

François Villeroy de Galhau: Card payments in Europe – latest trends and challenges

Speech by Mr François Villeroy de Galhau, Governor of the Bank of France, at the Bank of France conference “Card payments in Europe – latest trends and challenges”, Paris, 18 January 2016.

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Ladies and gentlemen, Dear Yves Mersch, Dear Mario Nava,

First and foremost, on behalf of Banque de France, I would like to warmly welcome you all in Paris. I am delighted to open this conference dedicated to card payments in Europe. A large number of European actors involved in the card payments market are represented today, including regulatory authorities and market players, and I have no doubt that the debates that are going to take place will give us a valuable insight on the latest trends and the challenges they bring with them. Before leaving the floor to our speakers and panelists, I would simply like to share with you a few thoughts on two of those challenges, one addressed to the supply side of the card payments market and one to the regulatory community.

I. **First challenge: the sustainability of the dominance gained by cards as payment instruments. Will the most used payment instrument in Europe continue to rise or will it fall?**

Over the last decade, payment cards have steadily consolidated their dominance as the most used non-cash payment instruments in France and Europe. In 2014, payment cards were used for more than 47 billion transactions in the European Union, that is to say a level almost identical to the overall combined number of transactions involving credit transfers and direct debits, respectively the second and third most used payment instruments. In France, payment cards were used in more than 50% of all non-cash payments transactions, amounting to nearly 9.5 billion operations in 2014, compared to only 3 billion transactions in 2001. The specificity of card payments is that they occur for transactions of a relatively small amount (47€ in average in France), making it the strongest alternative to cash for proximity payments.

This situation is the result of years of efforts made by market stakeholders to build a secure, efficient and convenient payment instrument. The French community was at the forefront of such evolution with the early adoption in 1992 of chip for payment cards, which has been followed by the introduction and the subsequent widespread adoption of the EMV standard. This latter evolution has been the cornerstone of the uptake of payment cards by allowing fast and secure transactions through Europe. This predominance of payment cards may nonetheless be at stake nowadays, with the conjunction of three main trends that have a disruptive effect on the market: new solutions, new behaviors and players, new regulations.

First, innovative **payment solutions** based on SEPA schemes are very likely to emerge. One prime example of this possible groundswell is the preparation, under the impulse of the Euro Retail payments Board (ERPB), of a pan-European *instant* payments scheme by the European Payments Council (EPC), based on the existing SEPA Credit transfer scheme. This new scheme, which should be finalized by the end of 2016 and operational before the end of 2017, will serve the development of further innovative products, especially via smart devices, for proximity and mobile payments. This is a relevant example of how the harmonisation and standardization work done in the context of the so-called “SEPA 1.0.” for legacy payment instruments (direct debit and credit transfer) may serve as a basis for market players to develop new innovative real time and paperless payment solutions, what I would call “SEPA 2.0.”.

Secondly, we observe the emergence of **new payment behaviors and new market players**, in relation with further technological innovations. This is mostly led by the rising prominence of e-commerce, which has fundamentally changed payment usages in the last few years. The

search for a payment instrument adapted to these evolutions has first led to a wider usage of payment cards, beyond proximity transactions. These Card-not-present payments over the internet now account in France for nearly 7.5% of all card based-transactions in volume, and for 11.6% of the overall value of these transactions. Nevertheless, new technologies are gaining traction, by capitalizing on devices such as smartphones and tablets and allowing to get rid of “plastic” payment cards through virtual wallets. These general changes, which are already affecting traditional actors, are reinforced by the introduction of new players, either the much talked about “GAFA” (Google, Apple, Facebook and Amazon) or the smaller actors concentrating on niche payment services, that capitalize on these new technologies to enter the payment cards market. To be fair, this move “out of plastic” is a bit slower than forecasted some years ago: but it shall probably accelerate.

Lastly, in Europe, the third trend that is also deeply influencing the payment cards market is the current **regulatory renovation** that is taking place, notably through the implementation of the new Interchange fees regulation for card based-transactions, which was passed in April 2015. This new regulation sets, amongst other measures, maximum caps for interchange fees, 0.2% for debit card and 0.3% for credit card transactions, and the obligation to separate payment card schemes and processing entities. In doing so, this new regulation might stand as an additional game changer for traditional actors.

Such a context will no doubt incentivize traditional suppliers of payment cards solutions to find new sources of revenue, building on added-value services on top of sole payments, and possibly revising the way payments are made and processed to keep their lead in the retail payments market.

II. The second challenge I would like to comment briefly is: what role for public authorities, and especially for central banks?

The trends I just mentioned require public authorities, especially central banks, to reflect on their role to ensure that retail payments changes underway support economic growth and consumer confidence.

1) The first way central banks can help bring about such an outcome is **through their catalyst role**, by fostering due cooperation and coordination between stakeholders in areas where it is needed. This role needs to be played both at national and European levels.

In that perspective, the new Euro Retail Payments Board (ERPB) should play a pivotal role in Europe, by gathering -under the aegis of the ECB and the NCBs of the Eurosystem- actors from the supply side and the demand side to facilitate the development of an integrated, innovative and competitive market for retail payments in euro. Works on card payments have already been carried out by the ERPB, especially focusing on the next phases of standardization, to pave the way for further action by market stakeholders at European level.

Nonetheless, these initiatives have to be complemented at the national level to be effective. This is one reason why a national strategy for retail payment systems has been elaborated by the stakeholders in France last October and endorsed by the Minister of Finance. One of the main axis of the strategy aims at facilitating the use of cards for proximity payments through the modernization of card terminals and infrastructures which will boost the development of contactless payments, as a secure and efficient alternative to cash for everyday transactions. The National Payments Committee, which will take over from the National SEPA Committee shortly, will, similarly to the ERPB at the European level, involve all stakeholders under the aegis of Banque de France to foster the necessary dialogue for an effective implementation of the national strategy and feed the ERPB with input from the French community.

2) In addition to their catalyst role, central banks through their **oversight function** should aim at ensuring that competition between market participants does not translate into a race to the bottom, but rather translate into a race to the top in **terms of security**, by setting high level objectives and by overseeing that they are complied with. Indeed, while innovation is a promise

and a vector for economic growth, it is also a door open to new threats for the very security of payments and public confidence in those. Changes in the customers' usages generate new risks that may not be fully and comprehensively mitigated at the present time. I will only recall that Card-not-present payments, though accounting for "only" a little less than 12% of the overall value of card-based transactions in France, represent more than two-third of the overall value of fraudulent card-based transactions. European figures are similar. Next generations solutions may begin to emerge to protect payments thanks to the works of the industry –I am thinking about the recent launch of dynamic cryptograms for example, as well as the use of biometrics–, but they also require time and action by the regulators.

In this context, the adoption of the reviewed Payment Services Directive in December 2015 represents a major achievement. This Directive will considerably reinforce the security of payments and related services by setting in hard law and at the European level the obligation to use strong customer authentication for electronic payment transactions or payment account access. This Directive also extends the scope of the European regulatory framework to new activities such as payment initiation or account information services. ***In this respect, it is a duty for public authorities to ensure level playing field between all market players, traditional actors or newcomers, through an overarching key principle: regulate according to the risk profile of the service, not according to the nature or status of the provider.***

Banque de France has been, amongst European public authorities, a trailblazer on these security issues since the creation of the Observatory for Payment Card Security in 2001. This institution, chaired by the Governor of Banque de France since its inception, has anticipated and addressed through its works many of the challenges raised by new technologies, such as the security of remote or contactless payments or the use of biometrics as an authentication tool. Nonetheless, in the current context of dramatic transformation of the retail payments market, it seems useful to consider adjusting the Observatory. Accordingly, the scope of the Observatory is expected to be extended in the next few months in order to encompass all non-cash payments instruments, beyond cards, and provide transversal recommendations better suited to the needs of the market.

To conclude, I wish you fruitful and vivid discussions on all of these aspects, hoping this conference will provide us with a comprehensive overview of the latest trends and challenges that lie ahead of card payments in Europe, as well as with some of the different solutions that may be envisioned at the moment. I now let the floor to our keynote speakers Mr. Yves Mersch, Executive Board Member of the European Central Bank, and Mr. Mario Nava, Director for Regulation and prudential supervision of financial institutions of the European Commission, who will give us their perspective on the payment cards market at the European level.

Thank you for your attention.