

A close-up photograph of a white ceramic coffee cup filled with coffee, with a thick layer of foam on top. Steam is rising from the cup. The cup is placed on a light-colored wooden slatted table. The background is softly blurred, showing what appears to be a white chair with vertical slats. The overall lighting is warm and natural, suggesting an outdoor or brightly lit indoor setting.

SECURE, FAST, DIRECT

IT'S TIME TO WAKE UP TO
EVERYDAY BANK-TO-BANK
CONSUMER PAYMENTS

In 2018, Europe will be hit by a new wave of payment regulation, called the Payment Services Directive 2 (PSD2). This little-known acronym has broad implications for retailers operating in Europe because it will pave the way for direct bank transfers as an everyday payment option for consumers. In fact, we estimate it will capture 20 percent of customer spend away from debit and credit cards and circumvent \$1.4 billion in card scheme transaction fees.

We believe this time will be different than previous attempts to enable bank-to-bank consumer payments in Europe because the regulation mandates direct, secure, and faster access to current accounts. Consumers will no longer have to log-on to lots of different sites and apps to view their financial information or transact purchase. As well as enabling easier and simpler transactions, if a consumer has a savings account in one bank, a checking account with another, and a loan elsewhere, the consumer will be able to view everything in one place for the first time, and move money around quickly and easily.

Under PSD2, any technology-enabled consumer business, including retailers, will be able to act as a Payment Initiation Service Provider (PISP), which essentially will be the new portal between bank accounts and customer information. The hold of banks over consumer relationships will weaken, and retailers acting as PISPs will be able to build stronger relationships with customers.

We think retailers should be encouraging consumers to adopt this new type of payment. From an economic perspective, retailers should prefer payments through a bank-to-bank mechanism, as it eliminates interchange and scheme fees paid for a card transaction. In addition, the ability to initiate a payment directly from a consumer's bank account will reduce any friction in making a transaction, improving the customer experience and building loyalty. More importantly from a strategic standpoint is the data advantage this could give a business, potentially allowing them to see who else customers shop with, allowing bespoke marketing activities.

For larger-value transactions, an incentive to use a direct bank payment could be a one-off discount, funded by the savings the retailer makes by avoiding the traditional card transaction fees. Elsewhere, it could simply be because the retailer has made this type of payment the fastest and easiest way to complete a transaction.

Exhibit 1: Adoption of bank-to-bank payment will depend on payment channel and transaction type

	LARGE MERCHANTS/BRANDS		SMALL MERCHANTS/BRANDS	
	High transaction value	Low transaction value	High transaction value	Low transaction value
MOBILE/ONLINE EXAMPLES	Payment for a holiday with a major travel website	Regular payments to an app store, or online retailer	Payment for a holiday rental property	Mobile payment at a kiosk
OFFLINE POS EXAMPLES	Purchase of a vehicle at a major dealership	Contactless card payment in a grocery chain	Purchase of a luxury item from a boutique	Contactless card payment in a taxi

- Many positive opportunities to benefit from PSD2
- Neutral or mixed opportunities from PSD2
- Least likely to benefit or be affected by PSD2

Source: Oliver Wyman analysis

In Exhibit 1, we show the purchase occasions and channels where direct bank transfers are most and least likely to be adopted.

Payments made through online merchants could easily be made through this new method, but it may take longer to introduce in brick-and-mortar stores because of the upgrades required at the point-of-sale. Larger businesses with strong brands will have the most success in driving consumer adoption, due to a high degree of trust and existing loyalty schemes. It will be important for retailers to move first and move fast to offer this service, as the winners will effectively own the customer wallet, gain significant customer insights, and become an essential part of the customer’s daily life.

This open-access banking trend is already significantly advanced in other countries. In China, Alibaba created a one-stop-shop app to fulfill many consumer needs on a daily basis, such as shopping, payment, wealth management, and ordering services. Consumers keep all of their financial information in one place, can manage it easily, and can make mobile and online transactions easily.

The approach has proven extremely popular with consumers. In 2015 Alibaba's Alipay and Tencent's TenPay took over 90 percent of the mobile payments in China, worth about \$3.4 trillion, up 134 percent from the year before, according to a Bloomberg report. Alipay alone has 300 million users and conducts 80 million transactions every day. Forbes estimates that China's banks lost \$22.2 billion in deposits in 2015 to Alibaba and Tencent.

More importantly, Alibaba now has access to a vast and valuable trove of transaction data, which gives them the ability to market different products and services to consumers in a highly relevant and targeted way.

New payment methods are changing the retailing landscape. Retailers must be ready to pivot in order to thrive and succeed in the new environment. To avoid being caught out by an Alipay of Europe, we recommend retail executives consider the following: the effect of PSD2 on the retail payments landscape in the near and midterm; becoming a PISP or partnering with one; capitalizing on emerging new payment methods; and changing their operating model.

CONCLUSION

Over the coming years, both opportunities and risks will be abundant in European retail as the PSD2 legislation is clarified. Even after Brexit, the UK will not be exempt, as their Open Banking Standard is producing recommendations along similar lines. Innovations are bound to emerge, and competition will intensify, with the potential to make or break a retail business, depending on what actions its leaders take and when. The pressure is on, and the time to ask difficult questions of your retail business model and technology capabilities is now.