Key success factors for delivering an effective and viable retail payments area

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European payments market at a crossroads

Technological innovations, regulatory adjustments and the increasing digitalisation of daily life have permanently altered the payments landscape in Europe, and will continue to shape it in future. The COVID-19 pandemic is fueling the ongoing technological shift transforming society, making daily life – including payments – much more digital than before. Payment behaviour in the post-coronavirus age will not completely return to what it was before the pandemic.

Technical capabilities for initiating and processing payments digitally have evolved at a rapid pace over the past few years. Playing an increasingly central role for trade in goods and services, smartphones have been a catalyst for the new business models developed and rolled out by a growing number of providers. These enterprises are capitalising on the use of data analytics, new means of accessing payment accounts and the introduction of instant payments.

Fintech and BigTech companies have attracted particular attention in this regard. These developments are putting traditional structures and existing economic principles in the payments sphere to the test. While these new developments generate efficiency gains and create a richer user experience, they also result in a tendency to operate increasingly within individual ecosystems. This could potentially lead to certain online platforms dominating the market, including where payments are concerned.

The structural change shaping European payment systems also poses new challenges for central banks, supervisory bodies and legislators. As it is, the majority of card, mobile and online payments made by Europeans already rely on technology platforms operated by global providers and based on international card schemes. In Europe, payment solutions have traditionally evolved along national borders, while global players have tended to think and act internationally.

This – in addition to increasing globalisation and growing use of the internet – has given them an initial edge in Europe, too. If an even larger share of payment transactions shifts to international providers and value and process chains span across national borders, there may be repercussions for supervisory mandates as well as implications under competition and data protection law. It remains to be seen how the decision of the European Court of Justice on the Privacy Shield will affect the European payments market.

While systems coped very well under the circumstances, the COVID-19 pandemic has emphasised how important it is for the EU to safeguard the uninterrupted functioning of essential infrastructures and the continuous provision of crucial services. Payment systems and services count among these. Reliance on non-European providers alone could jeopardise European sovereignty.

The challenge for European payment service providers is to create effective pan-European payment solutions to rival those offered by their global competitors. In response, a number of major banks, 16 so far, have proposed the European Payments Initiative (EPI), which is supported by public authorities and national central banks. This initiative could enable consumers to pay in a uniform, convenient, safe and efficient manner throughout the whole of Europe, covering both online and offline channels. Instant payments, the new service allowing bank transfers all over Europe within seconds, would form an integral part of this set-up.

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Even as banks focus on recovering from the repercussions of the COVID-19 pandemic, work should continue on pan-European payment solutions. EPI could be the decisive cornerstone for the future of the European retail payments market and is thoroughly in keeping with the political agenda in Europe.

The European Commission has made a European retail payment strategy a priority and the German Presidency of the EU is putting digitalisation high on its agenda. European private stakeholders should make the most of this momentum to pave the way for European omni-channel payment solutions that foster European sovereignty and competitiveness while fulfilling the needs of consumers and businesses. ●

Nathalie Aufauvre

General Director Financial Stability and Operations, Banque de France

The EU retail payments market must address new challenges to stay in the race

Retail payments have significantly evolved for the past ten years in Europe thanks to a favourable competitive market which stimulated innovations. The most significant evolution is their increased digitalization. European actors have made retail payments a digital activity and now offer state-of-the-art technologies. While addressing public demand and preserving consumers' choices, they set up safe online payments services, P2P payments through mobile apps or contactless payments. The COVID19 crisis also catalysed the shift to digitalized and contactless payments, inducing new payments habits that will certainly last. Meanwhile, more and more merchants try to make payment steps invisible, as illustrated by the planed disappearance of cashiers in some stores.

However, this digital evolution also sheds light on the challenges the European payment ecosystem is facing. First, despite the key achievement of SEPA, the European payment sector is still highly fragmented. Each country either has its own card scheme or rely on non-European schemes, while many banking communities have launched their own mobile payment solution with a purely domestic scope. While a significant wave of mergers has occurred in the payment industry in the US, it has only started recently in Europe. This fragmentation means a reduced profitability in a sector relying on mass effects. On the contrary, international technology companies, with a large and global customer base, benefit from network effects and can prove very competitive especially thanks to activities combined to payments (marketplaces, behavioural analysis). In addition, imperfections of the European retail payments market could strengthen this risk of marginalization of its incumbent stakeholders: the absence of an independent pan-European solution for daily payments (online or in shops), the still expensive costs of retail payment for merchants and the delayed enhancement of security for online payments expected from PSD2.

EU retail payments players still have their destiny in hand to build tomorrow's Europe of payments, as illustrated by the European Payment Initiative (EPI): a major project that will strengthen our autonomy in vital area, but which existence is conditional to a strong commitment of the concerned banking communities.

That said, they are not on their own: Central banks can and will play a key role to energize the retail payments market as permitted by their mandate. Following their oversight mission, they ensure that retail payments remain safe, functional and accessible. As catalysts, they lay the ground for a constructive cooperation between all the stakeholders. Finally, as payment operators of key market infrastructures, they have the responsibility to contribute directly to innovation, in cooperation with the private sector, in order to improve the financial system. Ensuring pan-European reachability for instant payments, experimenting wholesale MDBC or facilitating cross-border payments to reduce their cost and complexity, are in this vein.

For central bankers, their goal is not to disintermediate or to compete with the private sector but to facilitate, together with the EU market, the emergence of new tools and solutions simplifying operations for the benefit of European citizens and companies. ●

Maria Velentza

Director of Financial Services, Directorate-General for Competition, European Commission

Promoting innovative digital finance to European consumers and businesses

Digitisation is transforming the financial sector at a very rapid pace: consumers and businesses are increasingly accessing financial services digitally, market participants are deploying new technologies and business models are constantly changing. Digitisation is challenging the very structure of the financial system. The Covid-19 pandemic has further reinforced the shift to digital/contactless payments and has confirmed the vital importance of having safe and convenient payments for remote or face-to-face transactions.

In order to enhance the opportunities brought by digitisation, the EU financial sector has to adapt to the changing nature of innovation and embrace the digital revolution. With innovative EU firms in the lead, the benefits of innovative digital finance should be made available to European consumers and businesses. Moreover, pan-EU payment solutions, provided under fair competition ▶

terms, can reinforce the economic, monetary and technological sovereignty of the EU, enhance its role as a global player and contribute to financial stability.

Meanwhile, data is becoming more important for companies to compete. For security and privacy reasons as well as broader financial stability concerns, there has traditionally been little data sharing in the financial sector. The rise of FinTechs and the recent entry of Big Techs in financial services have demonstrated the potential for innovation in the financial sector; at the same time, data ownership and portability as well as interoperability of platforms will be key in determining the degree of competition in finance.

The time has come to strike a balance between security, financial stability and fair competition. Competition policy not only recognises the importance of access to data to compete, but also ensures that a level playing field is maintained, that competition takes place on the merits, and that the benefits of innovation reach consumers. Regulatory action and traditional enforcement tools work in tandem to serve these goals.

> *Digitisation is challenging the very structure of the financial system.*

In this sense, one of the priorities of the EU Commission has been to put in place a European financial data space to promote the use of digital data analytics in the context of open data policy. The EU has led the way and gathered invaluable experience in opening up data sharing with respect to payments accounts with important legislative initiatives such as the revised Payment Services Directive (PSD2). More generally, PSD2 aims to open up the market to new business models and represents a first step in the direction of a more open, collaborative and competitive EU financial sector. The EU is now ready to take further steps towards more data sharing and openness, for the benefit of consumers, businesses and public policy objectives such as the Green Deal.

Before taking such steps, regulators and policy makers will need to carefully consider the significant political and regulatory challenges that need to be addressed, such as:

- further adapting regulatory and supervisory financial services frameworks to new technologies and business models while mitigating possible new risks (e.g. cyber risk and new dependencies or third-party risks);
- promoting a well-regulated data-driven financial sector, while ensuring a level playing field; and
- ensuring innovative firms can scale up the Single Market, in particular thanks to enhanced supervisory convergence.

Sonja Scott

Country Manager Germany, American Express

Achieving an effective EU retail payments area

A long-held ambition of the EU, the creation of a truly effective retail payments area would be a major achievement, and it is at last in sight. If built on a stronger competitive foundation, it would undoubtedly help provide European consumers, businesses and merchants with greater choice.

The EU has tried many recipes to achieve its objective of a single market for EU retail payments, but to date hasn't yet found the perfect mix of ingredients. Not least, the achievement of this goal has been stymied by inadequate competition in the payments' ecosystem in the EU.

American Express have long held that, with more competition comes better services and better prices. Fundamentally we believe consumers, businesses and merchants deserve more choice. We support all efforts that are focussed on encouraging real competition to the dominant schemes – whether from fintechs, European-led initiatives or alternative models.

Indeed, addressing this issue was a central aim of the Interchange Fee Regulation (IFR). However, data from the Commission's own recent Report on the IFR shows that the market share of the dominant four-party schemes has either held the same or even increased since 2015. This has come at the expense of national schemes and alternative players, and has so far done little to advance a single retail payments area.

Still, one potential game-changer came only a few weeks ago, when the European Commission, the ECB and number of national governments publicly supported the European Payments Initiative (EPI), a new initiative by 16 European banks from 5 countries which aims at developing an EU interbank scheme based on instant payments. American Express welcomes this development. We believe that such a pan-European scheme would help to achieve one of the bloc's major policy objectives: to increase competition in the payments market, providing both consumers and merchants with greater choice in how they pay.

> *Consumers, businesses and merchants deserve more choice. We support efforts that are focussed on encouraging real competition to the dominant schemes.*

We would, however, underscore that – in a world where consumers want to shop globally – the EPI project must introduce true global interoperability, that it should be underpinned by a regulatory framework that ensures the proper economic incentives are guaranteed, and that the final product is as secure, convenient and fast as existing card payments. Failing that, it is unlikely to get the consumers' or political support and traction it needs.

Equally important, especially given the fast pace of change, we call on EU policymakers to support other initiatives in the sector that would help bring real challenge to the existing dominant players. Chief among them is doubling down on initial efforts to support Open Banking, by moving toward "Open Finance," and ensuring a truly open data economy.

Taken together, these options paint a pathway for the creation of a truly effective EU retail payments area, built on strong grounds of competition and innovation. Without them, and without a clear policy to tackle dominance in the market, these efforts may well be in vain. ●

Antony Cahill

Managing Director, Europe Regions, VISA

Open finance: the next frontier in FinTech and payments

COVID-19 has accelerated the shift to digital payments, in particular contactless payments. Notwithstanding this change in consumer behavior, more than a third of retail payment transactions in Europe are still in cash. The last five months have shown a clear appetite for consumers and businesses to embrace a world of digital payments and furthermore highlights the opportunity to increase digital payments through ongoing innovation and competition.

Open finance has and will continue to play a critical role for continued and sustained growth in this critical enabler of commerce as both innovators and regulators strive to place consumers increasingly in control of their money and financial data. New players continue to enter the market and established providers are responding accordingly with greater pace and improved services. This situation is steadily transforming the landscape in terms of players, features and price, ultimately providing consumers more choices than ever imagined. The revised Payment Services Directive (PSD2), through a focus on open access and standards, has placed Europe at the leading edge of that change.

The PSD2 regulation is designed to enable businesses to innovate in an unfettered and consistent way across the single market and overall it has been remarkably successful in achieving this aim. In a world of PSD2, companies can (with appropriate customer consent) combine their information with multiple external data sources to provide innovative and valuable customer products and services. The regulation has empowered consumers and allowed them to benefit from the best the world has to offer.

Open finance has the potential to lead to the convergence of digital payment rails ultimately leading to a real-time payment capability across all types of transaction. At the same time, Europeans will continue to have the highest expectations in relation to security, reliability, control and protection.

As Visa, we have responded by progressively opening up our ecosystem to allow participants including new (EU) Fin Techs to easily and quickly access the capabilities in our network while maintaining the highest possible standards of resilience, integrity and security. For example, our expertise in the secure authentication of sellers and buyers, and fraud prevention measures will be more important than ever in an instant payments context.

When we think about the future of payments, we should stay grounded in what consumers and businesses really need and how to manage risks in a digital environment.

In the payments world, not all transactions are the same, buying a new car or holiday is very different to buying a cup of coffee. What matters more to the consumer or business in the moment of payment is therefore very much contextual – for some it may be protection and security for others loyalty or invoice information. However, immediacy and simplicity may at times be the key attributes valued above all else.

The rapid expansion in the number and diversity of participants in the payments ecosystem has created new risks for consumers. It is important to set minimum operational safety and soundness standards, data -and cyber security standards for all payment ecosystem operators.

> *When we think about the future of payments, we should stay grounded in what consumers and businesses really need and how to manage risks in a digital environment.*

It is important for the future European Retail Payment Strategy to remain principle-based as the European payment market continues to undergo a rapid transformation. Such an approach will both encourage and enable payment participants to continue innovating and delivering for consumers and businesses.

The EU should determine specific outcome-based objectives for payment service providers such as fraud levels, security parameters, levels of market access and service delivery, but also give payment networks and companies the flexibility to deliver on these objectives.

This approach should allow Europe to stay ahead of payment innovation, while expanding the opportunities for competition, growth and innovation - which drives the best results for consumers. This will be ever more important as we move towards open finance. ●

Massimiliano Alvisini

Chief Executive Officer Europe,
Western Union

Fostering financial inclusion in the new normal

Western Union is a leader in cross-border, cross-currency money movement and payments; our customers can transfer money from one part of the world to another in seconds, transacting digitally or in cash at a retail location, or choosing cash, account or electronic wallet pay-out.

Offering all these options enables financial inclusion, but also risks misuse by bad actors—which is why Western Union invests so heavily in compliance, and why policy objectives targeting illicit money movement must account for the wide cultural and economic variability of today's global consumers.

Many of our customers are global migrants. We continuously work with different communities to deliver payment services for their unique cultural, economic and technology enabled circumstances. In that vein, we welcome the European Commission's work on an EU Retail Payments Roadmap, within the wider context of the current G20 and CMPI initiatives, at the centre of which is financial inclusion.

Financial inclusion is intrinsically linked to two things: price and technology. It's important to note that costs associated with cash transactions are significantly higher than costs related to account-based transactions, whether electronic wallets, bank accounts or cards. Besides the cost of physically distributing currency, our pricing must account for the channels through which funds move, as well as regulatory and infrastructure costs.

Western Union constantly drives technology aimed at financial inclusion. Real-time payments, for example, increase financial inclusion by improving the efficiency of financial systems; we have dramatically increased our real-time payments services. We also have increasingly digitalised our retail service, so many customers can start a transaction on our app and complete it in person at an agent location. But even as digital options increase, the majority of principal we move is still paid out in cash at retail.

The remittance sector is often deemed high risk for financial crimes; this fails to recognise the robust risk mitigation that the industry in general, and Western Union in particular, has put in place. Anti-Money Laundering compliance forms our single largest cost. We invested $1bn+ between 2015-2019 in people, processes, and technology, including predictive analytics and machine learning. We live on the bleeding edge of developments in AML/CFT, both in Europe and globally.

Our belief that the policy objectives of AML and financial inclusion must align does not entail compromises on AML. Some suggestions:

- AML rules should recognise the risk mitigation already in place. AML compliance is not a box ticking exercise; companies should be encouraged to adopt a risk-based approach, with the most resources allocated to those cases posing the most risk.
- There should be clear AML data privacy rules. AML enforcement works best where information flows both among and between the public and private sectors.
- Regulators should help reduce unnecessary compliance costs, most notably by streamlining reporting standards across the EU. This also facilitates information exchange and the use of AI and other technologies.
- Critically, we need EU-wide recognised e-ID and online KYC solutions. A universal on-boarding solution would truly offer customers the benefit of a Single Market in payment services, as well as introduce competition and drive down fees. There is no better way to foster financial inclusion. ●