

Benoît Cœuré: Retail payments at a crossroads

Speech by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at a joint conference by the European Central Bank and the Bank of France “Retail payments at a crossroads – economics, strategies and future policies”, Paris, 21 October 2013.

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I wish to thank Monika Hempel for her contributions to these remarks. I remain solely responsible for the opinions contained herein.

Ladies and Gentlemen,

It is a great pleasure for me to make some introductory remarks at this conference on the different roads that may lie ahead for retail payments. But first of all, I would like to thank the Banque de France for organising this conference jointly with the ECB, and for hosting it. I am also grateful to Christian Noyer for opening this event. I am sure we will spend two fruitful days having some valuable discussions and exchanges on the economics, strategies and policies of retail payments.

Four years ago, in 2009, the ECB and the De Nederlandsche Bank organised the first conference of this kind.¹ The idea behind the conference was to foster the dialogue between academics and policy-makers in the field of retail payments. The second conference was organised with the Oesterreichische Nationalbank in 2011.² And this is the third conference in the series. It shows that we are committed to build on the progress achieved and keep the dialogue going.

Before the crisis, the retail payments business went largely unnoticed as a substantial source of revenue in banking. During the crisis, as was outlined in the 2009 conference, the retail payments business had been resilient, providing reliable and regular revenues. As a result, the subsequent realisation that banks with more stable funding models were better able to cope with the crisis has led in recent years to a greater recognition of the importance of retail banking and retail payments.

Indeed, one of the conclusions drawn at the 2011 conference was that retail payments have also become more socially relevant. Businesses and individuals must have cheap and easy access to basic retail payment services in order to pursue their economic activities. The further development of retail payments is a key factor in financial inclusion. I will come back to this issue later today in my panel discussion.

That said, the social costs of retail payment instruments, including cash and non-cash payments, remain substantial, as a recent ECB study has shown. Those costs amount to almost 1% of GDP in Europe, with considerable differences from country to country.³

In the title of the conference we say that retail payments are at a crossroads. This means that the road we now follow will profoundly affect retail payment economics, strategies and policies. Different roads may appeal in different ways to the various economic actors. One possibility would be to preserve the status quo and to implement only the changes needed to comply with the existing regulatory framework. Alternatively, we could follow a road less travelled. Here, new economic actors may emerge and consumers may start to utilise more

¹ Retail Payments – Integration and Innovation. A Joint Conference by the ECB and De Nederlandsche Bank, 25–26 May 2009.

² The Future of Retail Payments: Opportunities and Challenges. A Joint Conference of the European Central Bank and the Oesterreichische Nationalbank 12–13 May 2011.

³ Schmiedel, H., Kostova, G. and Ruttenberg, W. “The Social and Private Costs of Retail Payment Instruments – A European Perspective”. ECB Occasional Paper No 137, September 2012.

personalised, simple and secure payment services and applications offered by the information and consumption channels they increasingly (and in some cases even exclusively) use, i.e. smartphones and the internet. Also, payment service providers may push forward into the uncharted territories of further retail payments integration and innovation.

I would like to elaborate on the different roads ahead, considering integration first and then innovation.

Retail payments integration

Without wanting to pre-empt, Michel Barnier's keynote speech on retail payments and their contribution to the Single Market, let me say that retail payment integration in the euro area – and in Europe – has made progress. Although there is still considerable effort to be made, we are just a few weeks away from completing the migration to new European schemes that have been developed for credit transfers and direct debits. It's a big step forward.

But progress in the field of cards has been slower. We are still far from a situation where “any card can be used at any terminal”. To ensure a level playing field, national borders for cards licensing, issuing and acquiring have to disappear, and the consistent implementation of the separation of scheme management and processing has to be ensured. Some movement in this area is expected to result from the revised Payment Services Directive and Regulation on interchange fees for cards.⁴ Regarding standardisation, despite some progress made during the last years, further work is required as recommended by the Eurosystem.

The question remains whether in future retail payments integration will be mainly a compliance-driven process or whether it can be pushed further, making electronic payments more widely used. Currently, there is evidence of cross-country convergence in the euro area, especially for cards, direct debits and credit transfers, and the speed of convergence has clearly accelerated for most of the payment instruments studied since the introduction of the single currency.⁵

Despite the convergence, however, there are still large differences in payment behaviour, starting with a choice between cash or *cashless* payments and then, say, selecting from a range of cashless payment instruments. For instance, the persistent use of cheques in some countries, even though it is steadily declining, shows that payment behaviour changes slowly. This also means that cash remains an important means of payment in the foreseeable future. Therefore, the Eurosystem continues in its efforts to protect the integrity of the euro banknotes and stay ahead of counterfeiters, e.g. with the introduction of our new series of euro banknotes, called the Europa series.

Promoting further integration of retail payments in Europe is seen as economically and socially advantageous. There is empirical evidence that initiatives to integrate and harmonise retail payment markets boost trade and consumption and benefit the whole economy.⁶ Data from 27 markets in Europe between 1995 and 2009 confirms that the shift to efficient

⁴ Proposal for a Directive on payment services in the internal market (“PSD2”, European Commission / 24 July 2013) and Proposal for a Regulation on interchange fees for card-based payment transactions (“IF Regulation”, European Commission / 24 July 2013).

⁵ See Martikainen, E., Schmiedel, H. and Takalo, T. “Convergence in European Retail Payments”. ECB Occasional Paper No 147, June 2013. Sigma convergence and conditional beta convergence for cash, debit card, credit card, direct debit, credit transfer, cheque and e-money in the 27 EU countries for 1995–2011 were measured.

⁶ Hasan, I., De Renzis, T. and Schmiedel, H. “Retail Payments and the Real Economy”. ECB Working Paper No 1572, August 2013.

electronic retail payments stimulates overall economic growth, consumption and trade. This effect is most pronounced for card payments, followed by credit transfers.

Deeper integration of retail payments is expected to bring about more price convergence among cashless retail payment instruments in the euro area, making those instruments more affordable and thereby promoting financial inclusion.

The Single Euro Payments Area (SEPA) is instrumental in this respect. Later this week, the ECB will publish the second SEPA migration report, which will highlight the progress accomplished and the remaining challenges as we come closer to the SEPA end-date of 1st February 2014 for migration to pan-European payment instruments. As recalled by the SEPA Council at its 23rd September meeting, the SEPA migration requirements set by law have to be fully respected without exception. Looking beyond the end-date, the ECB will establish and chair the Euro Retail Payments Board (ERPB) as successor of the SEPA Council to contribute to and to facilitate the creation of an integrated, competitive, innovative and level-playing field market for euro retail payments. The ambition is for the ERPB to achieve a wider membership, strengthened mandate and a more output-driven approach. I look forward to an active participation of the European Commission.

At present, financial inclusion is lower in those countries which make less use of cashless retail payment instruments.⁷ Giving more people, especially those on lower incomes, access to financial services not only adds to economic growth, but also plays a part in reducing income inequality and poverty. In this way, it can help to achieve higher social welfare. At the same time, it can integrate payment flows that currently exist outside the formal financial sector and strengthen the social role of banks. This matters enormously as Europe is emerging from a protracted crisis that has put its social model under strains and shattered public trust in the financial industry.

To sum up, I would say that there are strong economic, social and political reasons for retail payment service providers, users and regulators to aim for further retail payments integration. European regulation is essential in paving the way, but there are many other roads to follow for providers and users to reap the full benefits.

Retail payments innovation

As I said earlier, e-commerce and new communication and information media have set new challenges in terms of functionality and security for retail payments. They have also given providers of payment-related services new opportunities to compete. These chances are valuable because, as we know, competition is good for business, i.e. it should provide users with more choices and better services.

Unfortunately, these opportunities have not yet been fully exploited by the different market players. Innovative retail payment solutions in the euro area are still largely being provided by non-bank service providers, mainly for the payment initiation phase. Banks – the traditional payment service providers – are at a crossroads. They can either try to defend their existing products and leave this business segment to non-bank providers, or they can become more open and innovative. If they go down the first road, they risk ending up in the unpleasant situation of, say, bookshops confronted with the rise of online competitors. The ability to maintain a diversified business model, including through retail banking, will be key to the profitability and resilience of the European banking industry.

⁷ Around 58 million consumers over the age of 15 in the EU do not have payment accounts. The share of consumers without payment accounts is highest in RO, BG, PO, IT. (Source: Measuring Financial Inclusion, The Global Findex Database, World Bank, April 2012). The share of cash payments as a percentage of the number of payments in each country is highest in GR, BG, RO, IT (Source: Schmiedel, H., Kostova, G. and Ruttenberg, W. "The Social and Private Costs of Retail Payment Instruments – A European Perspective". ECB Occasional Paper No 137, September 2012).

One reason for adopting a defensive posture may be that, until recently, most banks heavily relied on interchange fees for cards in their business model. But this business model is being increasingly challenged in a number of countries and jurisdictions. I mentioned earlier the proposal for a Regulation on interchange fees for cards. This has the potential to break the stalemate that has occurred not only in the cards dossier but also on the innovation front. Transparency and clarity with respect to the real costs and benefits of cards and other payment instruments are vital for a harmonised and innovative European retail payments market.

Another reason for a defensive posture may be that banks face a coordination issue within their own organisations. For one thing, retail payments are often perceived as a cost centre, not as a profit centre. Moreover, innovations in retail payments require investments in IT as well as the will to challenge well-established and profitable business models. Clearly, these are not easy things to do in times of financial distress.

In the end, whoever provides innovative payment services should be mindful of two key issues. First, those services should be safe and protected against misuse. For instance, it is necessary that clear conditions are established under which payment initiation services offered by third party service providers can use access to existing online banking systems. Second, innovative services should have the potential to become pan-European solutions. If we do not think about the European dimension right from the start, in a few years' time we will face all the problems of having to merge multiple national solutions into a European framework.

I said earlier that retail payments *integration* brings benefits. The same thing applies to *innovation*. Fostering retail payments innovation is socially important as it should help to lower costs and reduce entry barriers, and promote financial inclusion among the underbanked and the unbanked.

Conclusion

I have only touched upon a number of very important issues. I am confident that today and tomorrow, these issues will be explored in greater depth. Taken together, the speakers, panellists, chairs and discussants at this conference as well as you in the audience possess a vast body of knowledge and expertise. If all those assets are put to good use in choosing the future direction, I am confident that the right road will be found.

Retail payments have reached a turning point as regards integration and innovation. As in the famous poem by Robert Frost,⁸ the road that will be travelled by will make all the difference – economically and socially.

Thank you very much for your attention.

⁸ Robert Frost (1874 – 1963): “The Road Not Taken”.