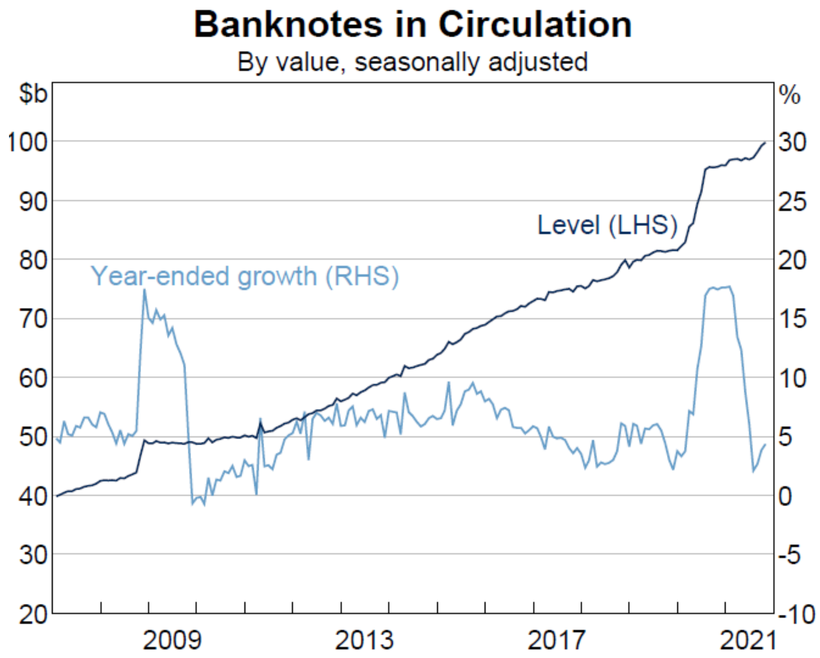
Key points

- ➢ The value of banknotes in circulation continues to increase, while cash as a form of payment has been reducing as a proportion of total payments, and to a lesser extent in absolute terms
- ➢ The continued presence of cash in the community (especially in certain regions and by certain demographic groups) means supporting the cash infrastructure is critical – and physical banking networks are an important way to achieve this

The value of banknotes in circulation has continued to grow (Figure 1), even as cash as a proportion of transactions has declined. The early stages of the COVID-19 pandemic saw an acceleration of this growth, with a 17.1% increase from March 2020 to February 2021 as Australians kept cash in reserve. The RBA identifies this as an acceleration of a trend experienced over several years, with physical currency increasingly held as a store of value, even as its use as a payment method proportionately decreased.[1]

[1] Gutmann et al, 2021, RBA Bulletin "Cash Demand During Covid-19"

Figure 1: Banknotes in Circulation[2]



While the value of cash in circulation continues to grow, the view that cash usage has declined, both as a proportion of total payments and in absolute terms, is generally accepted and is supported by the data. This decline has been occurring since around 2009, and the onset of the COVID-19 pandemic has significantly influenced trends in cash usage. However, the predictions of the future of cash – that cash usage will cease in various short-horizon timeframes – are simplistic and do not take into account the ongoing need for cash, particularly in regional and rural areas and by certain demographic groups. Based on the data and a series of thematic analyses, we believe that, whilst cash usage will continue to decline, cash will remain an important payment method for certain people for an extended period of time.

One of the challenges with any analysis of cash usage is the lack of economy-wide, reliable data. The most reliable data points are ATM/eftpos withdrawal data from the Reserve Bank of Australia's payments statistics, and to a lesser extent the RBA's triennial wallet studies on payment trends. The Issues Paper notes, in reference to the wallet study regarding cash transaction numbers, that "… the total share of retail payments – both in-person and online – made with cash fell from 69% in 2007 to 27 percent in 2019." While the decline is clear, the important point is that 27% of all retail transactions in 2019 were cash.

While these data are the best that is readily available, they each have limitations:

- Withdrawal data is evidence of card-based withdrawals, and is only an indicator of cash activity. It does not measure cash payments and misses the recycling of cash across the economy (discussed in more detail below).
- Wallet studies are only performed every three years, have a relatively small statistical base, and miss multiple segments of cash usage in the economy.

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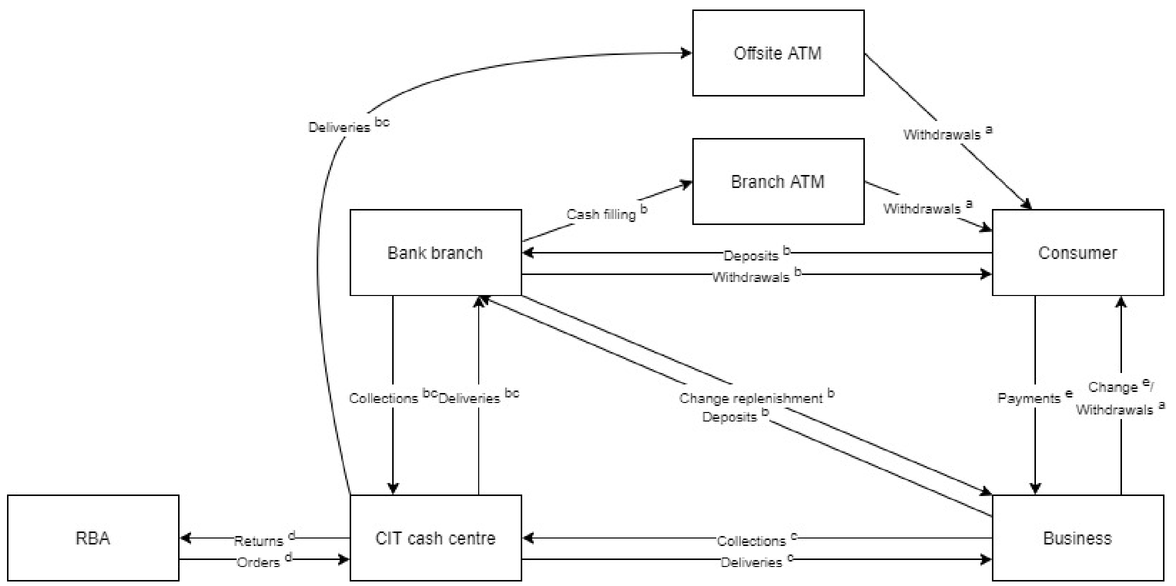
[2] Reserve Bank of Australia 2021 Review of Banknote Distribution Arrangements: Issues Paper

Despite these limitations, the RBA's work to understand cash usage patterns provides some insight into what the community is doing with cash. To add to the understanding of cash as a form of payment, we have prepared a graphical representation of the cash cycle at Figure 2, which indicates the potential sources of data to gain a full understanding of cash usage.

Figure 2: The cash cycle[3]



a. Data available and reported today (RBA payments statistics)
b. Data exists within bank systems, not reported, varying ease of accessibility
c. Data exists within CIT operator systems, not reported, generally accessible
d. Data exists within RBA and bank systems, not reported, varying ease of accessibility
e. If data exists it will be extremely challenging to capture, synthesise and report on

A sensible starting point to understand cash usage patterns is withdrawal data. Figure 3 shows the long-term trend of cash withdrawals, and Figure 4 and Figure 5 show the trend of cash withdrawals from January 2019 to October 2021.

[3] Source: Precinct

Figure 3: Cash withdrawals over time, 1994-2021[4]

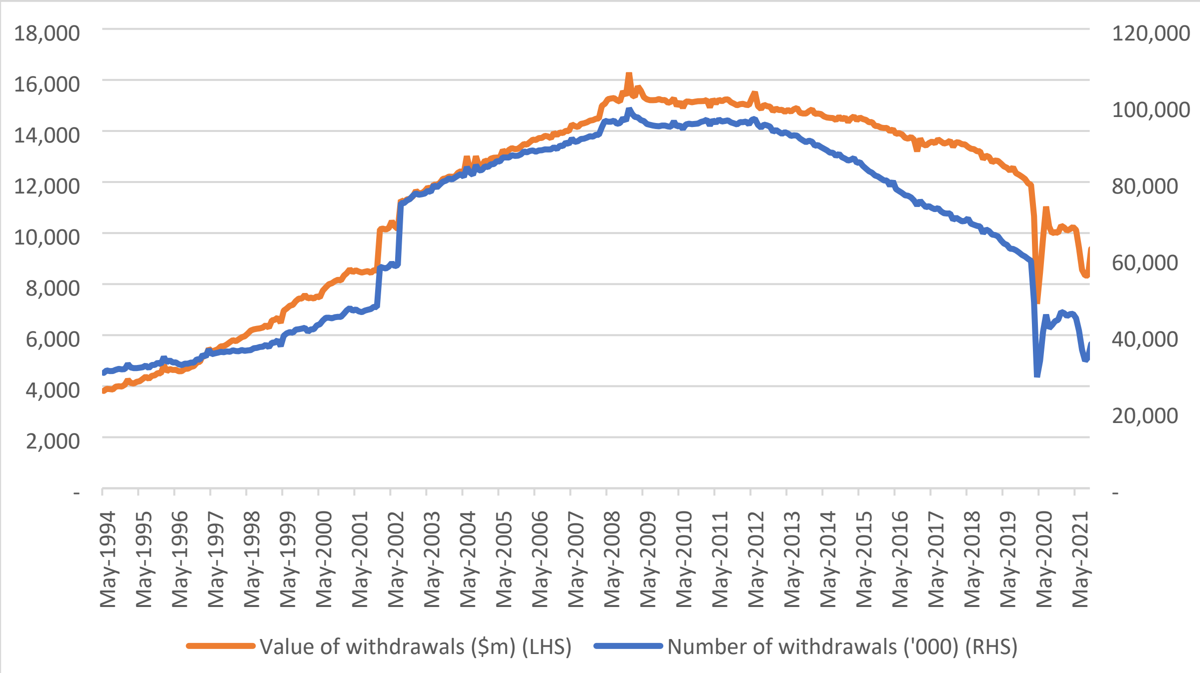
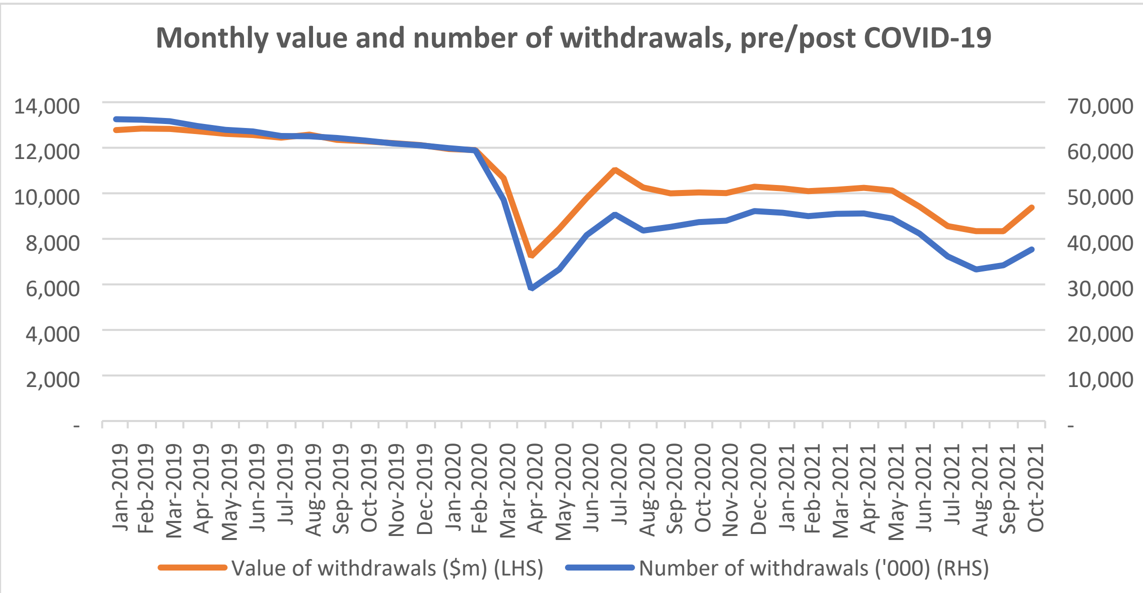


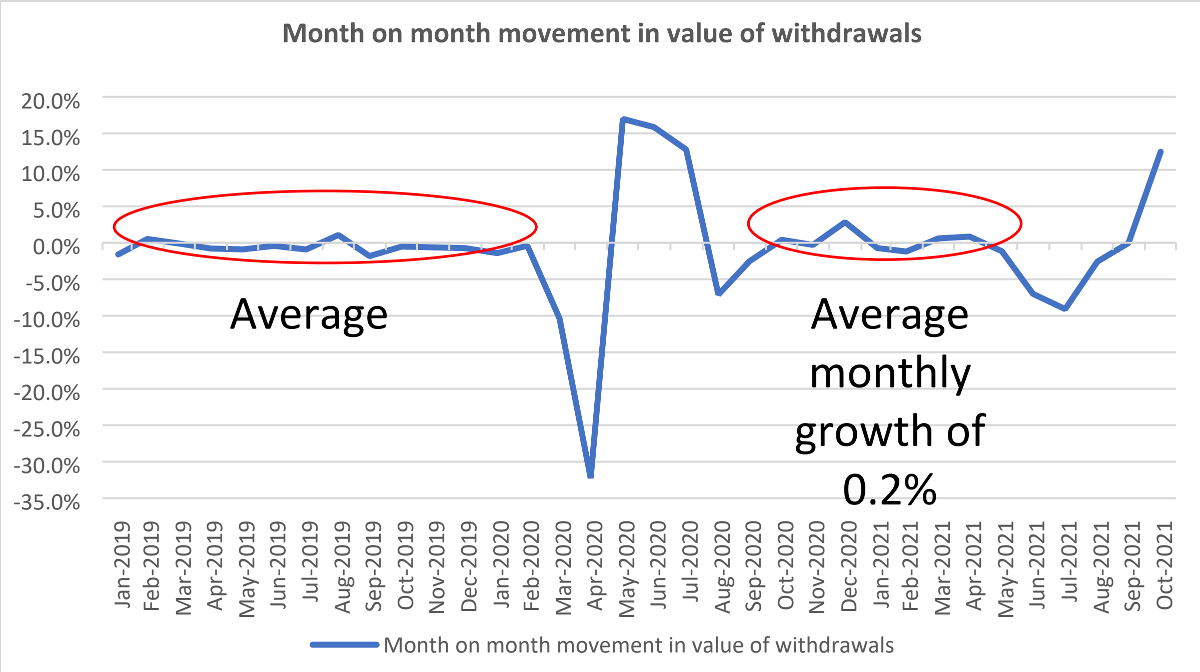
Figure 4: Cash withdrawals over time, 2019-2021[5]



[4] Source: Reserve Bank of Australia Payments Statistics

[5] Source: Reserve Bank of Australia Payments Statistics

Figure 5: Cash withdrawals over time, 2019-2021



We have had a hypothesis for some five years that the community demonstrates a spectrum of payments preferences, which we categorise as:

- digital most/only group
- cash most/only group
- a large 'mixed' group.

As we consider that there will remain a need by certain communities and demographic groups for cash as a form of payment, we have anticipated that cash usage would decline to a baseline, and then stabilise for an extended period. In reviewing the above withdrawal data, our interpretation is that the COVID-19 pandemic has accelerated the polarisation of those in the mixed group, such that those who were likely to migrate to primarily digital forms of payment have now done so, and those who are now using cash have a strong preference or necessity to do so.

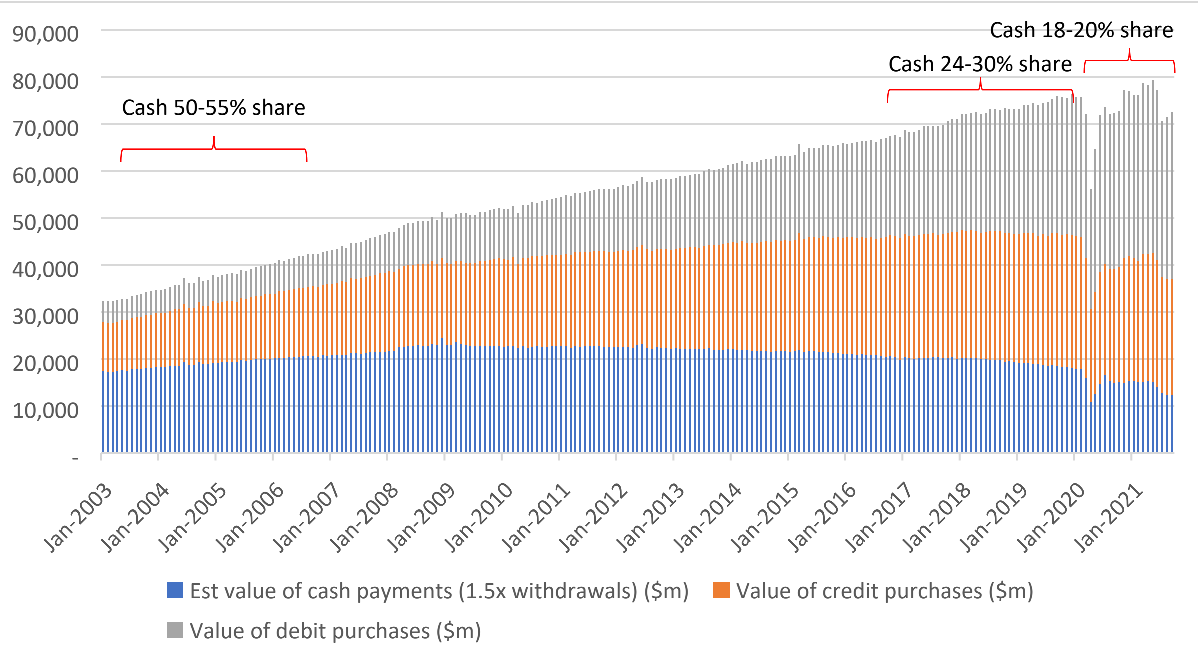
Of particular importance is the usage of cash as a proportion of the total payments landscape. As mentioned earlier, this is a difficult analysis to perform, because there are no reliable datapoints for actual cash payments. As noted in Figure 2, there is no publicly reported or generally available data for:

- consumer withdrawals from bank branches
- business withdrawals from bank branches
- consumer payments to business
- change provided to consumers by business.

Each of these are important inputs to the volume of cash payments.

Due to the non-availability of data, we have historically used a multiple of 1.5 of cash withdrawals as a proxy for cash payments. This is based on the rationale that when cash is used by consumers, they will typically receive change from the merchant, and this will cycle some 2–3 times, but at decreasing levels. We acknowledge that this proxy is an estimate, but it gives some weight to the recycling effect of the cash cycle, which provides a more reasonable comparison to other payment forms. Figure 6 shows the share of the three major payment forms by volume (cash, credit card, debit card) over time. As at October 2021, we estimate that cash makes up 18% – 20% of total payments by value, compared to 34% by credit card and 47% by debit card.

Figure 6: Cash as a % of total payments over time[6]



While there may be challenges with the data, it's clear that around 25% of all transactions are cash, and within specific communities or demographic groups this figure is much higher.

Prosegur believes that the decline in cash usage has been exaggerated by COVID and we are likely to see the curve flatten or return to a steady rate of decline, as was observed prior to the pandemic.

This warrants a focus on making cash available and efficient. The current review is very different to previous reviews because of these changes in cash usage.

The impact of reducing access to physical banking

Key points

- Cash usage and physical banking, while reducing, continue to be an essential service to the community and a way to protect the most vulnerable

[6] Source: Reserve Bank of Australia Payments Statistics, Precinct

- ➢ The removal of cash, which will increasingly happen if physical banking services reduce, will impose growing costs on business in general and small business in particular
- ➢ Physical banking has been seen as a promoter of local economies, particularly in regional areas
- ➢ Australia is not alone in facing these challenges, and there is international research we can draw on

In the sections above we have discussed the changing physical footprints of banking services, and the changing landscape of cash usage in Australia. We have focused on these two areas because physical banking and cash access are intricately linked when the impact of change is considered.

This section discusses the impact of reducing access to physical banking through three lenses:

- individuals in the community
- businesses and their costs to operate
- regional local communities.

We also look at two international studies that have explored these questions in more detail.

Community reliance on physical banking

Based on sustained media commentary around the decline in cash and the expected end of cash, it would be easy to draw the conclusion that cash has already been relegated to a niche payment form, used by only a fraction of the community. But on raw numbers alone, this conclusion is unreasonable. We have used the RBA's payments statistics to illustrate what cash usage might look like among the community, and what that means based on wages, in Figure 7.

Figure 7: Inferring individual cash usage patterns from payments data[7]

If the proportion of the adult population using cash is:	…then those who use cash would average:	…which equates to:
100%	2.1 withdrawals per month	
	$488 cash withdrawn per month	11.7% of after-tax median wage*

[7] Source: Reserve Bank of Australia Payments Statistics, Australian Bureau of Statistics Population Data, Australian Taxation Office, Precinct

50%	4.2 withdrawals per month	
	$977 cash withdrawn per month	23.5% of after-tax median wage*
30%	7 withdrawals per month	
	$1,628 cash withdrawn per month	39.2% of after-tax median wage*

* Median Australian wages are $1,150 per week, which after tax is $4,158 per month

These numbers point to some level of reliance on cash and, as a result, on physical banking. This reliance is either:

- widespread across the majority of the community, but with modest reliance at the individual level, or
- concentrated in a portion of the community, with these people having a very high reliance on these services.

The reality is likely to be somewhere in between. This tends to be discussed as the “choice and necessity” evaluation.

Choice, as a concept, is straightforward. In a democratic, egalitarian society, Australians believe strongly in freedom of choice. Allowing individuals in society to choose how they pay has been supported by the RBA in numerous speeches and is generally accepted as an important feature of the payments environment.

While we have an obligation to support choice in payments, the obligation is much stronger in the context of necessity. There is much to be said about necessity. We look at two ways of understanding necessity: financial exclusion and digital exclusion.

Financial exclusion as a measure has been defined by the Centre for Social Impact:

> Financial exclusion is the lack of access to affordable and appropriate financial services and products from mainstream institutions. Financial exclusion is measured on the basis of ownership of three basic financial services and products, namely a transaction account, general insurance, and a credit card.

The Centre for Social Impact’s 2015 report[8] provides substantial review and analysis around what financial exclusion means in practical terms and societal outcomes. Extending from this, if a person has no banking services in close proximity, then they are at risk of financial exclusion. This is most apparent in those who are already at risk, because they will have a proportionately higher reliance on physical services as opposed to digital/online services. While a little dated, Figure 8 highlights that a much higher portion of the population is severely or fully financially excluded than would be expected, and the level of financial exclusion is not improving.

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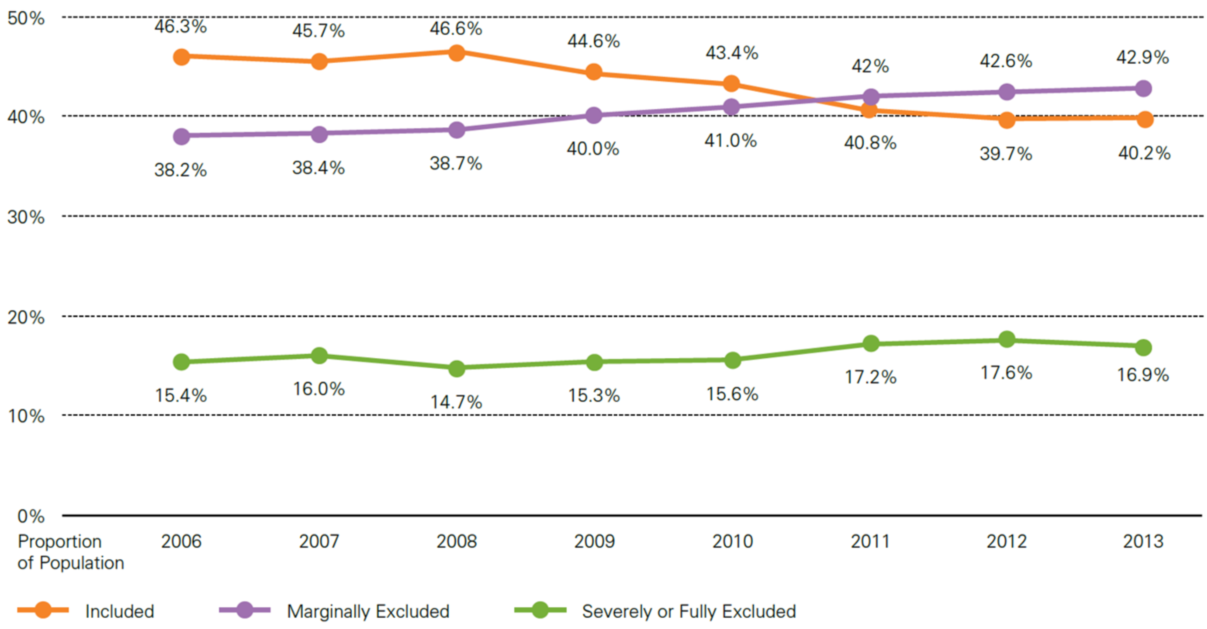
[8] Muir, K., Marjolin, A. & Adams, S. (2015), Eight years on the fringe: what has it meant to be severely or fully financially excluded in Australia? Sydney, Australia: Centre for Social Impact for the National Australia Bank

Figure 8: Financial exclusion in Australia (reproduced from Centre for Social Impact 2015 report) [9]



Definitions:

- Included: holds a transaction account, a credit card and basic insurance
- Marginally excluded: holds two of a transaction account, a credit card and basic insurance
- Severely excluded: holds one of a transaction account, a credit card and basic insurance
- Fully excluded: does not hold a transaction account, a credit card or basic insurance

In parallel with financial exclusion, it is important to consider digital exclusion. This impacts the part of the population that is most in need of physical services (rather than online services). A report prepared by RMIT and Swinburne University of Technology in 2020[10] highlighted the digital divide in Australia. Put simply, there is a portion of the community that has relative privilege: they can easily access, afford, and have the ability to use, digital technology. However, there is a substantial part of the community that lacks this. Table 1 highlights this divide through a breakdown of digital inclusion across income quintiles. Further, digital inclusion has been measured within cross-sections of vulnerable people. It is these people – for whom we need to take the most care in ensuring access to services – who are most digitally excluded.

These findings highlight the need for physical banking services and cash.

[9] Ibid

[10] Thomas, J, Barraket, J, Wilson, CK, Holcombe-James, I, Kennedy, J, Rennie, E, Ewing, S, MacDonald, T, 2020, Measuring Australia's Digital Divide: The Australian Digital Inclusion Index 2020, RMIT and Swinburne University of Technology, Melbourne, for Telstra

Table 1: Digital inclusion in Australia (adapted from RMIT/Swinburne report) [11]

Income quintiles	Australia	Income Q1	Income Q2	Income Q3	Income Q4	Income Q5
Access	76.3	82.4	82.8	78.5	70.9	62.2
Affordability	60.9	78.5	67.6	58.1	46.3	32.7
Digital ability	52	60.6	58.7	52.7	44.2	36.3
Digital inclusion index	**63**	**73.8**	**69.7**	**63.1**	**53.8**	**43.8**
Average household income	*116,584*	*280,956*	*135,928*	*88,764*	*53,248*	*24,336*

Vulnerable people	Australia	>65	Income Q5	Un-employed	Disability	Indigenous
Access	76.3	62.7	62.2	76.2	67.6	68.5
Affordability	60.9	51.7	32.7	57.6	50.5	54
Digital ability	52	34.8	36.3	56.8	39.8	42.8
Digital inclusion index	**63**	**49.7**	**43.8**	**63.6**	**52.6**	**55.1**

Green=high digital inclusion; orange=medium digital inclusion; red=low digital inclusion

Costs to small business

Reductions in physical banking potentially impact business costs, particularly the costs of small businesses. If businesses cannot bank cash takings, they will eventually not be able to accept cash, and are then at the whim of card schemes and the fees they charge.

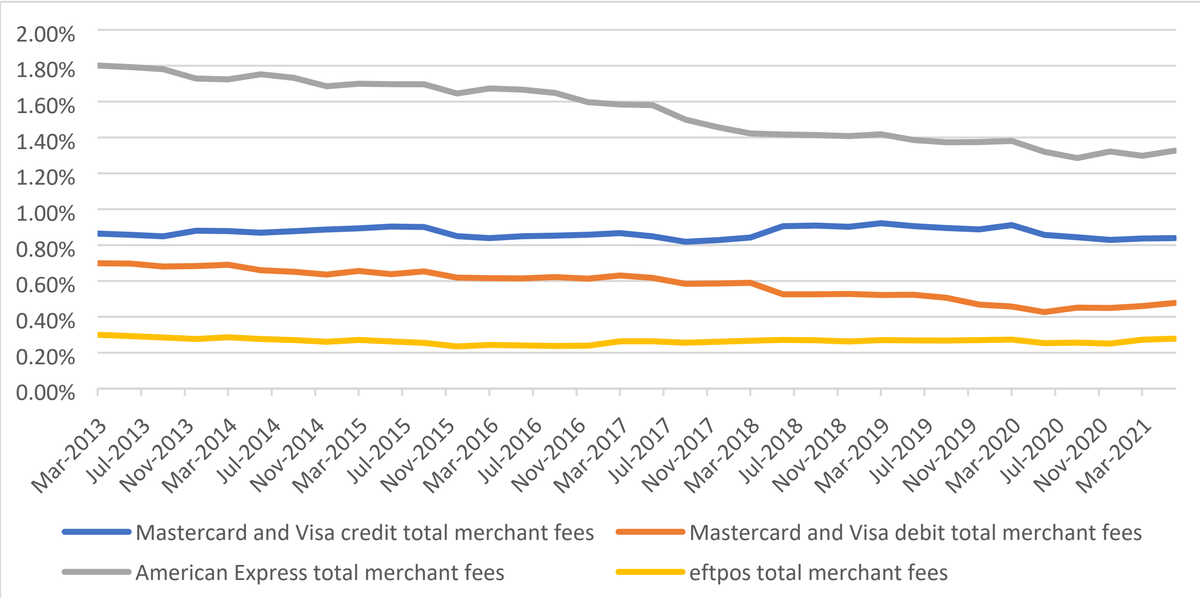
Cash plays a unique role in allowing businesses to avoid or minimise merchant fees – if cash was not able to be banked, then businesses would be fully exposed to the cost of card acceptance, and there would be few market controls to limit increases in those costs.

Figure 9 shows the RBA's quarterly analysis of merchant fees for the major card types in Australia. As shown in this chart, while the fees associated with some card categories have reduced over the past decade, merchant fees have been stable for the past three years, and now are tending to trend up. The risk to businesses in general, and small business in particular, is that if this upward trend continues, and cash becomes a less accessible

[11] Adapted from data reported in Thomas, J, Barraket, J, Wilson, CK, Holcombe-James, I, Kennedy, J, Rennie, E, Ewing, S, MacDonald, T, 2020, Measuring Australia's Digital Divide: The Australian Digital Inclusion Index 2020, RMIT and Swinburne University of Technology, Melbourne, for Telstra

payment form due to a reduction in branches, then there will be no way to avoid increasing costs for doing business.

Figure 9: Merchant fees over time[12]



Local economies

At the community level, the presence of physical banking is an important enabler of employment. Rural communities have always viewed the closure of the last bank in town as the beginning of the end for the town.

On 22 October 2021, the Government announced the establishment of a regional banking taskforce to assess the impact of bank branch closures on regional communities. Senator Perin Davey, one of the Co-Chairs of the Taskforce, raised some concerns relevant to the topic of this paper following a public consultation meeting in Mildura on 19 January 2022. Senator Davey is quoted in Queensland Country Life on 20 January 2022.

> "We've seen through COVID a move back to the regions, which is exciting," Senator Davey told AAP.
>
> "But when people are looking at towns they want to move to, they look at what services are in a town: is there a school, is there a medical centre, and is there a bank? "If the bank is not there, then they might look to the next town.
>
> "So rather than it being the beginning of the end (for country towns), we're hearing that it's an impediment to the beginning."

In relation to vulnerable people.

> "A lovely older gentleman said, 'I'm only going to be around for another 10 to 15 years and then you can go for broke, but don't leave me behind as you're racing to the next era of technology'.

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[12] Source: Reserve Bank of Australia Payment Statistics

> "That was a really important message. We can't leave behind anyone, the older demographic, people who rely on disability services, or our Indigenous people in remote communities."
>
> Small business owners also raised issues about people travelling to other regional centres because of the lack of a bank.
>
> "While they're out of town doing their banking they're going to buy a coffee or do their groceries or go to the newsagent in that town, rather than their hometown," Senator Davey said.
>
> "It means small towns are losing that economic movement."

The Victorian Government prepared a report in 2002 that investigated the effects of branch banking in local communities. While slightly out of date now, the essential findings of the report are relevant for consideration and consistent with what the Regional Banking Taskforce is identifying. Firstly, on the positive side, *“Following the opening of a [bank branch] that operates in both Rupanyup and Minyip in 1998, the local supermarket saw a 30 per cent increase in its turnover, enabling the manager to expand his product range and purchase new equipment.”*[13] This highlights the benefit of branches in local communities, because they draw the surrounding population to the town. From the same report, the negative side was also discussed: *“[Boroondara City Council] found that in both metropolitan and rural areas, the loss of the last bank branch causes butchers to lose 40 per cent in sales, general retailers between 10 and 25 per cent and pharmacies and newsagencies 5 per cent.”*[14] This shows the opposite effect of bank branch presence. The effect of the last branch leaving a town was particularly well expressed by Ian Alison, a resident of Boort, VIC, to the ABC: *“[When the last bank branch closes] people go away to do their shopping and banking and all that sort of stuff, and a little town dies.”*[15]

We see the need for banking services, provided in physical form, as essential to regional communities in particular.

Prosegur attended the Local Government Association’s National General Assembly in June 2021. We attended with one objective: to listen to local government representatives concerning access to physical banking. The sentiments expressed above were a common refrain: physical banking services were essential in the bush, the services offered through Australia Post were not sufficient for the long term, and the continuing decline of services was creating increasing challenges for local communities.

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[13] “Inquiry into the Impact of Structural Changes in the Victorian Economy” Parliament of Victoria, May 2002

[14] “Inquiry into the Impact of Structural Changes in the Victorian Economy” Parliament of Victoria, May 2002

[15] “What happens when a town loses its last bank?” Lauren Day, ABC. https://www.abc.net.au/news/2018-06-14/the-town-with-no-bank/9866310

International research

In the United Kingdom, a comprehensive report was released in 2019 called the "Access to Cash Review."[16]. As far as the impact of a reduction in physical banking and access to cash on the community, we highlight here the key risks identified in the report:

- **Risk to rural communities**. The report discusses the slower rate of movement to digital in rural communities, which can be as a result of poorer access to high speed internet. While in Australia the NBN has provided improved internet access to rural communities, 4% of the population are on fixed wireless connections which have variable reliability. The report also pointed to rural communities tending to "have a larger proportion of lower income, older and more vulnerable users"
- **Risk to personal independence**. This risk calls out the higher proportion of those who are elderly or who live with disabilities that rely on cash – and we would in turn say physical banking services – to manage their daily affairs
- **Risk of increased debt**. The benefit of cash as a tool for budgeting was observed, and this aligns closely with consistent findings by the RBA in their triennial cash usage studies[17] (with nearly 50% of Australian high cash users saying that budgeting was the most important reason that they use cash)
- **Risk of financial abuse**. Domestic financial abuse often takes the form of the abuser limiting or completely restricting access to finances for their partner. Cash can present a way of reducing the scope of such financial abuse because it allows anonymity in purchases
- **Risk to community and connection**. The ongoing move to digital-everything puts connection within the community increasingly at risk. In the payments and banking space, availability and use of cash, together with physical presence of services, creates personal interactions and the opportunity for connection
- **Risk of poorest paying most**. At both the individual and business level, those who can least afford to lose cash as a universal form of payment are the ones who will suffer the most through increased costs. This risk is in line with our earlier discussion on the cost of merchant services to small business, particularly if the ability to easily deposit cash takings is reduced
- **Risk of catastrophic failure**. While the UK report was written in a pre-COVID world, it was quite prophetic with this risk. We saw in Australia and across the world both a reduction in the day-to-day use of cash, but at the same time a flight to cash for safety, with substantial growth in currency in circulation and reports of large withdrawals over the counter from branches. While COVID is one type of crisis, of particular relevance to cash access and the infrastructure that supports cash as a form of payment, including branch networks, is the potential for technology failure including risk of cyber-attack and risk of failure in single-point components of the payments network. While access to cash does rely on the banking system, the nature of cash means that there is a lower dependency in the short term, making it a suitable redundancy

[16] "Access to Cash Review: Final Report" Natalie Ceeney (Chair), United Kingdom 2019, https://www.accesstocash.org.uk/media/1087/final-report-final-web.pdf

[17] "Consumer Payment Behaviour in Australia" James Caddy, Luc Delaney, Chay Fisher and Clare Noone, Reserve Bank of Australia, 2020

Earlier this year the Dutch Minister for Finance tabled a report[18] commissioned by the Dutch Central Bank and prepared by McKinsey & Company, which looked at possible future challenges with the cash infrastructure in the Netherlands. In brief, some of the findings of the report include:

- Cash usage in the Netherlands has tracked at a similar trajectory but slightly higher level than Australia, with an estimated 65% of payments being made by cash in 2011, 32% in pre-COVID 2020, and 21% in 2021
- The report provides some helpful analysis and insights around the overall cash cycle and the proportionate costs within the cash system
- There is an estimated 1.3-1.5m people in the Netherlands who are dependent on cash. This is between 7.5% and 8.8% of the population

The report advocates for a range of measures to ensure system resilience of the cash system. While conditions in the Netherlands are different to Australia, they are a helpful reference point.

Alternate global models

Key points

- Globally there are a range of models to address the need for sustainable physical banking that have been implemented or tested – Australia is not the first or only country confronting this challenge
- The needs of each country are different, and therefore the response will be country-dependent
- There is opportunity to learn and build from existing models, both to inform "best of breed" and to contextualise learnings

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Australia is not unique in facing the challenge of technology changes, demographic changes, and the resultant change in needs of physical banking infrastructure. We provide three examples of alternate models that are found globally that assist banks and the community in addressing this challenge, from Europe, the United Kingdom, and Latin America.

In the Netherlands, three of the major banks, ABN-AMRO, ING, and Rabobank, have established a joint infrastructure model for cash services, called Geldmaat (literally "money buddy"). Geldmaat now operates the majority of ATM and other bank cash automation devices in the country. While owned by the three banks, Geldmaat provides services to other banks in the Netherlands, and encourages all banks in the country to use the network to provide services to their customers. When considering the Geldmaat model, a number of key features are notable:

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[18] "The Future of the Cash Infrastructure in the Netherlands" Mckinsey & Company, the Netherlands, June 2021. Executive Summary available in English, Full Report available in Dutch, at https://www.dnb.nl/en/actueel/dnb/press-releases-2021/dnb-calls-for-new-agreements-about-cash/

- Almost all services are delivered via cash automation devices – ATMs and other device types, rather than tellers. There are some locations where staff assist customers, particularly as part of an education process
- The network is independently branded rather than being a co-brand of the founding banks
- Locations are both branch and offsite
- Geldmaat offers the following transaction types:
  - Loose note withdrawals
  - Loose note deposits
  - Sealed bag deposits
  - Coin deposit and withdrawal (starting to rollout)

In the United Kingdom, a number of models have been explored. In 2019-20, a pilot "business banking hub" was tested by three of the major banks (Lloyds, NatWest and RBS/Barclays). More recently, a startup called OneBanks has commenced rollout of their kiosk concept. Adopting the slogan "all banks, one location, all welcome," OneBanks has commenced deployment in Scotland. Some of the features relevant to understanding OneBanks include:

- At this point they have taken a light footprint approach, with kiosks deployed in Co-op supermarkets
- The OneBanks model aspires to 'preserve human interaction' by having staff as a key feature of their model
- OneBanks uses the United Kingdom's open banking infrastructure to facilitate financial transactions

In Latin America, outsourced banking solutions have been a feature of the banking landscape for many years. Prosegur has been central to this evolution. Prosegur commenced operation of "multiagencias" over a decade ago, and more recently has established its CORBAN business in multiple countries, including Brazil, Colombia, Peru, Uruguay and Chile. Key features of Prosegur's model over the years include:

- Explicit partnering with banks to deliver services that are fit for each bank's customer base
- Model flexibility to allow both "mono bank" and "multi bank" models
- Generally favouring light footprint models, including agency models (with CORBAN services delivered in retail environments such as pharmacies, newsagents, etc) and dedicated outlets including small shop fronts, kiosks, and "store in store" models
- Mixed technology and staff approach, with teller-style services being the norm
- Customer support models for lending and deposit products, including the initiation and management of loan and account opening applications on behalf of banks

We see a number of observations and questions relevant to any future model for Australia coming from this set of example international models:

Industry and community risks and challenges due to changes and the "default" model available

Key points

- Services need to be proximal to the users of those services.
- The physical banking landscape still processes a very high value of cash and a large number of customers, which means that the Bank@Post model is fundamentally inadequate for servicing the industry due to security, cost and service intensity, unless bank branch footprints remain essentially the same as they are today
- Leave-behind approaches that exist today, including the Bank@Post model, do not adequately consider customer experience, and with any growth in volumes being pointed to that channel, customer experience is likely to deteriorate substantially

The risk and challenge for service coverage

The most obvious risk and indeed what we see as a key driver is the need for service coverage across the community. When we talk about service coverage we don't see this as being limited to geographic coverage. While geographic coverage is of fundamental importance, service coverage also includes the services that customers can receive. We restate the ABC's reporting of Blayney Mayor Scott Ferguson's comment in relation to the need for services in regional communities: "Some services will be offered at local post offices, but most customers will have to do their banking online or in neighbouring towns. 'Things that could potentially be done at the post office, but we are finding that the post office will not be able to deliver some of those services that our businesses need.'"[19] Service coverage starts first with seeking to understand customer needs and expectations, a step that we believe has been sorely lacking to date.

The risk and challenge of access for all in the community

For many years now, basic ATM withdrawals have been available to any cardholder at any ATM. This is driven by the way that card scheme rules operate, by the technology architecture used to process withdrawal transactions, and by mechanisms that allow ATM operators to offer services directly to customers. Deposit acceptance is more challenging, for a number of reasons:

- The technology architecture has not existed for processing deposits except for on an "own-bank" basis

[19] "Commonwealth Bank shuts two more branches in regional New South Wales" Joanna Woodburn and Xanthe Gregory, ABC. https://www.abc.net.au/news/2021-06-04/two-central-west-banks-shut-up-shop/100184490

- While ATM withdrawals generally do not have significant risk in relation to financial crime, deposit solutions are an important area of focus for financial crime and AML/CTF risk, which means that solution development needs to fully consider these risks and how it will manage them
- Most existing models, including Bank@Post, are offered on an "agency" basis, which means that the service provider is acting only on behalf of the principal bank. To extend this logic, it means that unless a customer's bank has an agency relationship (and a technology link) with the service provider, they cannot receive services.

From a technology perspective, there are a number of avenues that offer potential, particularly via the New Payments Platform and via the major debit card schemes (eftpos, Visa and Mastercard). Solving the technology challenge is only one piece of the overall puzzle, but there are technologies that have the potential to at least solve this challenge in part.

The agency challenge is more substantial. Already some in the community feel the pain of this challenge, being refused service by Bank@Post because there is not a commercial arrangement between their bank and Bank@Post. We of course support the right of any commercial entity to enter into, or not enter into, a commercial relationship as they see fit. However, if the fundamental structure of the model means that those end customers are unable to receive services then there is a significant challenge which particularly affects regional and remote communities, where alternatives may be inadequate or unavailable.

The risk and challenge of sustainable business models

We have discussed some of the reasons for change in physical networks – why banks are reducing their branch footprints. To recap, these reasons include a shift toward digital channels and the resulting reduction in demand for services, together with the cost of operating physical channels. This points to the need for economic sustainability in any model that is considered.

On this risk there is a conflict: on the one hand, the more volume can be brought into any service model from multiple banks, the lower the per-transaction cost will be, and the more sustainable will be the model. On the other hand, setting policy that preferences one model, in particular the existing Bank@Post model, can limit the opportunities for other businesses, or business models, to find sustainable solutions for the challenges facing the industry.

The risk of financial crime

Financial crime and its management have been a key focus of the banking industry for some years. A number of large investigations by AUSTRAC have highlighted the challenges of managing financial crime risk well, and the need to ensure strong systems for risk assessment, customer identification, transaction monitoring and management, and reporting. Where these services are outsourced, the need to ensure these pillars remains strong is critical. Specifically in relation to cash deposits, where the receiving bank is one or more steps removed from the point of deposit, the challenge of ensuring sufficient knowledge of the deposit and the depositor increases.

A path for the future

The industry must actively work towards solutions that specifically deal with the challenges of reducing physical networks, access to cash and the cost of cash availability. Focus on:

- Delivering basic banking services, in particular transactional banking (deposits and withdrawals) as a priority
- Rapidly adding additional banking services on behalf of banks as part of an active product roadmap
- An objective of providing services across all of regional/remote Australia.
- Taking a "customer-first" approach to solution build, considering the needs of the customer, the need to assist customers with change and understanding how we can help them access services from their bank
- Building a model that does not give an avenue for financial crime to take place

Emphasising several things:

- Access to services for anyone in the community
- Footprint build principles that think firstly about the delivery of banking services, rather than attempting to squeeze banking services into existing retail models
- A digital experience that compliments the physical experience – so that customers who are comfortable with digital technology can use this to get a better overall experience than they have today

Support from the banking industry and government policy to remove roadblocks and market inhibitors are vital to have a strong long-term solution to physical banking needs. The cash distribution and wholesale cash system are fundamental in this solution.

Our responses to the Review of Banknote Distribution Arrangements

Australia's Banknote Distribution System

Q1. Are there aspects of the current BDA arrangements that affect the ability of existing BDA participants and approved CITs to manage cash distribution in an environment of declining transactional cash use? If so, please provide details.

Q2. Do the current BDA arrangements prevent additional parties who might otherwise wish to do so from participating in wholesale cash distribution. If so, how?

Response summary

- Access to wholesale cash should not be used by commercial businesses including banks and CIT companies for competitive advantage.
- CIT companies provide all services that are part of the BDA.
- CIT companies have direct service contracts for 60% to 70% of the market – the portion that is not BDA participants.
- The expression 'cash-in-transit' does not do justice to service providers. The business relationship is as cash management and solution providers.
- The BDA regime should be broken up and CIT companies participate directly with the RBA.
- Wholesale cash arrangements should be direct between the RBA and the CIT companies.
- Banknotes should be managed as a pool by geographic area.
- Current arrangements do not promote optimal activity.
- Regional and remote communities are particularly disadvantaged under current arrangements and a better level of service could be delivered through a more efficient allocation of resources.
- The carbon footprint of the industry needs to be reduced.
- We suggest that the current cost recovery model for banknote supply and distribution be reviewed in the context of the changed cash landscape and community needs.
- The financial aspects of the current BDA should be reviewed to allow greater participation.

- Review the treatment of banknotes in new generation on-site devices such as Smartsafes.

Banknote Distribution Agreement (BDA)

Prosegur believes that access to wholesale cash should not be able to be used for competitive advantage by commercial businesses. This is not the current position. In addition, while the current wholesale cash arrangement may have achieved desired changes in its early years, the system now is suboptimal – in fact, it encourages behaviours that create cost and inefficiencies.

Under the current BDA arrangements, the only BDA participants are the big four banks. This is in direct contrast with the Australian business environment for cash collections and deliveries. The CIT companies have the contractual relationship with virtually all non-BDA participant customers, but do not contract directly with the RBA. These relationships are acknowledged in the Issues Paper:

> CIT companies carry out the majority of the logistics associated with distributing and processing banknotes on behalf of banks, other authorised deposit-taking institutions (ADIs) and retailers. (page 10)

This statement does not fully reflect the relationships and work undertaken by major CITs. Nor does the expression 'cash-in-transit companies' do justice to their role. These businesses are cash management and cash solution providers. The major CIT companies have contracts with customers to provide a range of cash management, cash optimisation, reconciliation and reporting services, as well as logistics.

Most importantly, major CIT companies settle with their customers direct for cash collections and deliveries, using their own banking arrangements. CIT companies' cash collections and deliveries for their customers represent some 60% to 70% of total cash activity, exceeding those of the combined BDA participants. BDA participants do not have any granular or substantive visibility of this activity or its effect on cash distribution.

Excluding the four BDA participants, the CIT companies in Australia hold direct business relationships with virtually all other businesses that handle cash – such as other ADIs, retailers, ATM deployers, hospitality venues and local government organisations. In addition, the major CIT companies also undertake virtually all of the physical activity and note quality sorting on behalf of the BDA participants. Virtually all of the physical activity and compliance requirements related to the BDA is undertaken by the major CIT companies.

This is a strong case that the RBA should contract directly with the CIT companies.

The only participants in the current BDA are the four largest banks. The Issues Paper notes that:

> In principle, any organisation can enter into a BDA with the Reserve Bank provided they are prepared to sign up to the contractual requirements. In practice, however, there are aspects of the arrangements that may limit the ability of some organisations to enter into a BDA. (page 13)

We will address some of those limiting aspects later in this response. To our knowledge, no non-ADI has attempted to enter a BDA. In addition, some ADIs who were previously part of the BDA with the RBA chose not to renew that contractual relationship a number of years ago.

These points suggest that if wholesale cash is to be more efficient and available, the current structure of the BDAs must be addressed.

Given that the majority of cash activity is from non-BDA participants, how do they access wholesale cash? They do it through the major CIT companies, who must negotiate a commercial arrangement and contract for a fee with one of the BDA participants for access to the wholesale cash system to service the needs of the Australian commercial market, including other ADIs.

Prosegur has a contract with a BDA participant for access to the wholesale cash system to allow services to be performed to non-BDA customers. The last time Prosegur did a market scan for such access there was only one BDA participant that was willing to offer access to wholesale cash arrangements. Prosegur believes it is important that the structure of the BDA supports more access opportunities.

This commercial arrangement for wholesale cash access has significant costs and requires Prosegur to absorb the substantial cost of virtually all wholesale cash movements. Because of the lack of visibility of the BDA, it is not possible to identify if wholesale cash costs are being shared equally by industry participants. Again, if the BDA was between the RBA and the CIT company, the costs would be transparent and presumably the same for all participants – a competitively neutral position on wholesale cash.

The Issues Paper states that:

> As an alternative to purchasing banknotes directly from the Reserve Bank, BDA participants are encouraged to purchase surplus banknotes from each other. This is also how organisations that are not party to a BDA are able to obtain banknotes. (page 11)

We agree that surplus banknotes are traded between BDA participants. The trading process itself is understood to have inefficiencies, because such trades are only by mutual agreement. Therefore, if a BDA participant holds surplus notes but chooses not to trade them, then the requesting BDA participant must source those notes elsewhere, including directly from the RBA. In relation to the second aspect of the Issues Paper position, the only basis on which other organisations can obtain banknotes from a BDA participant is through a commercial agreement. As previously noted, only one BDA participant has been willing to offer such a facility, on agreed commercial terms. Presumably this is because there are obligations under the BDA that make it unattractive for other BDA participants to provide access to banknotes.

The existing system of wholesale cash access adds cost to the industry. CITs and non-BDA customers are disadvantaged, and it is a suboptimal method of managing wholesale cash. The RBA should investigate options to contract directly with major CIT companies and other organisations that require access to wholesale cash.

Management of banknote pools

Under the current system, the four BDA participants each manage their own verified cash holdings (VCH) in any CIT company's Authorised Cash Centre (ACC) that they contract for services. The single largest operational cost of wholesale cash is cash movements, particularly transporting banknotes by air and land from the Reserve Bank in Victoria to ACCs, and between ACCs either intrastate or interstate. The current system does not incentivise BDA participants to trade surplus banknotes and does not operate optimally.

1. Each BDA participant only has visibility of their VCH. This creates an inefficient trading process where parties can only identify if surplus notes are available by actual requests.
2. BDA participants are typically cash positive or negative in a region. If an ACC has the right balance of BDA participants, it can create a competitive advantage in wholesale cash. In our view wholesale cash should be competitively neutral.
3. The cost of transportation of banknotes does not incentivise a participant to trade surplus notes outside of an ACC. In fact, a participant is under no obligation to trade banknotes. Often, they are better to hold notes, as a contingency. There are many examples of this, most recently the pandemic: BDA participants held onto stock of banknotes because of uncertainty around resourcing and services.

We believe a better solution would be to view banknotes as a pool of banknotes in a geographic area which can be optimised. This would lead to optimal trading and transfers, which minimises cost. This could be undertaken in various ways, with the key being that the goal is optimisation of the overall banknote pool.

There will be challenges, including VCH ownership and who or how to manage the banknote pools. These challenges are worth addressing for a more efficient industry.

Regional and remote areas in particular need a better solution. The VCH system promotes expensive movements, particularly through flights for services to gain access to banknotes and through VCH compensation.

In addition, the current system does not encourage actions to support a sustainable approach to the environment. The current system does not promote solutions that reduce physical transfers and optimise secure transportation services. it is not contributing to reducing the carbon footprint of the industry. Prosegur has a commitment to be carbon neutral by 2040, ten years ahead of the Paris Agreement. Some areas that can be considered as priorities for the industry include:

- Green fleets, lower emission and greater energy savings
- Decarbonising
- Promoting of a circular economy
- Minimise production of waste
- Reuse of elements of the system

This review is a wonderful opportunity to work with the industry and Government to play its part in achieving Australia's objectives for a sustainable environment.

In summary, the BDA should be broken up and the manner in which it operates changed:

- Optimise cash trading and movements.
- CIT companies have direct access to banknotes by contracting with the RBA.
- Note quality arrangement direct with participant.
- Maintain the system of approved CITs, ACCs, audit, procedures and compliance. The standards of the industry must remain high for safety, security, integrity of industry and confidence in banknote supply. The RBA and banks to work on stronger industry standards regarding participants.

BDA participation issues

In relation to other organisations participating in wholesale cash distribution, the Issues Paper states:

> In practice, however, there are aspects of the arrangements that may limit the ability of some organisations to enter into a BDA. For example, the nature of the BDA requirements means that participants need to have sufficient financial resources to purchase banknotes that are held in inventory in the depot system. (page 13)

The 'financial resources' make it difficult for non-ADIs to participate in the BDA. Currently, these obligations are passed on by BDA participants to CIT companies. The funding required for banknote stocks (VCH) for the two largest CIT companies is hundreds of millions of dollars each. CIT companies may not have access to such funds – even if it does, it is a substantial commitment of finite capital. It potentially takes away capital from other worthwhile investments in the industry. While the RBA would compensate the CIT company for the interest foregone, the business still needs to achieve an acceptable return for shareholders on the cash committed to the VCH. The current interest compensation is inadequate, as it is less than the cost of debt and well short of required business returns such as weighted average cost of capital. We would like to work with the RBA on finding a solution that allows major CIT companies to directly engage in the wholesale distribution system without having to commit funds to VCH holdings while still complying with the control measures and quality standards required.

In this context, it is worth considering why there is a recovery of costs attached to the supply of banknotes, and what that cost recovery should be going forward. There are historical reasons for the current position, but we now operate in an environment where we need to maintain access to banknotes to ensure businesses and parts of society are not disadvantaged. This impacts freedom of choice and financial inclusion. Prosegur is committed to working with the RBA and the Government in making banknote distribution more efficient, and continuing this critical community service.

In addition, we would argue that banknotes stored in devices such as smartsafes and recyclers with note quality sorting capability should be treated as VCH. Currently they are not classified as VCH until the banknotes are returned to an ACC and processed to acceptable note quality standards. This practice does not optimise transport operations. For example, in the case of a smartsafe, the notes cannot be accessed and will be returned to an ACC.

There is a strong case for this treatment in a range of devices and locations, particularly in regional and remote centres. This would greatly reduce cash distribution inefficiencies and costs in these areas.

Maintaining banknote quality.

Q3: What role should private participants in the banknote distribution system have in quality sorting? Are there changes that should be made to the arrangements that the Reserve Bank has in place to support the quality of banknotes in circulation?

Response summary

- The current system is working effectively.
- The RBA should contract directly with major CIT companies.
- Bank branch cash should be sorted by note quality sorting equipment.

Prosegur supports the maintaining of banknote quality. The reasons this is important are outlined in the Issues Paper and remain very relevant. Community confidence in physical cash, minimising counterfeits and the quality of notes for cash processing and dispensing equipment is a foundation stone of the cash distribution system.

Polymer notes pose their own challenge when it comes to quality sorting of banknotes and the incentive scheme has supported the necessary capital investment and resources to achieve the high standards that quite rightly the RBA and the community expects. The CIT companies commit significant resources to achieving the standards required and challenges continue. For example, the replacement, reconfiguration and testing of equipment to process the Next Generation Banknote (NGB) series requires capital expenditure and significant resource and testing. The equipment needed to process both old series and new series notes is substantial. We remain committed to these endeavours and working with the RBA to maintain high standards.

The bulk of the quality note sorting is undertaken by the CIT companies however the RBA engages with the BDA participant banks. We recommend that the RBA engages directly with the CIT companies in relation to quality sorting. The CIT companies should be a direct party agreeing the quality note sorting provisions that are agreed in BDA's. It is not ideal that CIT companies have to engage in commercial negotiations with BDA participants in relation to note quality sorting incentives and penalties when we understand the RBA's goal is to incentivise the organisations undertaking quality sorting activity.

Prosegur also believes that the issue of note quality in bank branch cash can be improved to continue achieving the high standards that are desirable. At the moment branch cash is often quality sorted by hand by the teller and the banknotes are then recycled into the market or cleared as surplus to ACCs and then recycled to market. At the ACCs these clearances are not quality sorted as this activity is required at the bank branch and deemed to be sufficient. They are then sent out to other bank branches or used by the CIT companies for services such as ATMs. We recommend that all bank branch clearances should be processed through note quality sorting equipment before being redistributed. We also raise for consideration that the auditing of bank branch note quality should be undertaken at bank branches, not just in ACCs.

In the matter of unfit notes. After many years of working through this challenge it is working effectively. We suggest a change to the BDA: the RBA should contract direct with the CIT companies. Currently, CIT companies are responsible for returning unfit notes to the RBA and we understand the RBA pays the BDA participants for this service. CIT companies then undertake commercial negotiations with BDA participants. Prosegur believes a direct relationship with the RBA is simpler and would be more effective in achieving the RBA's goals.

Our last point in this area is to address how the CIT industry is represented in Box A, The Evolution of Systems of Cash Distribution. On page 17 of the Issues Paper a table is included identified as "Stylised Models of the CIT Industry: (Scholten 2017)" In Model 4, CIT as an owner model (the most advanced CIT model) it is identified that the relationship with retailers is *"Acts as courier; CITs deposit cash with commercial banks on behalf of retailer."*

While this may be accurate for some countries this is not the model in the Australian market, the relationship is much deeper. As referenced earlier the major CIT companies have contracts with a large portion of the market including retailers, ADIs, ATM deployers, hospitality, and local government to provide a range of cash management, cash optimisation, reconciliation and reporting services as well as logistics. Most importantly the major CIT companies settle with these customers direct for cash collections and deliveries using their own banking arrangements. The customers rely on the CIT companies to pay their cash takings into their bank accounts.

The Cash-in-Transit Industry.

Q4: How have the cost structures and revenue streams of CIT companies changed as transactional cash use has declined? Are there aspects of cash distribution that have costs that are difficult to reduce as cash use declines, and how significant are these?

Response summary

- The average cash value per transport event has reduced substantially.
- Declining cash usage has resulted in lower collection volumes but demand for physical servicing within the transport network remains high.
- The industry has a high fixed cost base.
- Scale is important to industry participants.
- Major customers often request a service provider have a national network.
- The industry needs viable service providers.
- The industry should investigate solutions that address volume challenges – utility styled models, shared arrangements.
- Industry standards must be maintained. The RBA has a role to play in this area.

The Australian CIT market is characterised by a few key attributes.

- seven customers represent 60% to 70% of the market. They are the four big banks, Woolworths, Coles and Australia Post. That concentration results in strong market power.
- These seven customers typically award their cash services contract to a single CIT company for periods ranging from three to five years.
- These customers often request the service provider have a national network of ACCs & secure transport services. Declining volumes and market pressures mean many geographic areas are costly to service. Over time this will get worse, and more regions will be affected. The industry should consider alternative competitively neutral models for certain regions – utility models, shared service models, government operated models as examples.
- There are two major CIT companies. The key is that each must have sufficient volume to support a national network, which becomes more difficult as cash declines as a proportion of payments.
- Australia's geography and low population density in many areas makes the national network challenging to operate economically.
- Physical transport services have not reduced at the same rate as cash usage, resulting in reductions in the per-trip value of cash being transported.

The current market climate and declining cash usage has seen low pricing leading to unacceptable business returns for the industry. This has resulted in a stronger than normal focus on cost reduction. The Issues Paper notes that *"… banknote lodgements at major cash depots were around 55 per cent lower in September 2021 than in 2012." (page 8)* However, cash remains important for many Australians with cash usage at around 25%. The decline in volumes has led to inefficiencies often linked to the geography of Australia, time critical services and the need to provide national services.

We have provided our own analysis on cash volumes in the Introduction section of this document. Broadly we agree that there are declining cash volumes, and this is significantly impacting the industry. This industry is a scale industry. Efficiency is achieved in physical servicing when the number of services on vehicles can be maximised and density optimised. In cash depots it is banknote volume to utilise equipment and minimum labour shift requirements. Each has a high fixed cost element – for physical servicing some of these are secure armoured vehicles, security technology, minimum staffing levels for security, licensed and trained staff.

Most of the volume in the market is consolidated in seven customers. Large customers often request the service provider to have a national network. This has a high element of fixed cost attached to it and declining cash use has meant higher costs to serve. This is particularly the case in regional and remote locations which are expensive to service. Customers are reluctant to pay the real cost to service these regions.

Physical transport services are typically characterised as cash collections or deliveries. While cash usage has declined the time critical element of many services means that transport services are much more difficult to reduce. This has meant the average cash value per transport event has reduced significantly. In Prosegur's case this is even after utilising industry leading cash management and route optimisation software. Examples of time critical services are bank customer sealed bag deposits that must be processed promptly (typically on a same-day or next-day basis) and deliveries of currency to retailers to be used as change. In most retail, hospitality and government environments the change delivery is small but vitally important for the operation of the business.

Transport services are perceived as costly in circumstances where these services are often provided at unsustainably low returns for CIT providers. Capital requirements are significant to maintain safety and security. Staff must have appropriate licences and require substantial training and refresher training. The temptation is for the market to look to reduce cost through less stringent requirements. This would be a mistake. The industry needs to ensure that appropriate standards are always maintained in order to protect employees and the community. The CIT Code of Conduct should be the minimum standard that all market participants require of their service providers.

The industry pricing structure has historically seen physical transport services as loss making and subsidised by the revenue received from cash processing for each respective customer. Customers have been reluctant to pay the real cost of physical servicing and a low physical service price was seen to reduce the risk of over-servicing. The significant decline in cash volumes in more recent years without a reduction in physical servicing has placed significant stress on CIT businesses. This is an area where all participants should ensure the price of services fairly reflects the cost to ensure optimal outcomes. However due to the typical length of contracts and market expectations, including from customers with strong bargaining power, this is a challenge to achieve.

Any participant requires minimum volume to support its infrastructure and costs. Declining cash volumes, and challenges to the ability to achieve economies of scale, together with customer market power has resulted in poor business returns for the CIT industry. This will get more challenging in the years to come without structural change.

Prosegur has identified a number of initiatives in earlier questions to reduce the cost of wholesale cash and associated distribution costs. We support an evaluation of alternative models, particularly for regional and remote services that would consolidate services and cash processing to provide a more economic solution. This could take the form of a utility model, shared services model or similar.

However, the industry must maintain high standards, have viable participants, and continue to invest and innovate. We suggest that the RBA and major customers consider this important issue in the context of a market climate that does not support reinvestment in the CIT business or innovation.

A potential issue for all participants was identified in the Issues Paper:

> "Also, should the profitability of an individual CIT company fall to such an extent that it exits the market, cash distribution – and with it access to cash – could be disrupted, at least in the short term." *(page 19)*

We agree with this point and the implication that the market needs CIT companies that are viable and have sustainable profitability. The failure of one of the major CIT companies (would be likely to result in a significant and material disruption to the cash system in the short-medium term while the remaining operator absorbs or transitions that activity. This disruption could include widespread out of cash ATMs and excess holdings of cash in retail and bank branch networks and may have widespread impacts.

Historically, the major CIT companies also have supported cash as a payment method in times of crisis. Recent examples are the Global Financial Crisis (GFC) and the COVID-19 pandemic where cash demand changed significantly and with very little warning. In the GFC there was a substantial surge in cash withdrawals from bank branch networks which was managed successfully by the CIT companies. At the start of the COVID-19 pandemic, cash activity dropped significantly and then rebounded significantly in the space of 2-3 months, while cash demand surged due to cash as a store of wealth and reliable form of payment, with CIT companies again responding rapidly to the change. In times of crisis community confidence is maintained when services such as cash access are maintained. We believe this is worthy of consideration when reviewing future plans.

Banknotes are a safety net for individuals and Australia. If financial infrastructure technology fails, cash is the alternative system. In times of natural disaster such as cyclones, floods or bushfires there is always an increase in demand for cash. Again, the major CIT companies have supported the Australian economy and found solutions to any delivery challenges.

In regional and remote areas a situation could arise where one or none of the CIT companies offer services. We believe the industry should consider some of the alternative models and solutions we have put forward to prevent such a situation.

The industry must maintain high standards. The Issues Paper noted that:

> "Smaller CIT firms tend to use non-armoured ('soft-skin') vehicles, typically to undertake low-volume cash transports. Liaison suggests that demand for these services may be increasing, as day-to-day cash use declines. The Reserve Bank has little involvement with these firms as they are not involved in wholesale cash distribution." *(page 18)*

It is not just softskin operators but also courier companies that undertake cash transport. Innovation and change in service models is good if industry standards are maintained. Prosegur with some other industry participants and facilitated by the peak body for the security industry, the Australian Security Industry Association Limited (ASIAL) worked together to produce a Code of Conduct for the industry that sets minimum standards for participants. It is a voluntary code. We believe the involvement of the RBA and other industry participants would assist in ensuring the industry collectively has the right standards and regulation. We can work together to maintain high standards and minimise the risk to human life and safety.

Q5: Are there factors that prevent CIT companies repricing their services to reflect rising unit costs? If so, what are they?

Response summary

- Repricing of services is very challenging.
- Concentration of buying power.

- ➢ Scale needs of service providers results in a highly competitive environment.
- ➢ Participants need to address transport services.

We have made reference earlier to a few key points that help to answer this question. Among them:

- Concentration of buying power in a small number of banks and retailers gives them a strong negotiation position.
- The CIT market is very competitive. The competition is intense for all customers because of the desire to protect or grow market share, the need for a minimum viable volume and the need to support infrastructure and the fixed cost base.
- Long term customer contracts often do not allow pricing to be revisited based on a shift in market activity such as reduced cash per physical event.

Our experience has been that because of these elements and low inflation, price increases cannot be achieved and if anything, the opposite is the norm.

Virtually all major contracts are for a three-to-five-year term and request fixed rates for the total term of the agreement. With declining volumes, this makes the pricing worse over time. This also does not allow changes in market activity to be addressed.

A competitive marketplace is important but there are a number of elements to such an environment, beyond the number of competitors vying for customers. Customers must receive value for money. Innovation, efficiency, safety and investment are also important. We believe it is in the best interest of all to ensure the cash marketplace achieves all these important elements by ensuring the way it undertakes sourcing and the industry structures result in a sector that warrants investment.

We have previously given examples of how the price structure which cross subsidises physical cash servicing could be reviewed by participants. They could also consider splitting contracts rather than awarding to a single service provider. We believe major customers and the RBA should consider adopting a strategic role as part of sourcing that ensures service providers are able to sustainably and economically operate.

Underutilisation

Q6: Is there underutilisation in the CIT industry in Australia? If so, how widespread is it (e.g. by region or size of depot)? What is being done, or could be done, to address underutilisation?

Q7: How would you describe the business conditions and issues faced by CIT companies? Are there other strategic issues faced by current or potential participants in cash distribution that have not been covered in this paper?

Response summary

- There is underutilisation in the industry.
- Business conditions are highly competitive and financial returns poor.
- The industry should review alternative models such as utility models.
- The current environment does not support investment or innovation.

There is underutilisation in the CIT industry and this combined with market pressures is resulting in poor business returns for the industry.

We have addressed what can potentially be undertaken to address this in previous responses in this document.

The challenge for current or future participants are also covered in other areas of this response.

Responses to changes in the cash environment

Q8: To what extent do the responses described in Section 4.3 assist businesses involved in cash distribution with managing the declining transactional use of cash? What other responses are being, or could be, pursued? Are there barriers to innovation in cash distribution?

Response summary

- The physical payments landscape should be supported with innovative solutions, ensuring every part of society is fairly treated.
- The Government should mandate cash access.
- The payments landscape providers, particularly physical services are changing. It is no longer restricted to ADIs.
- The RBA needs to engage with these new providers either directly or through independent forums.
- Review the treatment of banknotes in new generation on-site devices such as Smartsafes. Incentivise the use of devices that minimise cash transportation.
- Barriers to innovation are that proponents need to be able to communicate directly with organisations such as the RBA.

The Issues Paper commentary on the shift to digital payments and responses in the market are a good snapshot of some of the changes and opportunities. The challenge is that the payments landscape participants and innovators are shifting from the traditional service providers. Other organisations beside the banks are bringing innovation to the payments space and physical cash area. It is not dissimilar to Banking and FinTechs. International models referenced in the Issues Paper plus some examples we provided in the Introduction highlight the challenge. Solutions to payments system challenges and cash distribution will come from varied sources.

The RBA and other regulators should consider direct engagement models or well-structured independent forums with these parties. It is needed as currently these parties potentially have to put in place physical cash access arrangements with parties who may see them as a competitor. In addition, the parties need to be able to propose alternate, innovative solutions directly to an organisation such as the RBA that has an overarching community responsibility.

Some important points linked to changes in the cash environment.

- Cash usage and physical banking, while reducing, continues to be an important, indeed essential, service to the community and a way to protect the most vulnerable in the community
- The removal of cash, which will increasingly happen if physical banking services reduce, will impose growing costs on business in general and small business in particular
- Physical banking has been seen to be a promoter of local economies, particularly in regional areas
- Australia is not alone in tackling these challenges, and there is international research which we can learn from to inform the ways we can address the issue

There are global models that we can review.

- Globally there are a range of models to address the need for sustainable physical banking that have been implemented or tested – Australia is not the first or only country confronting this challenge
- The needs of each country are different, and therefore the response will be country-dependent
- There is opportunity to learn and build from existing models, both to inform “best of breed” and to contextualise learnings

We have overviewed some of these in the Introduction section.

There is reference in the Issue Paper to one of the alternate models, Bank@Post, a valued solution where other banking services have been removed from a community. While it plays an important role it is one solution and there are risks and challenges with it.

- Services need to be proximal to the users of those services. To the extent possible, regional and remote communities should expect and deserve to have services that are convenient to them
- The physical banking landscape still processes a very high value of cash and a large number of customers, which means that the Bank@Post model is fundamentally inadequate for servicing the industry due to security, cost and service intensity, unless bank branch footprints remain essentially the same as they are today

- Leave-behind approaches that exist today, including the Bank@Post model, do not adequately consider customer experience, and with any growth in volumes being pointed to that channel, customer experience is likely to deteriorate substantially

The Issues Paper discusses some of the options. In relation to Smartsafes, the Issues Paper outlines some of their benefits but also adds *“It is possible that this technology could reduce the market share of the smaller CIT companies, with the new technology offering faster crediting of deposits for retailers, increased security, and improved convenience.”* Smartsafes offer far more than *“faster crediting of deposits”. (page 23)* They optimise and thus reduce the cost of handling of cash in a facility but also enhance reconciliation, reduce cash shrinkage and improve safety and security. They offer a very different service offering to the traditional CIT companies and in fact have a higher cost but give the customer a greater return on investment. The investment is not large and the smaller CIT companies could offer these to customers or the customers can buy them direct.

There is also an argument that the banknotes in Smartsafes should be considered VCH. The banknotes will be returned to a facility that satisfies note quality sorting requirements. The solution supports cash efficiency in any location but represent a great solution for localities where physical cash access is limited. They should be supported as making cash more efficient and available. This highlights that a more in depth understanding of these solutions may result in a different view and certainly a different treatment to traditional products or solutions. Direct access to the right organisations.

A very similar argument applies to Cash Recyclers. Cash Recyclers should be supported as providing efficiency and availability in the cash cycle and be treated differently to traditional cash solutions. The note sorting capability on recyclers maintains the quality of notes in circulation.

Mandate cash access. We have covered the importance of cash to many parts of society and geographies. Cash is legal tender, and it should be legislated that businesses accept cash. The only exception should be where non acceptance of cash payments is in the public interest. A case before the Court of Justice of the European Union on 26 January 2021[20] outlined this position.

One of the barriers to innovation are the lack of direct forums to review innovative solutions. Parties who wish to bring different solutions to the physical payments area should be able to raise them directly with relevant industry bodies.

Options for addressing excess capacity in the CIT industry

Q9: What are your views on the options presented in this paper – and do you have other suggestions – to make the banknote distribution system more effective, efficient, sustainable and resilient over the medium term as the use of cash for transactions declines? How might your preferred option(s) be implemented by the industry?

[20] CJEU Joined Cases C-422/19 & C-423/19 | Johannes Dietrich and Norbert Häring v Hessischer Rundfunk

Response summary

- CIT companies in Australia provide excellent service and embrace technology.
- CIT companies historically have invested to achieve RBA and industry participant goals. There is a need to ensure the business environment supports this in the future.
- There is an opportunity for coordination within the system.
- There is an opportunity for consolidation with the system for wholesale distribution – it should be competitively neutral.

1 **Participants improve distribution efficiency**. The CIT companies in Australia are some of the most advanced in the world. The level of service that has been delivered to customers is world class. The industry already utilises technology. The CIT industry has undertaken significant cost reduction in recent years. However, market conditions are poor. The risk for market participants at the moment is that, while historically CIT companies have invested and worked actively to achieve efficient cash distribution and note quality, the current environment does not support future investment.

2 **Coordination within the system**. This has got potential, particularly in regional and remote areas. Prosegur supports an investigation of options.

3 **Consolidation with the system – wholesale distribution**. Yes, we should support this with appropriate changes to BDA. Wholesale cash supply should be competitively neutral.

Changes to the operation of wholesale distribution

Q10: What are your views on changes that could be made to the current arrangements to make wholesale banknote distribution more effective, efficient, sustainable and resilient over the medium term as the use of cash for transactions declines.

Response summary

- The public sector should be more involved with the industry. Direct relationships and independent forums to support innovative solutions.
- Quality arrangements are working effectively with some improvements recommended.
- The BDA should be segmented.

We have outlined the reasons behind our views on these matters in this paper.

1 **Changing the nature of public sector involvement.** The public sector should become more involved in the sector.

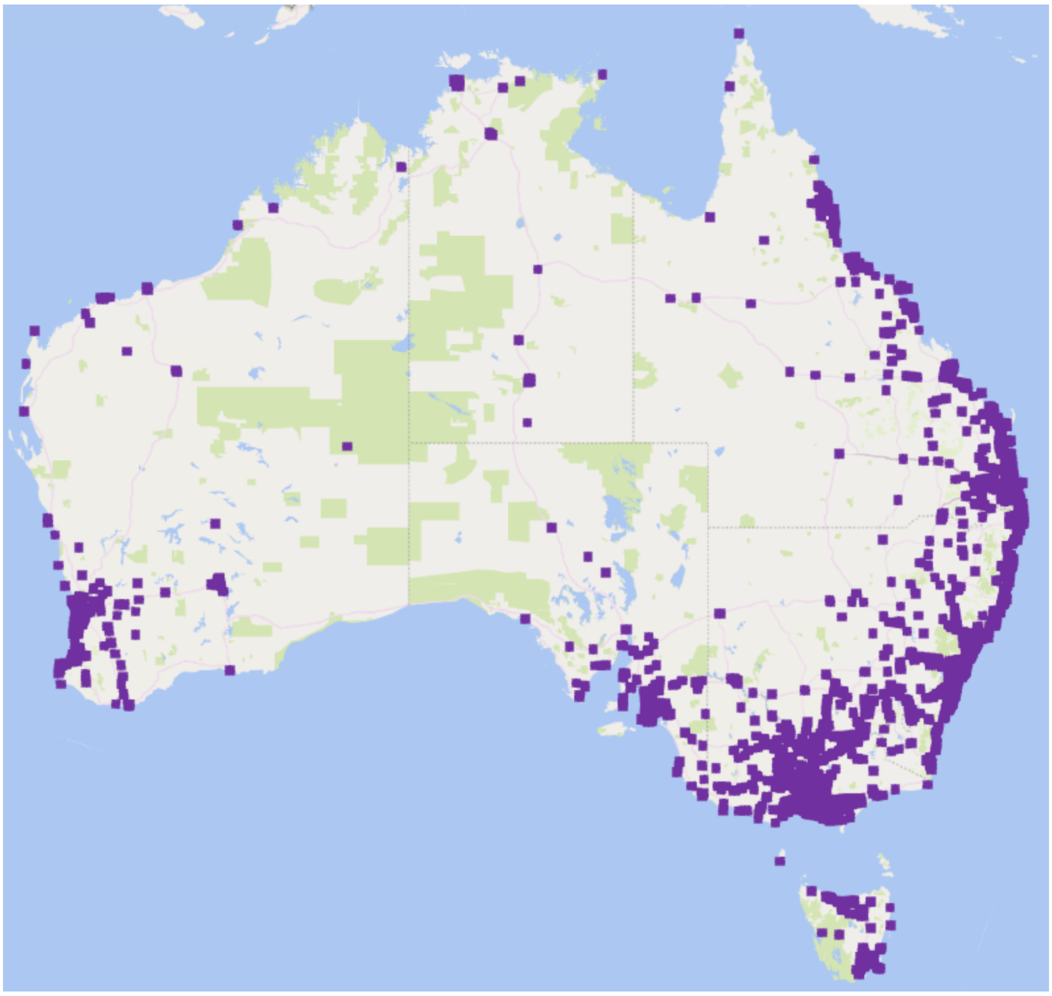
2 **Consideration of quality arrangements.** We are supportive of existing note quality arrangements. The industry must maintain high standards in all areas.

3 **Segmenting of BDA.** Prosegur is supportive of this and has identified the elements that need to be broken out in our response.

Prosegur

In Australia, Prosegur Australia Pty Limited (“Prosegur”) is a provider of cash in transit (“CIT”) services. Prosegur celebrated its 75-year anniversary last year, having been established in Australia in 1946 as the Escort and Armoured Transit Company. The business that is now Prosegur has been something of an institution in the armoured car/cash in transit sector in Australia, having previously been Transurety (1977-86), Brambles Armoured (1986-2000), Chubb Security (2000-2013), and finally Prosegur (2013 to date). Prosegur operates over 200 vehicles in Australia and has over 1,000 employees. We service well over 20,000 locations across Australia, as shown in the map at Figure 10. This includes such remote locations as Thursday Island, Nhulunbuy NT, Warburton WA, Coober Pedy SA, King Island TAS, and Norfolk Island. Prosegur provides services to communities that account for 97.2% of the Australian population.

Figure 10: Prosegur service coverage[21]



Prosegur is owned by the global Prosegur group, one of the largest security companies in the world, with over 160,000 employees and presence in 26 countries and on every continent. As part of Prosegur's global operations, we operate our "CORBAN" business in Latin America, a banking agency model with over 2,000 points of presence in Brazil, Colombia, Peru and Uruguay.

Prosegur is locally developing innovation in banking services, it's an example of a large employer in Australia developing new pathways to growth and sustainability of their business. The work Prosegur is doing in developing innovations in the banking and retail sector is intended to transition the CIT business into a range of new delivery models. In a policy sense we are looking at solutions that are a better fit for the new world of commerce and consumer behaviour that is arising through new forms of payment. The Prosegur story can be a success story of traditional industries renewing themselves and the workers employed in them being skilled for the future economy. To do this the existing banknote distribution and payment systems must evolve.

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[21] Source: Prosegur