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A STUDY OF DIGITAL PAYMENTS AS DRIVERS OF ECONOMIC GROWTH

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ABSTRACT

Digital payments are increasingly central to modern economies, transforming how consumers and businesses transact. This paper examines the role of digital payments in promoting economic growth, using secondary data from cross-country studies, country-specific analyses, and macroeconomic evidence. We identify key transmission channels — financial inclusion, consumption, formalization, and productivity — and analyze empirical findings to understand both the magnitude and mechanisms of impact. We also discuss policy implications and risks.

KEYWORDS: Digital payments, Economic growth, financial inclusion, Unified Payments Interface (UPI), Mobile money, M-Pesa, Digital financial services, electronic payment systems, Informal economy, financial intermediation, Digital infrastructure, Payment innovation, Cashless economy, Fintech, GDP growth, Blockchain payments, E-commerce, Digital divide, Mobile banking, Central Bank Digital Currency (CBDC).

INTRODUCTION

Digital technologies have transformed economic interactions across the world, and payment systems are among the areas most significantly reshaped. The shift from cash-based transactions to digital modes—such as mobile wallets, instant bank transfers, QR-based payments, contactless cards, and emerging blockchain platforms—has changed how individuals, firms, and governments conduct financial activities. These tools not only improve the speed and safety of payments but also reduce operational costs and broaden access to financial services.

In contemporary economies, growth is influenced not only by capital accumulation and labor productivity, but also by how efficiently payments circulate through the economic system. Digital payment platforms help money move more quickly, lower informal cash-based practices, and create smoother conditions for business operations. In doing so, they support both inclusive and sustainable development.

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This study focuses on understanding how digital payments influence economic growth by relying solely on previously published findings, official reports, and global databases. It asks a central question:

How do digital payments contribute to economic growth, and through which channels does this impact materialize?

RESEARCH OBJECTIVE:

Primary Objective

To examine how digital payments promote economic growth using secondary data sources.

Secondary Objectives

- To identify and explain the pathways through which digital payments affect economic activity.
- To review global studies that analyze the relationship between digital payment adoption and GDP outcomes.
- To highlight country-specific examples showing the influence of digital payments on economic performance.
- To outline potential risks and policy considerations associated with expanding digital payment systems.

RESEARCH METHODOLOGY:

This research uses a qualitative synthesis of secondary information rather than primary data collection. The sources reviewed include:

- Academic journal articles
- Databases maintained by the World Bank, IMF, and other international organizations
- Publications and reports from central banks
- Data released by the Bank for International Settlements (BIS)
- National statistics on digital payments and financial systems
- Empirical studies employing methods such as VAR, ARDL, and panel data analysis

Since no surveys or fieldwork were conducted, the goal is to integrate insights from existing literature to form a comprehensive understanding of how digital payments relate to economic growth.

LITERATURE REVIEW:

Theoretical Background

Transaction Cost Theory

Digital payment systems help minimize several transaction frictions—such as delays, administrative burdens, and cash-handling expenses—which contribute to more efficient economic exchanges.

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Financial Intermediation Theory

When payments are digitized, financial institutions can mobilize resources more effectively. This improves credit allocation, supports investment, and enhances economic performance.

Innovation and Growth Theory

Technological advances, including digital financial tools, introduce new forms of productivity, stimulate entrepreneurship, and create growth opportunities.

Empirical Evidence from Existing Studies

Cross-Country Findings

Multiple international studies indicate a positive association between the rise of digital transactions and economic growth. Research analyzing large samples of countries has found that greater use of digital payments is linked with stronger GDP performance and declines in informal economic activities. Studies focusing on developing regions also highlight that digital financial inclusion—especially through mobile payments—contributes significantly to economic development when supported by appropriate institutional structures.

Country-Specific Evidence

India

- The rapid spread of the Unified Payments Interface (UPI) corresponds with increased consumer spending and higher transactions among small businesses.
- After the 2016 demonetization policy, many individuals shifted to digital payment modes, and studies observed higher spending among users who adopted digital platforms extensively.
- Time-series analysis indicates that digital payments generate noticeable short-term effects on India's real GDP growth.

China

- Platforms such as Alipay and WeChat Pay have played a major role in expanding financial services to small firms and rural populations.
- Some research suggests that the benefits of digital payment adoption vary across regions, with greater gains in areas where financial inclusion was initially low.

Turkey

- Empirical studies show long-run linkages between digital payment volumes and GDP.
- Shock analyses reveal that increases in digital transactions are followed by positive movements in economic output.

Indonesia

- Regional studies highlight that the role of digital payments strengthened further after the COVID-19 pandemic, as digital transactions became a key driver of household consumption and regional income.

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The global business environment has seen a dynamic transformation as a result of the era of ICT and digital advancements, with cash-based transactions continuously giving way to electronic ones (Mohamadetal.,2009).

The internet's widespread use and quick uptake have made electronic commerce a crucial component of the global corporate landscape. A cash-based payment system was replaced by an electronic payment solution as electronic transactions increased. A platform for paying for products or services bought online over the internet is known as an electronic payment (Roy & Sinha, 2014).

According to Kaur and Pathak (2015), a dependable and cashless payment system provides protection against theft of paper and electronic money. Other advantages of e-payments include cost savings, enhanced customer service, better working capital, increased operational efficiencies and cycle times, and processing efficiencies. According to Bezhovski (2016), mobile payments will eventually outnumber card payments. He warns that in addition to improving compatibility with a wide range of users, utilizing the newest technology, and addressing security and privacy concerns, trust and consumer habits are crucial to this expansion. According to Peter and Babatunde (2012), an electronic payment system is a type of online money transfer.

Furthermore, electronic payment is defined by Kalakota and Whinston (1997) as an online financial transaction between the buyer and supplier. Another way to think of an e-payment system is as a method of payment other than cash and checks: electronic transfers. An electronic payment system that includes electronic transfers, commercial card systems, and automated clearing houses (Lin and Nguyen, 2001). E-payments are defined by Shon and Swatman (1998) as any financial transaction started over an electronic communication channel. The global payment system is now in line with the current trend of transactions between people, companies, and governments as a result of the development of e-payment systems (Odi & Richard, 2013). Coins and paper money are gradually giving way to electronic forms in the global payment system (Premchand & Choudhry, 2015).

E-payment systems are crucial tools that people and businesses utilize to make safe and practical online payments while also opening doors to technical advancements in the global economy (Slozko & Pello, 2015). Oladeji (2014) asserts that e-payments have developed into a significant e-commerce facilitator that is essential to the success of an electronic firm. According to Premchand and Choudhry (2015), the advent of the electronic payment system has improved the global payment system's

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efficiency, decreased fraud, and increased creativity.

Economic Empowerment and Financial Integration Financial inclusion is still a key component of fair and sustainable economic growth in emerging nations where sizable portions of the populace are unbanked and outside the financial system. By offering safe, affordable, and practical financial services to underprivileged and remote populations, emerging digital payment systems have significantly increased financial accessibility (Greenland & Toth, 2024). Millions of people have been able to safely store, borrow, and transfer money thanks to these platforms, all without needing access to conventional banking infrastructure.

According to the World Bank (2024), since 2011, 1 billion individuals have accessed their accounts electronically using mobile and online platforms, demonstrating the exponential influence of the digital financial services industry on account ownership. In sub-Saharan Africa, financial inclusion and economic empowerment have been greatly aided by mobile money services, including M-Pesa in Kenya. M-Pesa adopters now have more stability and are better equipped to withstand economic shocks thanks to mobile financial services, which have completely changed household financial behavior (Chinoda & Kapapura, 2024). M-Pesa's improved access to microcredit and remittance payments has had a profound impact on poverty and women's economic independence.

Due to a network of agents with more than 300,000 service locations, M-Pesa had over 34 million active users in Kenya alone as of 2024 (TechAfrica News, 2024). This degree of coverage has further closed the inclusion gap by enabling residents of underserved and rural areas to access the necessary financial resources online. By offering other services like digital loans, savings plans, and insurance goods, the platform has also helped to promote and maintain the economy.
M-Pesa recently won the 2024 African Fintech Awards for Excellence in Financial Inclusion.

Formalization of the Economy and Taxation
In developing nations, the informal economy—which is not subject to formal taxation and regulatory oversight—remains prevalent. Due to the production of traceable digital records, transactions done through digital payment systems facilitate formal economy records and enhance tax capture (Aguilar et al., 2024).

Nearly 38% of people in rural and semi-urban areas had adopted UPI by the end of 2023, and it accounted for more than 75% of digital transactions in the retail sector (Economic Times, 2023).

There was an 8% rise in lending to subprime borrowers and a 4% increase in loans to new credit borrowers due to increased credit availability to disadvantaged populations in areas with more UPI

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usage (Times of India, 2023). All of these data suggests that digital UPI payment infrastructure may contribute to both financial inclusion and the reduction of informal economic activities. A research by the Bank for International Settlements found that a 1% rise in digital payment usage will result in a 0.06 percent decrease in informal employment (BIS, 2024). The impact of these digital platforms on the informal sector is demonstrated by the formalization of informal retail payment systems with the introduction of India's UPI system, which currently accounts for more than 80% of retail transactions (Moneycontrol, 2025).

Case Studies: Digital Rupee and UPI in India

India's payment system has completely changed since the Unified Payments Interface (UPI) was introduced, and other countries looking to create scalable and effective digital payment systems might use it as a model.

Instantaneous bank-to-bank transfers are made possible by UPI; in January 2025, an astounding 16.99 billion transactions totaling Rs. 23.48 lakh crore were reported (Financial Express, 2025). This increase in digital payments is especially noteworthy in rural areas where access to traditional banking has been restricted, underscoring the rising acceptance of digital transactions. UPI's interoperability and user-friendly design, which make it simple for both consumers and businesses to execute financial transactions, are responsible for its growth. Additionally, the Reserve Bank of India is promoting the Digital Rupee program, which encourages the use of Central Bank Digital Currency (CBCD), in conjunction with UPI. By providing a safe and reliable digital currency substitute, this initiative hopes to reduce dependency on real money and improve transaction efficiency. In line with the government's more general goals of financial inclusion, the Digital Rupee is anticipated to streamline international payments, reduce inflation, and bolster economic security (Aguilar et al., 2024).

Kenya: M-Pesa's role in promoting financial inclusion

By giving millions of unbanked people simple access to mobile money services, Kanya's M-Pesa has completely changed the financial environment. M-Pesa, which was introduced in 2007, allows users to send and receive money, pay bills, and apply for microloans straight from their mobile devices, doing away with the need for a traditional bank account. Its extensive adoption has been greatly aided by its price and user-friendly interface, especially in rural areas with few banking options. According to (Chinoda & Kapapura, 2024), M-Pesa's creative strategy has improved access to essential financial services and increased remittance flows, enabling thousands of people to transcend poverty. Additionally, by offering safe, cashless payment methods, the platform has helped small businesses expand. In addition to revolutionizing Kenya's financial landscape, M-Pesa's success has opened the door for comparable mobile money programs in Tanzania and Uganda, demonstrating the potential of

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mobile payment solutions to improve financial inclusion throughout the continent.

Conceptual Framework

Digital payments influence economic growth through several interconnected mechanisms:

Financial Inclusion

Digital platforms allow individuals to access financial services using basic mobile technology, reducing traditional barriers such as distance and cost. This facilitates savings, credit access, and formal financial participation.

Consumption and Demand

Electronic payments increase ease of use and reduce friction in transactions, encouraging more frequent and timely spending. Higher consumption supports aggregate demand.

Formalization of the Economy

Because digital transactions leave verifiable records, they discourage informal, unreported activity. As a result, governments gain more accurate tax information, and workers and firms can transition to formal structures.

Productivity and Efficiency

Digital payments reduce reliance on manual record-keeping, lower theft and cash-handling risks, and speed up business operations. Firms adopting digital systems often upgrade their management practices, improving overall productivity.

Financial Intermediation and Credit Access

Digital transaction trails provide banks and fintech companies with data that can be used to assess creditworthiness. This allows small enterprises to access credit more easily, encouraging investment and entrepreneurship.

Analysis and Discussion

Economic Growth Impacts

Short-Run Effects

Secondary studies highlight several short-term outcomes associated with expanded digital payment use, including:

- Increased consumer expenditure
- Greater transaction frequency
- Higher velocity of money
- Continuity of economic activities during external disruptions (e.g., COVID-19 lockdowns)

Evidence from countries such as India and Indonesia suggests that digital payments contribute meaningfully to short-run GDP growth, primarily through demand-side channels.

Long-Run Effects

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Long-term outcomes are less uniform and depend heavily on a country's institutional setup. Nations with well-developed regulatory frameworks and strong digital infrastructure—such as Singapore and South Korea—tend to experience larger and more persistent gains. Some studies conclude that while digital payments drive short-run growth, long-run impacts require supportive structural factors.

Sectoral Impacts

Retail and E-Commerce

Digital payments serve as a backbone for online shopping platforms, allowing quick and secure transactions and supporting the growth of digital marketplaces.

Small and Medium Enterprises (SMEs)

SMEs benefit from reduced reliance on cash and improved access to credit, as digital transaction records can be used to establish financial credibility.

Government and Public Services

Digital payment systems improve the efficiency of public transfers by reducing leakages, enabling direct benefit transfers, and strengthening tax compliance.

Challenges and Risks

Digital Divide

Not all regions or populations have equal access to technology. Areas with low connectivity, limited smartphone ownership, or low digital skills may be excluded from the benefits of digital payments.

Cybersecurity Threats

Greater reliance on digital systems exposes users to risks such as hacking, fraud, and unauthorized access to personal data.

Over-Indebtedness

In some cases, easy digital credit offerings can lead individuals into cycles of debt, especially where consumer protection frameworks are weak.

Regulatory Gaps

Inadequate regulation or lack of system interoperability can limit the effectiveness and reach of digital payment systems.

Policy Implications

Expand Digital Infrastructure

Strengthening internet connectivity, improving mobile network coverage, and promoting affordable devices are essential to ensure equitable access.

Improve Regulatory Safeguards

Regulations must protect user data, enhance system security, and ensure fair digital lending practices.

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Promote System Interoperability

Interoperable platforms—like India's UPI—enable seamless transactions across banks and applications, fostering wider adoption.

Encourage Digital Payment Usage

Governments can motivate adoption through financial incentives such as tax rebates, merchant subsidies, and rewards for digital receipts.

Enhance Financial and Digital Literacy

Educational programs help users understand the benefits and risks of digital payments, improving confidence and safe usage.

Research Gap

Although numerous studies have explored the relationship between digital payments and economic growth, several gaps remain in the existing body of literature:

1. **Limited Long-Term Evidence:**
   Most empirical studies emphasize short-run impacts of digital payments on GDP growth, often using time-series models covering relatively short periods. There is limited research examining long-term structural effects, especially in developing countries where digital payment ecosystems are still evolving.
2. **Uneven Country Coverage:**
   Existing studies are heavily concentrated in certain regions such as India, China, and a few OECD economies. Many low-income countries, small island nations, and African economies remain underexplored, despite experiencing rapid fintech adoption.
3. **Lack of Micro–Macro Linkage Studies:**
   Although firm-level and household-level data show changes in spending patterns, few studies connect these micro-level behavioral shifts directly to macroeconomic growth indicators using integrated models.
4. **Insufficient Analysis of Institutional Factors:**
   There is a gap in understanding how governance quality, cybersecurity frameworks, data protection laws, and financial regulations influence the effectiveness of digital payment systems in stimulating growth.
5. **Inconsistent Evidence on Financial Inclusion Effects:**
   While digital payments are commonly assumed to enhance financial inclusion, research outcomes vary across regions. Some studies reveal significant gains, while others show limited impact, indicating a need for more nuanced, context-specific analysis.

8. CONCLUSION

An assessment of global studies and secondary evidence shows that digital payments play a

meaningful role in economic growth. They do so by enhancing financial inclusion, supporting consumption, formalizing economic activity, improving productivity, and enabling better credit allocation. However, the full benefits of digital transactions can only be realized when supported by strong infrastructure, sound regulatory frameworks, and public trust.

With appropriate policies in place, digital payment systems can be a driving force for inclusive and sustainable economic growth, particularly in developing economies that are rapidly digitizing their financial landscapes.

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