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**BANK OF ISRAEL**

Office of the Spokesperson and Economic Information

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**Press Release:**

**The Deputy Governor: "The Digital Shekel - A Public Platform for Payment Innovation by the Private Sector"**

The Deputy Governor of the Bank of Israel, Mr. Andrew Abir, spoke at the "New World of Payments" conference organised by the Israel Securities Authority and the Bank of Israel. Here are the main points of his speech:

Today's conference focused on the revolution happening in the world of payments in Israel - a revolution we have all been planning in recent years and is now underway. In my remarks, I would like to talk about what might be the continuation of this revolution - the possible launch of a digital shekel. And there is no more suitable audience than the one here today, because for this revolution to succeed, you all need to take part.

First, let me clarify: unlike everything discussed so far at the conference, developments that will definitely happen because they have already passed the decision and legislation stage - we still cannot say for sure if there will be a digital shekel in Israel. Like all central banks in developed economies, the Bank of Israel has not yet made a final decision on the matter. The digital shekel project is an “action plan" - the project's goal is to enable us to be ready to issue the digital shekel if and when we find it appropriate and necessary. In fact, in the global discourse about central bank digital currencies (CBDCs), many argue that a CBDC is no more than a solution in search of a problem. Our decision will be greatly influenced by the extent to which we conclude that the digital shekel can be a good infrastructure for all of you to develop solutions to many problems - problems that only you know how to solve. This is what I will try to focus on today.

One of the inherent problems in the financial system in general and in the world of payments in particular is that for the system to work, a very high level of trust is required between the customer and the financial service provider. We saw this, for example, when interest rates in the economy began to rise, and the public was not satisfied with the pace of deposit interest rate increases. The public had a good alternative to deposits in the form of money market funds. They offer a better return relative to deposits and a high level of liquidity. However, we saw that the public hesitated to adopt money market funds. Why? There could be several reasons, some technical, but in my opinion, one of the main reasons is the lack of a sense of security. The public knows the banks, trusts them, and feels safe keeping their money with them. This is, of course, a good situation, but it also has negative effects on competition. This situation may also affect the ability of new payment entities to operate in the market, as the public may hesitate before agreeing to transfer some of the money they hold in banks to them. The digital shekel may be a solution to this - because the public will be able to keep their money in the digital cash of the Bank of Israel, while allowing various entities to provide advanced and competitive payment services without the public having to transfer their money to them.

First, let's remind ourselves - what is a digital shekel? A digital shekel is a liability of the Bank of Israel to the public - and in that sense, it is similar to cash, whose holding does not involve credit risk. This, unlike a bank deposit or a payments wallet, which involves a risk that may be small but not zero. On the other hand, the digital shekel is... digital, and in that sense, it is somewhat similar to the money we hold in a bank account.

First of all, the digital shekel will bring the money issued by the Bank of Israel back into all areas of our lives. In recent years, the economy has become more and more digital, and there are many types of transactions that simply cannot be paid for with cash issued by the Bank of Israel - for example, e-commerce transactions. The cash of the Bank of Israel played a role in the competition between different payment methods, but its role has been eroded due to its technological inferiority. The digital shekel will allow us to pay with Bank of Israel money everywhere, and in any transaction we choose. This will enable the Bank of Israel to intensify the competition between different means of payment.

So the digital shekel is indeed a commitment of the Bank of Israel, but it will operate in a two-tier model, with a wide range of participants who can serve as payment service providers (we call them Digital Shekel PSPs) or as Additional Service Providers (ASPs) on the digital shekel platform. In fact, the Bank of Israel will make the platform it builds accessible not only to banks, as it does today, but also to other payment companies, fintech or big tech companies, consumer clubs, retail entities, and more. Any entity operating or intending to operate under the new regulation presented at today's conference is a natural candidate to be a participant of some kind in the digital shekel system. Of course, the activities of the participants in the digital shekel will need to be supervised, but the supervision is expected to be lighter than that on the payment service providers we know, because digital shekel payment service providers do not actually hold the public's money and do not create credit and liquidity risk.

The participants in the digital shekel will first of all support the regular payment use cases we know today, but they will also be able to develop advanced and innovative use cases. I will detail some examples of use cases mentioned worldwide.

* DvP: The digital shekel can support Delivery vs. Payment use cases, where payment in digital shekels is conditional on the delivery of goods, whether physical (a package, import shipment, etc.) or digital (digital financial asset, a video, a digital book, software code, etc.). These applications can reduce the risk that exists in remote payments, which are becoming more and more common as the economy becomes more digital.
* PvP - Similarly, Payment Vs. Payment uses can also be offered - payment in digital shekels against payment in another currency or another means of payment.
* Supply Chains: Conditional payments, combined with the ability to split payments, can support various uses of supply chain financing in the B2B world. For example, a digital payment request from a goods supplier against the consumer serves as collateral for credit provision. Upon completion of the transaction, the consumer's payment is split - most of the payment to the goods supplier minus the interest paid immediately to the credit provider.
* Micropayments: The digital shekel should support ongoing payments in very small amounts. For example, a payment of fractions of a cent for a few seconds of media consumption or for charging an electric car. This capability will eliminate the need for pre-subscription to many services, including, for example, AI engines.
* Sub-wallets: Many uses can be imagined where a parent can open a sub-wallet for a child, or a company can open sub-wallets for branches or separate profit centres of the company.

What is important to note is that the Bank of Israel will not be the one offering the use cases. We have no comparative advantage in this. Our responsibility is to build the platform that will allow the private sector to generate innovation. One of the advantages of the Bank of Israel building the platform is that it will be accessible to everyone. Unlike various closed-loop systems, if a participant in the digital shekel system develops an innovative payment scenario, they can allow their customers to pay or receive his advanced type of payment from any digital shekel end-user, even if the other user is not their customer. A participant acting as an ASP can offer their services to any digital shekel end-user, even if they are not the one through whom the end-user is connected to the digital shekel. This way, we will ensure that innovation is broad and will not lead to the creation of walled gardens.

In this context, a few weeks ago, we launched the "Digital Shekel Challenge", inspired by the Project "Rosalind" carried out by the BIS Innovation Hub. For the challenge, we built a sandbox based on an API layer and invited all of you - with an emphasis on new fintech companies and established financial entities - to develop advanced and innovative use cases that will help us understand how to design the digital shekel system to support such use cases. Registration for the challenge will close in the coming days, so if you haven't done so yet - go to the Digital Shekel Challenge website today.

The contribution of the digital shekel to competition will not be limited to the world of payments. The digital shekel can also impact competition in the world of deposits. The public's ability to hold part of their money in digital shekels will put pressure on the banking system and cause banks to want to incentivise the public to keep their money with them - whether by paying interest on current accounts and higher interest on deposits, or through other added values such as better service, better technology, and the like. Additionally, the digital shekel will be built in a way that allows the Bank of Israel to pay interest directly on the public's digital shekel holdings. If today the Bank of Israel sets the interest rate in the economy and competition between banks determines the extent to which this interest is passed on to the public, such a mechanism could allow the Bank of Israel to directly influence the degree of transmission and further increase competition in the deposit market. Of course, this is a very complex issue, and it will need to be carefully thought out and designed.

So the good news is that the digital shekel can be a nationwide platform for innovation in the world of payments and make a significant contribution to competition, both in the field of payments and, if necessary, in the field of deposits. However, we are still thinking about it and planning it, and it will take time before it enters all of our lives if we decide to implement it. In the meantime, you should all start preparing for this possibility. We offer two ways to stay in touch with us regarding the digital shekel project: in the immediate term, I mentioned the Digital Shekel Challenge, and I again suggest that everyone seriously consider participating in it. On an ongoing basis, we hold forums for public consultation in the project, and you can request to join them and help us in the ongoing thinking process.

Thank you very much!