

The Future of EU Card Processing Revisited 2004 compared with 2010

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In mid 2004 PSE Consulting interviewed executives from 20 banks and 11 card processors and delivered a report (sponsored by Visa Europe) on “the Future of EU Card Processing” which attempted to forecast how the EU’s processing market would shape up by 2010. Six years on we can now look back and assess the prescience of the study’s conclusions and also look forward to how the market might evolve in the next five years. Has there been significant change? Is even more radical transformation expected in the future?

In 2004 plans for SEPA were just emerging. Banks and processors were cautiously optimistic that many of the barriers to entry in the fragmented EU markets would be removed by the end of 2010. There were high hopes of common systems, common platforms, convergence of card and electronic systems and many more aspirations. Sadly very few of these ambitions have been achieved. Markets remain fragmented, processors continue to operate to national standards and the concept of a common SEPA processing is still in the future

Six years ago there was almost unanimous agreement that the number of processors would shrink radically by 2010. Several of those interviewed optimistically predicted a reduction to 20 to 30 from the then 80 to 100 players. There was also a belief that the co-operative model proposed by the SiNSYS Consortium was likely to be followed by others. Since 2004 there has been a first wave of M&A and mergers primarily driven by First Data buying processing businesses in Austria, Germany, Poland, Slovakia, the Baltics and Greece. Banksys, as a processor and an acquirer, was sold to ATOS. easycash in Germany sold to Warburg Pinkus and more recently sold again to Ingenico. Link, the UK interbank ATM processor, merged with BACs to form VocaLink and similarly in Italy SSB and SIA also consolidated. Cetrel merged with the SIX Group (Telekurs) and PBS merged with BBS. Equens, on the other hand, has adopted a different strategy reflecting a co-operative concept whereby TAI, Interpay and Seceti operate as a group to deliver scale and service in multiple markets. The effect has been to reduce the number of commercial processors by 3 and interbank owned processors by 10 if mergers are included. The key driver for the interbank changes appears to be gradual Board recognition that processing companies operate best in an open commercial market decoupled from the national strategies of their owners.

Looking forward it is difficult to predict the outcome of the second round of M&A and rationalisation. There are still nine interbank owned card processing companies operating independently, plus five merged or co-operative entities. However many of these have been given licence to commercialise and offer their services across the broader European market. The effect has been to increase competition particularly in Benelux and the Nordic region. Consolidation is still expected in the German NSP sector and in the Italian GT market.

Whilst M&A has delivered some commercial benefits so far economies of scale have been slow to emerge. Only in the past two years has First Data begun to rationalise its processing centres. Similarly, SiNSYS has found developing a multi-country pan-EU platform is more complex than initially planned. Other players such as TSYS and ATOS are believed to be bringing harmonised product and common process to market during this year.

Again looking back, there was much criticism of the European Payments Council (EPC) and their plans for SEPA. Despite pressure from the European Central Bank, the European Commission and other key stakeholders, the EPC still struggles to deliver solutions for Europe's cards business. However the EPC has been highly successful in delivering SEPA for electronic payments. The SEPA Card Framework, with hindsight, now appears to be a diversion which has had little effect in removing the barriers to entry across Europe's cards processing markets. However the good news is there is general consensus that the SEPA POS Standards will be effective although implementation is some five to seven years away.

Six years ago there was much discussion over the opportunities for the processing sector to deliver card business solutions to multi-country banking. At that time there were several multi-country processing solutions in the development pipeline. In the generality, few of these initiatives have resulted in deliverable workable systems. In addition, banks who originally believed they could outsource the multi-country harmonisation problem have rethought their strategies. Some have reverted to in-house development; others have built their own internal processing operations. There is some evidence that 2004's optimism has not been realised because the processing sector has struggled to find the investment, skills and resources to build the complex systems required.

In 2004 bankers, and to a lesser degree processors, perceived regulatory intervention as one of the most important drivers for change. How right they were! But few anticipated that intervention and regulation would focus on the wholesale and investment banking sectors and not so much on retail! However there remains the threat of intervention to mandate SEPA, force scheme and processor separation and remove country barriers to entry.

In the middle of the last decade banks were sceptical about the potential of outsourcing, however over the past six years the growth in outsourcing services has continued at a steady pace. More particularly in the last two years, as a result of the recession, the number of RFI's/RFP's issued has accelerated rapidly. However there is a general perception that the easiest card business outsourcing contracts have been won over the past 20 years. The next phase will be more difficult, will require significant bespoke development and a capability to manage major projects rather than simple

migrations. The processing sector needs to improve if it is to be successful in delivering complex solutions.

Looking ahead to the next five years are the 2004 drivers for change about to change? Undoubtedly the most important change has been the rapid growth of acquiring as a major revenue generator for processors. PSE Consulting's forecast is that if RBS Worldpay is sold to a non bank then almost 45% of EU acquiring will have been transferred to the processing and non-bank sectors. A second driver for change is the need to achieve real scale and for the merged card and electronic processors (Equens, SIA-SSB, VocaLink) to develop components of a common card and electronic platform within the next seven years. A third important new driver is the demand by banks and other players for JV's and alliances. These will continue to grow significantly. A fourth driver is an increased focus in serving the merchant community and meeting their needs directly rather than through banks. A fifth driver is further consolidation, M&A and mergers. Potentially the target of 20 to 30 processors may be achieved by 2015!!

About PSE Consulting

PSE Consulting is a leading European payment business and technology consulting organisation. The company was created in 1991 by Peter Jones and operates from offices in London.

PSE Consulting is a founder member of the European Payments Consulting Association (EPCA), an association of like consultancies operating in eight European nations.

PSE Consulting provides independent advice to many of the European institutions mentioned within this article and to many other players who are currently shaping the European market place.

