

Cecilia Skingsley: Are non-banks reshaping the retail payments market?

Speech by Ms Cecilia Skingsley, Deputy Governor of the Sveriges Riksbank, at the conference “Non-banks in Payment Market: Challenges and Opportunities”, organised by the Bank of Lithuania and the Sveriges Riksbank, Vilnius, 8 October 2015.

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The retail payments market is undergoing a structural change, potentially unparalleled with anything we have seen in a long time. This gives rise to a number of important questions as regards competition and cooperation, regulation and where this development may take us in the long run.

An interesting and important market

The retail payments market is an interesting and important market. Important because it underpins the modern economy. If we were unable to pay in a safe and efficient way, the economy would soon grind to a halt when markets for goods and services stopped functioning. Interesting because of its rapid development. It is here the action is. On a global level, the payments market has grown by some 8 per cent a year for a decade. Growth has been higher not only in the developing world, reflecting overall higher economic growth rates, but also in Europe and North America, where it has been some four per cent annually. Given the financial crisis and the relatively low economic growth, this is a healthy growth rate.

On a global level, estimates indicate that the retail payments market is worth several hundred US billions in revenue from transactions. If we add account-related revenues and interest rate and penalty fees from credit cards, the figures increase further. With this growth rate and potential revenue, it is no wonder that the retail payments market attracts so much attention.

There are other factors that help explain why so much has happened over the last few years and that continue to drive the development. The rapid technological development of smartphones, tablets, and high-speed Internet connection is one of the most important factors. Today, approximately half of all adults in the world have a smartphone and this share is likely to increase significantly. Some 40 per cent of the global population use Internet. This technology is widespread and accessible at a reasonable cost and it has changed the way we shop. We purchase goods and services in new ways and because of this we also demand payment services that are suited to this new type of interaction. E-commerce is the prime example. This year some 38 billion e-commerce transactions will take place. We interact with e-merchants who we have no previous relationship with. We download or stream music and movies. We order taxis through a smartphone app. To maximize convenience, we demand tailored payment solutions increasingly often.

Businesses are in a similar situation. In e-commerce the purchase is often aborted if the payment method is not quick and convenient enough. They want to be able to offer payment alternatives that customers want to use.

This new technology has not only created a demand for new or improved payment services, it has also provided payment service providers with new channels through which their services can be supplied. The growing number of mobile payment services is an example of this.

A number of challenges for the banks

Banks have dominated the retail payments market for a long time and they still have a strong position. They are the “factories” of the retail payments market. They are usually

large scale and sell standardized payment services. However, they have to meet a number of challenges.

One challenge relates to the fact that banks operate on a vast scale providing payment services that can be used in a broad variety of situations. In an environment that quickly changes and where tailor-made payment solutions are increasingly demanded, it is a tall order to meet such a variety in demand. We should also remember that the core business of banks is financial services including payment intermediation. They are not technology firms even though they are heavy users of technology.

Innovation in payment services is usually not a question of inventing a wholly new payment process from account to account. Rather it is taking some service that is already out there and offering a new way of accessing that service. As an example, many mobile payment services and electronic wallets are just new ways of initiating card payments. A recent example is Apple Pay.

The possibility to create new access channels provides opportunities for nimble firms that are not banks to act as middle men and provide interfaces that facilitate the initiation of the underlying, more old-fashioned payment. Remember that payment initiation services and third-party providers have been at the centre of the discussions on the new Payment Service Directive. These firms don't compete outright with the banks and in some cases they may even directly cooperate with them.

In other cases, the non-bank may compete directly with the banks. It may even have built its own infrastructure or account structure through which it processes payments. This is most likely in cases where the non-bank already has a kind of network that it can adapt and utilize for payments. Telecom operators and Internet service providers are examples of such firms. A concrete example of such a case is M-Pesa, the mobile payment service launched by SafariCom in Kenya. Initially intended for person-to-person payments, it quickly became a success and a platform for a number of financial services.

Non-banks can also act as suppliers of services to the banks, e.g. payment switches routing the payment information or the outsourcing of back-end services such as the operation of large IT-platforms, etc. These are all essential inputs for payment intermediation.

Because non-banks can enter the payment process in so many places, we have longer and more complex payment processes with more actors involved. Banks, at least for some type of payment services, have less direct contact with the end-users. This development, whether we like it or not and depending on who we are, is a reality that we have to relate to. In this structural development in the payment market, there will be several challenges for commercial players, as well as for those of us working on the public side. Evolvement is seldom a gradual and smooth process. This gives rise to a number of interesting issues that we have the chance to address here today. It also explains the conference agenda.

Three topics for the conference

The first topic concerns the current development. How do the different market players view the evolving ecosystem? Are the banks hurt or do they benefit from the entry of non-banks as a result of an increase of payment traffic through their systems and between their accounts? Are all market players a big happy family where everyone cooperates with everyone else or is it razor-sharp competition, a dog-eat-dog market? Who, if anyone, is gaining the upper hand? I'm looking forward to learning more about this type of issue in the first session.

The second topic concerns the regulatory environment. The central role of the retail payments market for social welfare ensures that the authorities will want to promote an efficient outcome. How to balance cooperation and competition? How to ensure a level playing field and how to protect consumers? For example, is the current supervision

sufficient or will we have to sharpen it in the future? Central banks have an additional stake in this game. Cash is one of our main products and an increased supply of services from non-banks is likely to reduce its usage. On the one hand, central bank should embrace the development from an efficiency point of view. On the other, a rapid decrease in the use of cash is not without problems. This is only a few of the aspects that may be debated in the second session.

The third topic is the future and we all want to know what it will look like. Will the banks be reduced to mere suppliers of infrastructure and account holding services while other actors, the non-banks, have most of the end-user relationship? Or will the banks win by knock-out? Will the non-banks become banks over time as their activity expands? Will payment services be delivered to us by Apple? Google? Facebook? Alibaba? What about Bitcoin and its peers? Will we simply have payment services provided by an anonymous network?

In addition to having all these kinds of issue debated among representatives for market actors and authorities, we will also have the pleasure of listening to the academic perspective of Professor Charles M. Kahn from the University of Illinois.

I'm really looking forward to learning more about all these topics today.