

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

1. The most significant shifts and trends in the European payment area

A Central Bank official outlined that technological innovations, regulatory adjustments and the increased digitalisation of daily life have permanently altered the payment landscape in Europe and will continue to shape it into the future. The COVID-19 pandemic is fuelling the ongoing technological shift transforming society, making daily life much more digital than before.

1.1 The COVID-19 pandemic is fuelling the ongoing technological shift, but cash still has an important share in the EU

An industry representative stated that Europe has historically remained a heavy user of cash compared to many other regions. In the last three or four years there has been a significant growth in digital payments. COVID has accelerated that change. However, it is still not at the level of penetration in some economies around the world.

1.2 Trends and challenges in digital payment developments

1.2.1 Unprecedented growth in e-commerce across most European countries

An industry representative considers there has been tremendous growth in e-commerce. Visa has seen a 25% growth in e-commerce across most European countries. Contactless payments as part of the use of cards have also increased significantly. There has been a harmonisation of contactless limits across Europe. Most countries in Europe, partly as a result of COVID, have moved to a €50 limit.

1.2.2 Ever-increasing cross-border fund transfers

An industry representative considers that the financial remittance industry has been recognised as an essential service. During the pandemic most Western Union locations were able to stay open and to serve customers because cross-border payments were considered essential. Digitalisation has been a big step. In 2020 there has been triple-digit growth, and in the last three months the company's digital growth has accelerated at about the rate that would have usually been seen in the next two or three years, because people have more and more need to transfer funds electronically by downloading the mobile app.

There is a different digitalisation phase across Europe, especially in the remittance sector. It is essential that there should be innovation in order to have a seamless way to transfer funds and allow for electronic identification. Electronic ID is much more developed in northern Europe and the UK, while in other countries in southern Europe it is less developed. That did not allow many consumers to leverage the opportunity of the digital online remittance cross-border payments.

1.2.3 Technological disruption, data ownership and control challenges, varied and numerous new players in the payment landscape as well as new forms of risk

A Central Bank official considered that there are two main trends. The first one is the digitisation of the economy. It

is important to underline the introduction of disruptive technological innovation that could have a strong impact on the payment landscape and also on the economy. The development of distributed ledger technologies has made it possible to transfer value through cryptographic digital tokens and also paved the way for the creation of a new form of virtual assets, like bitcoins, stable-coins, and global stable-coins. This development could be disruptive, both for European payment players and international players.

The second trend is about the arrival of a crowd of new players. European regulation with PSD1 and PSD2 encourages the arrival of new players. It is a very positive trend to allow Fintechs to enter the market, but it has also resulted in a greater footprint of large international players and tech giants.

The current COVID-19 crisis acts as an accelerator of these trends; they carry substantial benefits for customers, who now have access to a wider array of payment solutions at a lower cost. It is also very important to take new risks into account which is why regulation needs to be adjusted over time. Operational risks also exist, such as cyber risks, fraud, anti-money laundering, and privacy.

An industry representative stated that it is important to understand how data is being used. Visa does not use data in any way that some other platforms do. One of the important things is that consumers are actually aware of their data, how their data is being used, and what the value is of their data.

1.2.4 Payment schemes add value and competition by attracting and cooperating with additional and new participants

An industry representative stated that when the European retail area is examined it would be a major achievement if there was a truly effective payments area. The Interchange Fee Regulation (IFR) report that was published in June states that the major four-party schemes either kept their market share or even gained market share, which was not the intention.

An industry representative considered that competition is good, which Visa pursues in terms of its open network strategy. It welcomes new players onto the network, but all participants in the ecosystem need to work to ensure that safety, security and resilience are maintained. AML/KYC remains something that every participant in the industry needs to be aware of. Competition is a good thing. Visa has a very close partnership with Western Union. Around 45% of small businesses in Europe today either still do not take card or cannot sell their services in an e-commerce environment. Visa has just launched a major campaign across Europe called, 'Where You Shop Matters'.

An industry representative does not see American Express as challenged; it cooperates with many players in the markets and is also cooperating and investing with fintechs so that it has a good portfolio of legacy systems and new systems.

2. EU pro-competitive policies need to follow an ongoing adaptation process

2.1 Competition policy should lead to more interoperability between more players and fintechs regarding a broader range of services than is necessary today

An industry representative would look forward to more competition in the European payment arena, which could come by giving more interoperability to more players, fintechs, or firms that could offer consumers even more than open banking. In the future it would be beneficial if people could access insurance services or any other service and then look into where the best products are offered and make this space much broader than it is at present. EPI cannot just be left to Europe.

2.2 The EU payment landscape is governed by certain regulations and competition enforcement

A policymaker stated that the Payment Services Directive is a very good step and has reshuffled the logic of business models. It regulated new services and new business opportunities. The interchange fee regulation established caps for debit cards and credit cards for interchange fees within the EU. That was complemented later on by case law with the Visa and Mastercard cases last year with respect to inter-regional fees. GDPR is about the processing of data, the free movement of data and portability.

When it comes to the application of legislation, beyond compatibility and checking whether the letter of legislation is strictly respected, implementation also has to be conform. Industry standards also need to be pro-competitive.

2.3 Competition is part of the deepening of the internal market and compatible with financial stability and other important objectives

A policymaker stated that the Commission has a variety of tools to preserve competition beyond traditional enforcement action, e.g. advocacy. It is surprising to hear people saying that legislation, policy and competition are silos which are separated. Competition is embedded in the internal market policy, cohesion policy, and interacts with financial stability. Financial services legislation and competition enforcement in that sector are complementary

2.4 The EU's competition framework feeds into legislation and consists of various tools in addition to traditional enforcement activities

A policymaker explains that experience gain through competition cases can feed into legislation. The Payment Services Directive, the Interchange Fee Regulation, and many other pieces of legislation have been built precisely on the basis of experience based on competition law. Enforcement is not simply investigating and imposing sanctions, including important fines, but there are much broader tools at the Commission's disposal. Beyond sanctioning established projects, the Commission examines projects in the making, such as Libra and Calibra or advises on projects like the EPI.

2.5 The EU's competition policy and the Central Banks, support the idea of European projects when combined with further innovation and market openness

A policymaker highlights the advocacy and advice to facilitate projects in the making. The European Payments Initiative is precisely something that the Commission has been facilitating; it supports the idea of a European project, but it is important to ensure that the governance of the

project is fair, open and does not close the market for other competitors.

A Central Bank official stated that the market is still highly fragmented. Due to this characteristic it is very difficult for European players to reach the same level of profitability and economies of scale compared to the very large players Central banks want to have competition but also want to have some European players in the field.

An industry representative commented that there are currently some very strong, dominant card schemes in certain countries in Europe such as Carte bancaire and Girocard.

A Central Bank official considered that there are three major challenges. The first one is to be able to support technological innovation which brings real benefits to users, i.e. innovation that will not lead to the creation of monopolies, innovation that will not lead to an even greater fragmentation and innovation that will not increase financial exclusion.

The second challenge is to preserve European sovereignty. It is not to have a less open economy. Payment services are crucial services; they are critical for the economy and critical for society, so they cannot only be delivered by non-European providers.

The third challenge is that Europe needs to preserve the role of central bank money as a settlement asset, not only for the financial stability of the wholesale market, but also as an anchor of stability for the retail payment market.

3. Policy priorities, ambitions and possible trade-offs

3.1 Making compliance duties consistent throughout the EU is an essential area for progress

An industry representative applauded what has been built, because the Single European Payment Area (SEPA) is quite unique. SEPA has been a great platform. It needs to be built on, because it requires additional intervention in order to facilitate financial inclusion to make payments seamless, but also particularly in the area of compliance since currently there are 27 specific requirements each time enforcing EU legislation.

3.2 Ceasing digitalisation opportunities requires that regulation has consumer convenience as a starting point

An industry representative considered the open finance piece important because American Express would like to look at it from the consumer side, the small business side, and offer services and products that they really appreciate. In every market small business are really suffering. Hard work is needed to get strong customer authentication (SCA) over the line by the end of the year. The consumer and small merchants' businesses will suffer because they will not be able to transact. More data is something that small businesses would really appreciate.

3.3 The EU must improve its agility to cease all the opportunities open by technology beyond existing legacy infrastructures

An industry representative commented that being the most advanced countries and economies is not always an advantage. A more established market like North America or Europe has a legacy and an infrastructure in place and is therefore slightly behind on new technology. In Africa Western Union has made agreements with mobile operators, and it is impressive what can be done in respecting the rules and always operating within the correct environment.

3.4 Combining financial inclusion, affordable costs for customers and AML policies require further adjusted trade-offs

An industry representative stated that the payment and cross-border industry is important for financial inclusion. Some of the regulations that are needed sometimes cannot be compatible with achieving all of the same objectives. The first is financial inclusion. The second is having AML compliance rules at the maximum standard. The third is a very affordable cost for consumers. There are some trade-offs that regulators should try to understand that are not possible.

3.5 Symmetric access to data; interoperability and portability of data; competition concerns raised by network effects and potential exclusionary conducts of certain cooperation arrangements, as well as fair access to technology, are some of the main points of attention in the field of competition policy

A policymaker stated that there are four main areas of focus: access to data; interoperability and portability of data; network effects stemming from platforms; and potential exclusionary conduct.

Companies need to have the capacity to access large amounts of data, and big techs have a significant advantage. One issue which has been brought to the Commission's attention is the alleged asymmetry in access to data between banks and Fintechs/Bigtechs. This is something that should be discussed and fixed to regulation, but any response should be proportionate, precisely in order not to create other bottlenecks. It also has to be calibrated to the specific niche and the specific area and service.

Data interoperability and portability is another issue; various ecosystems need to be able to cooperate with each other. There needs to be fluidity between those ecosystems. That can relate to licensing conditions or pricing conditions of the relevant data.

Network effects can scale businesses, but network effects can also raise competition concerns. Monopolies are not bad as long as the market power is not leveraged precisely to impede the operation of other participants or the entry of other participants in the market.

Exclusionary conduct is another issue, which means stopping innovative third parties entering a market or implementing an innovative solution. The Commission is closely examining collaboration and cooperation among market participants. As an example, cooperation between card schemes can be beneficial for consumers but should be adequately designed precisely not to exclude innovative solutions.

3.6 EU Central Banks will focus on cash, instant payment, central bank digital currency and pay particular attention to set the appropriate balance between central bank and commercial money to achieve safety and confidence, as well as competition and innovation

A Central Bank official considers that central banks can and should support innovation in the retail payment field but that cash should not be forgotten. Central banks have to be neutral; their role is to ensure that customers have access to all types of means of payment in a secured and effective way. Therefore, central banks are providers of several types of payment solutions or infrastructures. It is important to support technological innovation in a way that provides real benefits. That is why the TARGET Instant Payment Settlement Project (TIPS) has been implemented by the Eurosystem. Instant payment use-cases have still to be

developed, but that will come with digitalisation. Work has also started on the potential benefits, costs and challenges of a central bank digital currency (CBDC). As cash is a central bank money offer to the general public, the question is whether central banks should continue to provide an access to central bank money for the wider public in case of a move towards a cashless society.

When providing these kinds of services or means of payments, it is important to keep an appropriate balance between the private and the public sector. For centuries, there was central bank money on one side and commercial bank money on the other, and they co-exist. When central banks are thinking about the possible creation of a central bank digital currency, the objective is not to crowd out the private sector. a CBDC should be considered as complementary to commercial bank payment solutions. Actually, central banks are not eager to provide directly central bank money to the general public as it would require overcoming all compliance issues that need to be thought through. Central banks are very conscious that it would be not be good value to duplicate this work.

4. The European payments area five years from now

A Central Bank official hopes that the EPI project will go live and that it will be well adopted by European customers, as it would mean that a number of stakeholders and other players have agreed on the way forward. CBDC could also be in the landscape.

A policymaker stated that going cashless is unavoidable. The question is whether Europe is going to move from card-based to other types of payments. More incentives need to be examined in order to have parallel competition and other types of payments.

An industry representative was of the view that there will be more competition. There will be new entrants coming into the payments market, which is a good thing, and therefore there will be better outcomes for consumers. Digital wallets will start to play a larger role as Europe sees the growth of new payment types. Instant payments will start to play a larger role. There will hopefully be more cooperation between all participants, as it will ultimately give better outcomes for all participants.

An industry representative considered that in five years' time there will be an increase in digitalisation, but cash will still be part of the economy, with around 25% or 30% of total consumer expenditure.

An industry representative commented that consumer choice should always be protected. The goal is an ecosystem with multiple touch points where people can transfer funds electronically to a bank account, mobile wallet, or cash, but in a way that is facilitated, seamless, flexible and accessible at a very low cost to different operators.

An industry representative hoped that in five years' time Europe will have more players, more innovation, and the two dominant card players will have less than a 90% market share. ■