

Cecilia Skingsley: Changing payments market

Speech by Ms Cecilia Skingsley, Deputy Governor of the Sveriges Riksbank, at the Royal Institute of Technology, Stockholm, 24 November 2014.

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The market for payments is changing rapidly. Sweden is in the forefront with regard to the development and use of electronic payments. Cash has therefore met with tough competition from new, innovative methods of payment. This development is positive in many ways, but changes also entail challenges. The Riksbank is taking an active part in the work on managing these challenges to make things easier for economic agents.

Why is it important that our payments function?

We rarely think about it when we are paying for a product or service. Often we pay in the same way as we have always done and we assume that this will work. It is rather like walking or cycling – we can think about something else while we are doing it.

Nevertheless, all of the day-to-day payments are very important to us – they give us access to the goods and services we need in our daily lives. But all payments mean that we are using highly-specialised services. Behind every non-cash payment we make there are intermediaries mediating the payment from payer to payee. This is done within an infrastructure of various technical systems that are necessary to make the payment. The intermediaries and infrastructure that are required depend on which means of payment is chosen. It is therefore very relevant to talk about payments as a consumption of payment services. An efficiently-functioning market for payment services assumes that payment services meet certain important requirements.

Three important requirements of retail payment services

Firstly, the payment service must be safe, but this is not enough. It must also be perceived as safe. Both the payer and the payee must feel secure, otherwise the payment service will not be used. If banknotes are easy to counterfeit, shops will not want to accept them. If cards can be easily hijacked, consumers will not want to pay with them.¹ When we pay by other means than cash, security also means that we rely on the mediator of payments that we have actually entrusted with our money.

Secondly, the payment service must be useful. It must be simple and convenient. You may remember when a card payment was made using a paper slip, with carbon in between, where you filled in the amount and signed it and showed your ID. This was not as simple and easy as the chip and PIN code in today's card terminals.

Thirdly, payment services must be accessible to households and accepted by companies and public authorities. Accessibility means it is easy to get hold of cash when you need it, that it is not too expensive or complicated to acquire a card or online banking services or that the mobile network has good cover if I want to use mobile payment or banking services. The same reasoning also applies, of course, to the recipient of a payment. Willingness to accept various types of payment may be undermined by factors such as technical problems, high costs and difficulty in depositing daily takings. Accessibility is also closely linked to uniform payments standards. The methods of payment should be predictable and this is the case if

¹ By hijacking a card, we mean skimming and similar activities where the card data is secretly scanned and then used for fraudulent purposes.

we all agree on how payments will be made. The more of us that are in agreement the better, as we can then make use of the network effects and economies of scale that are inherent in the mediation of payments. For instance, this type of unanimity means we can be fairly certain that it is possible to pay by card or in cash at the nearest shop.

The reason for a positive attitude towards innovation and development is that they enable us to have safe, efficient and accessible payment services. I believe we can all agree that it is easier to use banknotes and coins today than it was a couple of hundred years ago, and that it is easier, quicker and safer to use chips and PIN codes than paper slips for card payments. Cards are in turn preferable to cheques. What about the Swedish payments market? Does it give us payment services that are uniform, safe, efficient and accessible?

The transformation of the Swedish retail payments market

As the market changes rapidly through technological advances and through the establishment of new operators, it is important that the Riksbank follows and analyses the Swedish retail payments market. The results I am about to describe come from a telephone interview survey about households' payment behaviour that the Riksbank regularly carries out.

High accessibility and high level of confidence

If we look at the most common payment services we use when we pay at points of sale, 96% of the respondents said that they had access to cash, and almost 99% said they had access to a bank or credit card. No respondent said that they had access to neither cash nor cards. Accessibility for cards and cash is thus very high and so is the general public's confidence in them and this is reflected in the fact that both are used to a considerable extent. However, cards are being used increasingly often as a means of payment at the cost of cash.

The Riksbank also examines access to the payment services we use when we pay at a distance, for instance, our household bills.² In Sweden we mainly use various credit transfer and direct debit products for paying bills. The survey showed that almost 90% had access to online banking services and 23% had access to credit transfer using paper forms. Only 3% said they did not have access to any of these services. If we add direct debit, only 1 per cent lacked access to a payment service for paying at a distance. These payment services were also used to a large degree.

Broad access to innovative payment services

Sweden is often said to be a technology-friendly country and this is reflected in the fact that so many have access to online banking. Now, online banking services have been available for nearly 20 years, while mobile payment services are much newer. It is therefore remarkable that almost one quarter of the respondents said they had access to some form of mobile payment service.³ If we broaden the perspective somewhat and include non-traditional payment services such as payments via a third-party provider and virtual currencies such as Bitcoin, then 40% have access to one of these services.⁴ A good 23% of respondents said they had paid with one of these alternative methods in the past month. Another example is that some banks reported as early as last summer that they had more log-ins via mobile banking services than via traditional online banking services. This, as I see

² Cards can be used when paying at a distance, too, for instance for online purchases. However, the Riksbank has no confirmed statistics on these payments.

³ Examples of mobile payment services include Swish, WyWallet and SEQR.

⁴ Examples of payments via intermediary include PayPal, Klarna (payment by invoice) and direct payments that link you up directly with your online bank.

it, broad acceptance of new technology solutions is a very interesting observation to which I will return shortly.

The fact that so many people are using cards and other electronic payments is a form of proof that these services are widely available, not just for households but also for retailers and companies. There are more than 20 million cards in Sweden and just over two hundred thousand card terminals. Recently mobile card terminals and opportunities to accept card payments by mobile phone have also arisen. This chart, which shows how often households say they have *not* been able to pay by card or cash, illustrates the high level of acceptance among payees. A large majority say that they are unable to pay by either card or cash less than once a month.

Close to ATMs and good Internet connections

Cash should not only be possible to use in shops. Households also need to be able to withdraw cash and the retailer has to be able to deposit his daily takings. This makes the physical distance to service points and ATMs important. The average distance for a shop-owner to the nearest service point to deposit his daily takings is 6 km for Sweden as a whole and more than 10 km for Jämtland county, which has the longest distances. The distances for cash withdrawals are less; around 4 km for the country as a whole and around 7 km in Norrbotten county.

For electronic payments, access to the Internet is the equivalent of geographical proximity. It is also becoming increasingly important for both households and companies to have good Internet connections to be able to make and receive payments. In Sweden as a whole, around 500 households and companies are unable to have access to the Internet. Given that we are a sparsely-populated, but geographically large, country, this is nevertheless an impressively small figure.

Of course, what I have just said does not mean that individual shops and households may have much longer distances, that the fees paid by a shop-owner for card payments or for handling daily takings can be perceived as high or that it is not a problem for those who are unable to have access to the Internet. I shall shortly return to the challenges we have identified on the market, but before I do so I would like to say a few words about current trends and developments.

Trends and changes

Sweden is in the forefront

I said earlier that Sweden is in the forefront with regard to using other payment services than cash, and this is illustrated in this chart, which summarises the situation in a few selected countries.⁵ The picture that appears is that use of cash is much lower in Sweden than in most other countries and that the use of cards, primarily bank cards, is higher. The situation is roughly the same in our Nordic neighbour countries.

I mentioned earlier that Sweden is a technology-friendly country. We have an extensive infrastructure for telecommunications and a high percentage of households have Internet in their homes, are familiar with technology and have smart phones and tablets. Moreover, there is a high degree of confidence and trust between households, companies, payment intermediaries and public authorities. This chart shows an aggregate of all of these factors. It is the World Economic Forum's ranking of countries according to how well they are situated

⁵ If we look at cards and cash, it is unfortunately difficult to find good and comparable statistics. The information on other countries than Sweden is often a few years old, and the exact percentages should be taken with a pinch of salt.

with regard to utilising possibilities offered by information and communication technology. We can see that Sweden is highly placed and has been for a long time. Of course, this creates the right conditions for the payments market to develop.

Changes also create difficulties

It is positive that the market for payments is developing and can meet the new payment requirements that arise. Payments are increasingly based on technology and this trend will probably continue and expand. However, at the same time this development leads to new problems and tensions that need to be overcome. The problems we have identified include the following:

Households and companies need even better access to different payment services. The capacity in the mobile network is not always adequate to manage temporary peaks and it may then be difficult, for instance, to make a card payment for a hot dog and soft drink at a sports event attended by several thousand people. Some groups in society, such as the visually impaired and very short people, can face problems as card terminals and ATMs are not always adapted to their specific needs.

Other problems concern to a greater extent the tensions that may arise in relation to new payment services. Households may also have access to the technology needed to use a new payment service, but nevertheless prefer to use the old technology. As the latter technology becomes less accessible, tension may arise when the individual feels that his or her needs are not met. For instance, an elderly person may want to continue depositing and withdrawing cash over the counter in a bank or to pay payments there, but as fewer bank branches handle cash manually; this is becoming more difficult in practice.

There is also a risk that the market will become fragmented and by this I mean that there may be a number of different payment solutions, but that none of them is generally accepted by the payment recipients. One example could be mobile payments. If the launch of new mobile payment services continues, perhaps I as consumer will need to have a couple of different payment applications in my mobile phone to be sure of being able to pay in different shops. Similarly, the retailer will then need to subscribe to several different payment services.

Last year, an inquiry on the use of cash in Sweden was published, and earlier this autumn the commission of inquiry presented its report entitled Cash management in Sweden. This inquiry has resulted in a number of proposals and I will discuss two of them here. The first is that it is proposed that the Riksbank has overall responsibility for cash management in Sweden. The second is that the counting services of cash-in-transit companies should become subject to licence and come under financial supervision. It is recommended that the Riksbank become the supervisory authority for these operations.

The Riksbank welcomes the work of the inquiry as we consider it important that cash management in Sweden functions smoothly. We have taken part in the work of the inquiry and will now analyse the proposals put forward and respond to the submission sent out for comments.

Cash changeover positive but entails practical challenges

It is not only the banks' services that need to become more user-friendly, cost-effective and certain over time, our banknotes and coins also need to develop in the same way. When the new banknotes and coins are introduced, starting next year, the size and weight of the banknotes and some of the coins will decline and two new denominations will be introduced; the 2-krona coin and the 200-krona banknote. The banknotes and coins will thus become much more user-friendly and will be cheaper to handle. Safety is also increased through the new security features. I believe that we all agree these improvements are positive for all parties concerned. However, as with electronic payments, the introduction of the new banknotes and coins will give rise to some practical problems and friction during a transitional period.

Firstly, there is a huge amount of banknotes that are to be replaced; 300 million banknotes are to be withdrawn and around as many are to be put into circulation. For coins the figure is 500 million to be distributed in both directions. Secondly, Sweden has one of the world's most automated cash systems. This means that all appropriate equipment in Sweden must be adapted to be able to handle the new banknotes and coins. Thirdly, much of the practical changeover work will occur in the retail trade and shops, partly because this is where we use cash and partly because the banks have cut down on their cash handling. However, conditions vary considerably in the retail trade with regard to, for instance, technical equipment and security. It is necessary to ensure the entire changeover functions in a way that is felt by the general public to be simple and secure.

How should we deal with the challenges?

To summarise, one can say that there are two groups of challenges on the Swedish payments market. One concerns the slightly longer-term challenges following on from developments on the payments market, and the other concerns more near-term challenges regarding the banknote and coin changeover. Let me begin with cash and the near-term challenges.

The cash changeover 2015–2017

The Riksbank has over a long time, and since its planning began in 2008, had a dialogue with the various participants in the market regarding the banknote and coin changeover. This means that the banks, cash-in-transit companies and retail trade have been able to influence every part of the work, especially the timetable. This has been very important to the Riksbank, as we no longer play any role in the practical handling of cash. The timetable for the changeover has been divided into two stages and extends over a relatively long period, which means that all of those involved have had plenty of time to prepare.

You saw from the slides I showed earlier that the general public on the whole has relatively good access to places where they can make cash withdrawals and the retail trade has good access to service points where they can leave their daily takings, but is it at the same time a well-known fact that several of the banks have cut back on their manual cash handling. The consequence is that a number of households, perhaps those in sparsely-populated areas in particular, have had a long way to travel to the nearest bank that handles cash. This is a problem that may increase with regard to the banknote and coin changeover. The Riksbank is therefore conducting a regular dialogue with the banks on how the changeover should be managed. The banks have said that they will help their customers to the extent that they need it and that they will contribute to a smooth changeover. We are assuming that the banks will take this responsibility, but we are at the same time monitoring developments, for instance, by making a survey of access to cash services in different parts of the country. The continued dialogue with the banks will show whether the Riksbank needs to take any further measures.

Starting from 2015, we will carry out extensive information campaigns aimed at both market participants and the general public.

The effects of more electronic payments

The challenges regarding electronic payments are essentially very different. The challenges I have mentioned include shortfalls in capacity on the telecommunications network, accessibility and user problems for some vulnerable groups and possible fragmentation of some segments of the market. But there are other challenges, too. Common to these is that the Riksbank does not have any formal tools to manage the problems. Often the primary responsibility for these areas lies with another authority and often there are many different parties involved who need to cooperate to resolve the problems. For instance, the county administrative boards and the Swedish Post and Telecom Authority have the task of ensuring

that everyone has access to basic payment services. Finansinspektionen (the Swedish financial supervisory authority) has responsibility for financial supervision. The Swedish Competition Authority is responsible for ensuring there is suitable competition on the payments market, and so on. The banks, other providers of payment services and the retail trade are on different sides of the market, but their participation is often a decisive factor for bringing about a change.

The Riksbank is inviting to a new retail payments council

I believe that the Riksbank is well-positioned to take part in managing the challenges arising from a changing payments market. But as I mentioned earlier, successful management depends on the various market participants talking to one another and working together. At present, there is no suitable forum for these discussions. The Riksbank, which is a centrally-located and independent participant, can contribute by creating a forum where stakeholders can discuss and try to resolve problems on the market. This is why the Riksbank sent out an invitation to take part in a new retail payments council last week.

The idea is to bring together public authorities and market participants from both the supply and demand sides of the market. The council will not make decisions, but will act as a discussion forum that will identify and analyse problems and shortcomings on the market and propose possible ways of counteracting and resolving them. The council can thus become a joint resource for all of the parties involved. Examples of questions that may be discussed include how to improve the situation for vulnerable groups, how to remove obstacles to competition or to improve statistics. The invitation was sent to central participants in the market and to public authorities. Preferably, the council members should represent groups of participants rather than an individual participant, that is, the banks should be represented by the Swedish Bankers' Association rather than by an individual bank. We are aware that at present this excludes smaller participants who are competing with the banks and introducing innovative products on the market. But our aim is to broaden participation by having greater participation in the working groups that may operate under the council.

Nor should the Riksbank's proposals be regarded as set in stone; it must be possible for the retail payments council to develop to remain relevant and thus working methods and participation should be reviewed on a regular basis. The Riksbank intends to have a preliminary constituent meeting at the beginning of February.

The way forward involves new and old technology

To summarise: Sweden is in the forefront with regard to the development and use of cashless payment methods. This development is positive in many ways, but changes also entail challenges. The Riksbank is taking an active part in the work on managing these challenges to make things easier for the various participants in the economy.

Given this, I am convinced that we have a good basis for resolving short-term and long-term problems and frictions. The way forward is to continue refining old technology in new versions and also to create entirely new solutions. There is good scope to ensure our payment services will be even safer, more efficient, easily accessible and cheaper in the future.

Thank you!