INSTANT PAYMENT ATTRACTIVENESS FOR EU CITIZENS

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Why instant payments are set to become the new normal

In Europe, instant payments, which allow end-users to transfer money within ten seconds at any time of any day, continue to grow. In February 2023, the average number of transactions in euros conducted daily on the pan-European platform RT1 passed the 2 million mark, which is more than 40 per cent higher than a year earlier. Nevertheless, this form of payment still accounts for a relatively low share of total settled credit transfers. According to the European Payments Council, at the end of 2022, only 14 per cent of direct credit transfers were instant payments.

Two factors are holding back their development: the fragmentation of the market on the supply side and the slow pace of change in people's habits. The different automated clearing houses (ACHs) that have adhered to the SCT Inst scheme are not able to offer full pan-European reachability on their own. Therefore, in line with objectives shared with the European Commission (EC), the ECB's Governing Council has acted to make PSPs reachable even in the absence of a connection between ACHs by requiring all PSPs and ACHs to have an account on the Eurosystem's TIPS instant payments platform (without the obligation for the PSPs to send payments to that account).

The development of a true pan-European market, made possible by the leveraging of the functionalities offered by TIPS, not only enhances the accessibility, safety and cost-efficiency of instant payments, but also paves the way for a reduction in fees, leading consumers and businesses to no longer consider instant payments as a premium service to be used in special circumstances. In this sense, the EC's recent proposal to require PSPs to ensure that the price of instant euro payments does not exceed that of non-instant transfers, and that the provision of transfers is accompanied by the provision of instant payments, is to be welcomed.

Ensuring a level playing field, increasing confidence and building on central bank money.

Leaving fees aside, people may be deterred from accessing instant payments by the perceived riskiness of the instrument. Data from a sample of Italian banks in 2021 show that, in fraud on credit transfers, the share of instant payments was much higher than that of non-instant payments. However, it is reassuring that a very large share of these frauds (92%) has been blocked or the funds recovered, thanks to a protocol between banks defined by the Italian Banking Association.

In this vein the EC has recently proposed introducing an obligation for service providers to verify, at the user's request, the correspondence between the account number (the IBAN code) and the name of the beneficiary provided by the originator. Awareness-raising campaigns for a safer use of digital channels and tools, as experienced in Italy thanks to public-private cooperation, provide another valuable means to prevent fraud.

While obstacles to a level playing field need to be overcome, other factors can stimulate the development of instant payments. Public authorities can foster them in their role as regulators, service providers and catalysts for change.

The first factor is technological progress. Mobile phones have become the main tool for using digital services. Sending and receiving instant payments can be greatly enhanced by functions such as mobile proxy look-up services, request-to-pay schemes and near field communication technologies.

Second, although it makes little sense to talk about 'use cases', because instant payments can be used in any circumstance and for any type of retail payment, there are some areas where their growth potential is greatest. One of these is payments at the point of interaction (virtual or physical). In Europe, the development of safe and efficient instant payments from customers to merchants has considerable room for growth as an alternative to cards and international circuits. Cross-border payments are another very promising field of application.

Fast payment systems (FPSs) are particularly suitable for interconnecting different currency areas, as they (i) operate 24/7, 365 days a year; (ii) process transactions in a matter of seconds; and (iii) normally use international messaging standards. This objective is being pursued by initiatives from both the private sector (e.g. the IXB pilot by EBA Clearing, TCH and SWIFT) and the public sector (e.g. TIPS's participation in Nexus, the BIS project to link FPSs with multiple currencies). Another example of synergies is a digital euro, which is meant to complement physical cash without replacing it.

A digital euro and instant payments would become complementary forms of digital payments, drawing on the same pool of people's skills and, potentially, of technologies available on the market.

Finally, instant payments are closely linked to financial innovation, and, just to give an example, are an alternative to crypto services in providing payment solutions.

We still have a long way to go to make instant payments the 'new normal', but we have made considerable progress in that direction and we have our common objectives clearly in sight.

TIM HERMANS
Executive Director - National Bank of Belgium

Instant payments as a new standard

In the payments landscape, instant payments (IPs) stand out by allowing funds to be transferred 24/7/365 and in less than 10 seconds. In this regard, IPs constitute a significant breakthrough for consumers, businesses and administrations as they can access their funds without delay. This is a clear advantage in a context of rising interest rates where cash flow management is a key concern. IPs also create great opportunities for payment service providers (PSPs) and fintechs to develop new payment solutions.

Use cases of IPs are much broader compared to traditional credit transfers. IPs should therefore be considered, not only as improved credit transfers, but as an additional payment method for many business cases. In the person-to-person sphere, IPs are used to split a bill, to pay second-hand items or to make a transfer to a relative facing an urgent and unexpected need of money. In the business-to-business sphere, IPs are used, among other use cases, for intercompany transfers driven by short-term treasury needs or for urgent correction of a payment error.

When it comes to the person-to-business sphere, notably payments at the point of interaction (PoI), the immediacy of the transactions is particularly appropriate to offer convenient payment solutions. Both at physical points of sale and in e-commerce, the deployment of IPs offers alternatives to card schemes and thereby reduces the high level of concentration currently affecting this market, especially for cross-border payments.

The offer of new payment services based on IPs is driven by private players. These, whether established or new entrants to the payments market, have the opportunity to challenge the dominant position of incumbent players who enjoy a lack of competition in some payment areas, mainly cross-border payment at the PoI. The payments industry is very innovative, IPs are logically central to its future.

In the Single Euro Payments Area (SEPA), the deployment of IPs has been made possible by the entering in effect, in November 2017, of the SEPA Instant Credit Transfer (SCT Inst) scheme of the EPC. Pan-European reachability has been achieved thanks to the creation of infrastructures such as TARGET Instant Payment Settlement (TIPS) developed by the Eurosystem and RT1 developed by EBA Clearing.

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In Q4 2022, around 61% of European PSPs joined the SCT Inst scheme and almost 14% of credit transfers are being processed instantly. It is a great step forward, but insufficient for the full materialisation of the benefits of IPs for the market. This is because a significant network effect applies to the payments market. As a matter of fact, the ability to successfully execute one type of payment does not only rely on the payer and its PSP but also on the ability of the payee's PSP to receive the payment in question.

When analysing the barriers to the widespread adoption of IPs in Europe, the fact that the level of adherence to the SCT Inst scheme have plateaued over the past four years suggests that many PSPs do not have sufficient incentive to adhere to the scheme. The insufficient level of adherence restrains the development of IP-based payment solutions, whereas the limited number of IP-based payment solutions does not incentivize PSPs to adhere. And when PSPs adhere, they often charge a premium service rate to IP users, encouraging them to turn to other payment methods. Fear of fraud and errors may also, to a lesser extent, discourage users from sending IPs. And when users initiate an IP, the rejection rate is higher than for other payment means, due to the technical challenges posed, notably the limited time for processing, particularly in the application of AML/CFT procedures.

Overcoming obstacles for faster uptake of IPs is a political priority in Europe. In October 2022, the European Commission published a proposal to amend the SEPA Regulation with the aim of fostering the adoption of IPs. The proposal provides that all PSPs that offer regular credit transfers in the SEPA must also offer IPs without surcharges. It also introduces the obligation for PSPs to offer to payers a concordance check between the IBAN and the name of the payee prior to the placement of the payment order. The proposal further introduces prescription regarding AML/CFT procedures by requiring PSPs to perform a regular pre-screening of their clients against EU sanctions lists. These checks made prior to the introduction of a payment order limit the check required during the 10-seconds limit of IPs and should consequently lower the rejection rate. The co-legislators are currently analysing and discussing the Commission's proposal.

Instant payments as the new normal should also be applicable to the digital euro, should it be created. Instant payments rails might thus provide technical convergences on which the digital euro might leverage, with a key difference though, IPs are currently settled in commercial bank money, while payments in digital euro would be settled in central bank money.

MARIANNE DEMARCHI

Chief Executive Europe - SWIFT

Enabling a better cross-border payments experience for all

The financial services landscape looks a little different to how it used to. New firms, business models and job titles now exist, evolving as fast as the markets themselves, fuelling innovation and leaving a whole host of new opportunities in their wake.

These changes have affected individual behaviour too. People are no longer limited to living in the country they work in, but instead, can run their own business from anywhere in the world. New ways of working have been driven by advances in technology, changing regulation and accelerated by the pandemic – affecting the global flow of money and the types of financial services people need. In light of these changes, international consumer and SME payment volumes have skyrocketed.

A growing market

Recent research estimates that the combined consumer-to-consumer, consumer-to-business and business-to-consumer cross-border payment segments are worth over $4tn and are expected to grow by 11% compared to last year. Data from the Swift network echoes this sentiment too, with payments under $500 currently growing twice as fast as those worth more.

Today, small businesses can reach more markets from their desks than they can from most airports, and that's partly thanks to the expansion of marketplaces like Amazon, AliExpress or Etsy. Not all businesses have the means to trade internationally, but marketplaces make it easy to capitalise on consumer demand and enable small businesses to sell their goods or services abroad. Combine that with the fact that marketplaces relieve the administrative burden associated with overseas trade, and making this move becomes a no-brainer for businesses wanting to broaden their horizons.

And it's not just SME behaviour that's changed, consumers are sending money abroad more often too. Whether it's migrants sending wages back home to support family or international students funding tuition abroad, cross-border transfers have become a normal part of everyday life for many.

Growing competition

This demand hasn't gone unnoticed. Over the past 10 years, fintechs have been emerging thick and fast, all looking to capture a piece of this market. They're backed by serious investment too, with BCG reporting that investors funnelled $11bn into payments-related fintechs in the first half of 2022 alone. And customers have clearly found their offering attractive. Fintech adoption rates have been steadily increasing and recent research found that 75% of surveyed people had used a fintech money transfer or payments service before.

Many banks are already collectively defining the new standard for low-value cross-border payments.

While the fintech offering may look a little different to what banks have traditionally provided, they still use many of the same networks and payments routes to process transfers, including the correspondent banking network. So where do the differences lie? Often, it's in the experience. Fintechs have simplified the process of sending money abroad, with a minimalist approach to user experience that requires as few steps as possible for customers to make a payment. Payments are competitively priced too, with all fees displayed upfront to give total transparency on the cost of a transfer before it's sent, avoiding any unexpected surprises when the money arrives.

Building on strengths

Banks already possess a lot of the ingredients needed to succeed in this market, including customer bases millions strong and unparalleled reach that facilitates the global movement of value. At its core, this reach is built on strong bilateral relationships that have been in place for years. And robust compliance coupled with the highest standards for financial crime prevention put customers in the safest place possible, wherever their money is heading.

As banks continue to evolve their offering to add transparency, predictability and an improved user experience into the mix, they further strengthen their relationships with their customers. And by collaborating and adopting a community-driven approach, they are most likely to succeed, both for the currencies we know today and a future that could see central bank digital currencies (CBDCs) enter the frame. With the rapid adoption of Swift Go, many banks are already collectively defining the new standard for international consumer and SME payments within an interoperable framework that lowers costs, connects multiple payment methods and channels, and delivers instant and frictionless transactions to end-users.

From instant and frictionless payments to central bank digital currencies (CBDCs), a range of new and emerging digital developments have the potential to transform the face of the cross-border landscape, alongside the industry-wide transition to the data rich ISO 20022 standard. But change doesn't happen on its own – and Swift is working closely with the financial community to build a better cross-border payments experience for all.

PERRINE KALTWASSER

Managing Director of Risks, Compliance and General Secretariat of the Financial Conglomerate - La Banque Postale

Instant payments are also an issue of European sovereignty

Banks have played a leading role in the development of SEPA payment instruments in France and Europe, but the launch of instant payment by the EPC in November 2017 did not have the success expected. Although the use of instant payments is already widespread in some Member States, such as the Netherlands, Estonia and Spain, others have been slower to adopt this technology. At the beginning of 2022, only 11% of credit transfers in the EU were made via instant payments (3% in France).

At the same time, applications allowing real-time transfers between individuals, or used to pay professionals, have experienced strong developments in recent years. Soon, all money transfers from individuals will be made in real time. The need exists, and banks must adapt to it or expose themselves to leave the market to fintechs. When it comes to usage by companies, the added value remains to be found.

In practice, we consider that the large-scale development of instant payment requires a combination of three key success factors: real value for customers, value creation for PSPs and a relevant regulatory framework.

As far as individuals are concerned, looking for immediacy and simplicity in their transactions, the issue seems clear: instant payment will necessarily replace the traditional credit transfer, but for this clientele, the question of price is crucial compared to other payment tools. This is why, at La Banque Postale, we chose to make it free in 2022.

Regarding companies, professionals and public institutions, the case is less clear. In a rapidly changing ecosystem with a lot of dedicated offers, these actors may only marginally adopt this new solution if failing to clearly see its benefits. Banks should be able to improve their reporting, adopt relevant pricing and offer more value-added services (which can be created in cooperation with fintechs) to attract customers to this payment solution.

La Banque Postale, pioneer on free instant payments for retail clients in France.

Secondly, while the European authorities put forward objectives linked with banking players' profitability, liquidity and solidity, they continue to enforce regulatory changes that put pressure on their business models. Banks will only promote instant payment, even in the wake of binding regulations, if it is relevant for them. A payment system cannot be built and run for free. It must therefore create value for PSPs: the economic model should be sustainable to finance IT developments and investments for banks, and the costs of compliance monitoring and anti-fraud measures in real time for these operations.

Finally, the regulatory framework should favor the large-scale development of this payment solution. However, the optional membership of banks to the SCT Inst scheme, particularly in reception, raises a concern in terms of reachability of all banks in Europe. The Commission's proposal is interesting on this topic, even if in France, 95% of payment accounts held by French payment services providers can issue and receive instant payments. In addition, current anti-money laundering policies for cross-border transactions are still a significant barrier to transparent and seamless instant payments. Still, we welcome the Commission's position to facilitate these payments by making less burdensome anti-money laundering controls in Europe.

La Banque Postale has chosen to actively promote the instant payment, in line with its principles as a citizen bank. It promotes immediacy, efficiency and quality of service to the benefit of its customers. To develop its use, we were the first major French bank to make this product free of charge for retail customers.

Beyond the needs of a demanding and competitive payments market, the development of instant payment in Europe is also a way to support Europe's ambition to regain sovereignty in the field of payments.

Instant payment is a major progress, bringing efficiency in many use cases, whether they are linked to P2P payment, e-commerce or even payments at physical points of sale, currently paid for in cash or by card. It is in some way comparable to cash since the payee receives the money immediately and irrevocably. This is why La Banque Postale has supported from the beginning the European Payment Initiative, which based its development on it.

In this regard, we question the relevance and usefulness of a central bank digital currency, as proposed by the ECB. In our opinion, such an initiative does not respond to a real consumer demand or a new use case. In addition to directly competing with an efficient and market-driven payment solution, this initiative could potentially weaken European banks by shrinking their balance sheets and affecting their revenues while generating additional development and operating costs. On top of that, while the European card world is already dominated by international card schemes, the launch of a digital euro could open up European payments to major technological players based outside the European Union.