SEPA Instant Credit Transfer

Payments within the European Union are shifting up a gear

Fast money

WITH USE CASES P. 13
Dear Readers,

For too long banks have sought cost savings and economies of scale for payment services and have avoided significant investments in their payment infrastructure. This reluctance to invest in future technology has come at the expense of gradually losing the customer interface to innovative players and technology companies. In fact, the newly emerging competitors were bold enough to build their innovative payment solutions on top of the existing, but outdated, banking infrastructure. However, current developments such as PSD2 and instant payments are forcing banks to update their infrastructure and enhance the traditional bank account, enabling it to become the banks’ anchor product for new and innovative solutions and services. To leverage the possibilities, instant payments should be squarely on the management agenda, not only from a technical perspective but also from a broader strategic point of view.

Sebastian Maus
Partner
Several countries in the European Union have implemented systems enabling rapid domestic payments between customer accounts at different banks. Initiatives such as Faster Payments Service in the United Kingdom and Nets in Denmark connect the majority of banks in the country and enable instant payments. However, until late 2017, a pan-European instant credit transfer scheme was lacking and customers often had to wait days for payments to be settled.

The introduction of the SEPA Instant Credit Transfer scheme – SCT Inst for short – solved the problem of delayed payments throughout the eurozone. For customers, it reduced payment transfer time to under ten seconds, enabling consumers and businesses to optimize, for example, their liquidity management (e.g. paying invoices right on time). The introduction of SCT Inst (the rules) and accompanying instant payment technology (e.g. TIPS) can help to reposition banks – and with them the traditional bank account. They could regain reputation and customer trust as a result of more transparency, and level the playing field with non-bank players such as PayPal and other financial technology (“fintech”) companies regarding innovative payment solutions.

However, we are convinced that instant payments will soon become a standard for money transfer and thus do not allow banks to differentiate. Since the start of SCT Inst, fintechs had the same chance to participate in the new scheme and offer those services to their clients.

In this report, we examine how banks can make the most of this opportunity to recapture the customer interface and claw back market share to regain pole position from non-bank competitors. But let’s remember, customers are not interested in new payment rules and technology without a clear use case. They want convenience, usability, efficiency and security.

Banks have several assets that put them in a good starting position: a large customer base, which still frequently interacts with them; experience and expertise in the areas of security, regulation and operations; and a large product range. As instant payments become little more than a convenience, banks should combine them with other products in their portfolio to create attractive solutions for customers, retail as well as corporate. Given this, we will look at some of the potential and beneficial use cases for instant payments, including point of sale (POS) payments, enhanced cash/liquidity management and flexible, instant credit products. Even more importantly, we will show how instant payments can become the technical foundation to defend the bank account as the central anchor for clients’ financial transactions.

Finally, we suggest some actions to be taken – and some to be avoided – by top management. These will help to adjust their current payment and product strategy to reflect the opportunities and risks offered by instant payments.
Payments are moving into the fast lane.

In November 2017, the European Payments Council launched SEPA Instant Credit Transfer, or SCT Inst (see p. 8). The scheme revolutionizes the way credit transfers are handled, making funds available in the target account within ten seconds, as opposed to 1-2 business days.

This development reflects customers’ demand for immediacy and transparency, a trend visible with the rise of companies such as Netflix, Uber, Amazon, Deliveroo and Spotify. Rather than offering new products, these disruptors provide a new way of delivering an existing product. The desire for instant payments is a natural extension of this expectation of immediate service.

But why did it take so long for the financial services industry to react? Prior to the introduction of SCT Inst, some individual European countries had already implemented solutions to tackle the challenge of rapid payment within their own borders. In the United Kingdom, Faster Payments Service enables real-time payments and makes it possible to provide services around the clock. Most banks in the United Kingdom are connected to the system (in 2018 around 2.0 billion payments and EUR 2.0 trillion credit transfers were processed via the platform). In Denmark, Nets launched its instant payments scheme RealTime 24/7 in 2014. It connected the entire Danish banking community and experienced rapid market uptake as a result. Not surprisingly, the Nordic region is one of the most innovative regarding payments, due to collaborative industry solutions like Swish. It has by far the highest adoption rate of digital payments in Europe. What was lacking, however, was a pan-European solution. Different rules, formats and interfaces prevented the interoperability of

Is this the opportunity banks have been waiting for?
national schemes, creating a fragmented European landscape. This ran counter to the objective of a Single Euro Payments Area (SEPA) within the European Union. Moreover, the industry did not have a standard definition of what a faster payment should be – was it a real-time payment, a near real-time payment, or a payment within a set timeframe?

The SCT Inst scheme addressed these issues, moving national and cross-border euro payments within SEPA into the fast lane. This is a welcome development for customers. More than that, it is a golden opportunity for banks to win back their reputation as innovative and trusted partners, and improve value-added service offerings to retail and corporate clients. The relevance is clear: Credit transfers, which are covered by SCT Inst, represent almost 95 percent of all payment transactions within the EU (see p. 4).

But the advantages of the new technology for banks are not immediately obvious. Instant payments will soon become little more than a convenience for financial players, a standard feature that does not offer them any medium-term or long-term competitive advantage. Moreover, financial technology (“fintech”) companies also benefit from instant payments. Indeed, fintechs and some big tech are already well ahead of banks when it comes to new technology. PayPal, for example, offered instant payment services even before the introduction of SCT Inst. In addition, the EU’s revised Payment Services Directive (PSD2), which came into force in January 2018 – just two months after SCT Inst – orders banks to open up for access by third-party providers from September 2019 onwards. Fintechs now have much more scope to further explore financial services. What can banks do to thrive in this new environment? We believe they need to leverage instant payments as part of a comprehensive approach that builds on their existing strengths: their strong customer base; their unrivalled expertise in the areas of security, regulation and operations; and most important, a broad product portfolio that offers the opportunity to combine instant payments with existing products/services. In the following section, we examine these advantages and how banks can exploit them.
In the past, the bank account was the undisputed platform for all financial transactions. Other customer payment options were virtually non-existent. This arrangement suited banks perfectly, putting them in full control of the customer interface – something they had little need to defend.

Regrettably for banks, this is no longer the case. The technology on which account-based payments are processed is outdated. The expectations of banks’ customers, be they individuals, retailers or other business clients, have also changed. Customers rely on simple, convenient, secure payment methods as an enabler and a vehicle. And banks are no longer able to meet that expectation.

The result? Banks have been hemorrhaging market share on payments to competitors such as PayPal, Venmo, Klarna, ApplePay and even credit cards. All of these offer functionalities the traditional bank account could not provide: PayPal with its aggregation of different payment methods and simple log-in by user name (convenience – who remembers his IBAN, when an email-address will do?) and password; Venmo with instant money transfers between its users (P2P); Klarna with invoice-based payments as a form of deferred payments; and credit cards, which ensure worldwide acceptance and deferred payments. Yet new payment methods still mostly rely on a bank account, linking to it in PayPal’s case or drawing funds from it in the case of credit cards. P2P offerings (like PayPal or Venmo), however, could become a threat to the traditional bank account. They are developing in the direction of a virtual account and try to “keep the money” within the system. Venmo has launched its own debit card in addition to its virtual account.

Instant payments can help banks claw back market share and relevance.
Why the bank account is still king

All current electronic payment methods are rooted in the user’s bank account.

POS

E-commerce

"Transmission" layer

NFC  NFC  QR-code

Data Input

Username + Password  Biometrics

"Form factor"

Card  Mobile phone  Apps  Card  Invoice

Visa  Mastercard  Apple Pay  Alipay  WeChat Pay  Visa  Mastercard  Klarna

e-wallet  e-wallet

Examples

Card infrastructure

Account infrastructure

Bank account
What is

The SEPA Instant Credit Transfer scheme – or SCT Inst for short – is a pan-European initiative of the European Payment Council and European Central Bank. It enables both domestic and cross-border payments in near real time.

The scheme, which is non-mandatory for banks, addresses the shift in consumer, corporate and retail expectations of payment processing.

SCT Inst covers credit transfers in euros. Sums transferred from the payee’s account are available in the beneficiary’s account in a maximum of ten seconds. Initially, transfers are limited to EUR 15,000. The system works day and night, 365 days a year, and will cover 34 European countries.

Payments are processed individually at transaction level, with no clearing and settlement process in batches, as was previously the case. Instant payments are flagged as such by the initiator or bank, and as soon as the payment service provider (PSP) sees this indication, they process, clear and settle the payment immediately. SCT Inst is considerably simpler than current payment models, involving fewer players and interactions. It will make transactions more efficient and less expensive in the long run.

The new scheme ensures interoperability across euro countries and financial systems, and does not require end customers in the transaction to sign up to a new system or provider. By contrast, non-banks’ payment systems often lack such extended interoperability. Thus, it is easy to exchange money between peers using the same non-bank provider, but less easy if the person you need to send money to does not have the same provider. SCT Inst requires the payment provider to comply with the new scheme and sets no further requirements for the end customer. The scheme enables the end customer to make convenient instant account-to-account payments.
However, the introduction of SCT Inst gives banks an opportunity to reinvent the traditional account. Instant payments can help reestablish accounts as the key platform for financial transactions, and allow banks to enhance the customer interface and avoid being relegated to the position of a pure infrastructure provider. Ultimately, instant payments will allow them to recapture lost market share and reputation.

Sooner or later, all banks will have to implement SCT Inst in response to customer demands. Instant payment will become the new standard. By choosing to be "first mover" rather than "follower", banks can give themselves a competitive advantage over fintechs and other competitors. There are three main factors at play here, presented below.

First, banks have a large customer base that still relies on traditional payment methods. The proportion of customers who rely on traditional payment methods varies from country to country. In Germany, for instance, despite a downward tendency, the proportion is relatively high: In 2017, 20 percent of customers used direct debit, and another 30 percent used a bank transfer after receipt of an invoice, as their preferred method of paying for e-commerce purchases. This compared to less than 20 percent who chose PayPal. In the United Kingdom, by contrast, credit transfers are less common, largely because PayPal entered the market earlier and because debit and credit cards are much more common.

Customers who still rely on their bank account for payments, independent of POS-, e-commerce or consumer-to-consumer payments, are an asset for banks.

The second advantage that banks hold over non-bank competitors is their wide product range across all customer groups. They can potentially combine instant payments with other financial products and services to create comprehensive digital solutions. Some examples are given in the following section. A combinatory approach of this type will
likely be more successful than trying to shape a sustainable business case based solely on SCT Inst, such as charging end customers for instant payments. We consider such an idea unsustainable in the long term. Combining instant payments with existing products (e.g. instant credit) allows banks to fully leverage their wide product portfolio and knowhow. Banks have great scope for developing products that cannot easily be imitated by emerging competitors and financial intermediaries, which often focus on a single product. For example, fintechs with the ambition to offer instant payments to their customers will need to identify a profitable use case for a standalone payment solution.

The third factor driving opportunity for banks is their wealth of experience in the areas of security, regulation and operations. Recent regulatory changes in payments, like the PSD2, aim to improve transparency in the payments segment, as well as protect consumers. However, they also establish stronger regulations for PSPs (Payment Service Providers), which not all competitors – and especially not all fintechs – are prepared for. For example, our study “FinTechs in Europe – Challenger and Partner” found that 73 percent of fintechs underestimate the importance of regulatory competence. Banks, on the other hand, have highly developed skills in dealing with complex and constantly changing regulations and compliance demands.

Security and trustworthiness is another increasingly prominent issue. Data security and security of payment methods are primary demands of today’s customers, particularly in light of recent data breaches and privacy concerns. Ironically, banks benefit from the fact that they have not used customer data extensively in the past. Customers still rank them highly with respect to data security compared to companies such as GAFA (Google, Apple, Facebook, Amazon).

These three assets put banks in a strong starting position. But to fully leverage the excellent opportunities Instant Payments offer, they need a springboard. Using SCT Inst to develop innovative products and services provides this.

Now is the time to move. The new PSD2 rules will be mandatory from September 2019, meaning consumers can authorize third-party providers to interact directly with their bank accounts. This puts traditional banks under pressure to reposition themselves. Key to this will be banks’ ability to differentiate their own products and services from those of their competitors. When banks switch over to instant payments, as we believe they will have to, they will need to transfer their IT payment infrastructure from “batch processes” to real time (at least for instant payment, clearing & settlement).

But by only technically updating their IT structure, banks risk ending up as pure infrastructure provid-
"Use cases" for instant payments are a way of pinning down the advantages and disadvantages of specific solutions for consumers, companies and banks. They help evaluate the viability of a solution from a strategic point of view. Banks employ tailor-made use cases to identify the specific needs of customers or merchants and then develop viable payment solutions. Instant payments have a variety of potential use cases for private consumers and businesses. Most of these revolve around reducing costs and enhancing customer experience. For banks and payment providers, the use cases likewise involve cost reductions – but also valuable opportunities for boosting existing revenue streams and generating new ones.

From simpler payments to new credit products.

Potential use cases for instant payments.
USE CASE NO. 1
Instant payment for retail clients – Buying a new car (and selling the old one)

Don and Deanna, a married couple in their forties, have decided to buy a new car. First, they need to get rid of their current car, which they decide to sell online to generate some extra cash. The couple find a potential buyer, but they are uncomfortable about how and when the money should be transferred. If the buyer makes a bank transfer, it will take a few days to go through – should that be before or after he picks up the car? If he pays by check, the check might bounce. Cash would be straightforward, but it’s a large amount to carry around. Don and Deanna don’t want to be swindled, but on the other hand they don’t want to deal with a large amount of cash. Instant payment offers a solution. The buyer can send a peer-to-peer payment on-the-spot using a banking app on a smartphone. Don and Deanna receive the money in their bank account instantly, even though they have a different provider. The advantages for both parties are evident.

In the meantime, Don and Deanna have been looking for a new car. They find one at a large car dealer, order it and go to pay at the cash desk. Here, SCT Inst again offers advantages in terms of customer convenience. Don and Deanna can make an instant payment at the POS without using a payment card (which would need a significant limit). The transaction is less expensive as the risk of fraud is reduced, and no payment guarantee or credit card infrastructure is necessary.

The cost savings at the POS are beneficial for all parties involved. Moreover, the transaction is simpler and safer. Instant payment thus addresses the main demands of customers and retailers: a fast, secure, convenient and low-cost method of payment. But wait. Just as Don and Deanna are about to pay, Don changes his mind. The store has a special offer on convertibles and Don thinks they should splash out. The problem is, the convertible pushes them over budget and they would need a small loan to make the purchase. In the past, customers used financing solutions offered by banks via stores or dealers. This meant banks paid large sums for commercial agreements with retailers. Now, however, Don and Deanna can request an installment loan from every online consumer specialist and have the money transferred to their bank account instantly. The couple is happy with the flexibility: It allows them to pay the dealer in full at the POS, take their new convertible home and pay back in installments. They benefit from increased convenience and lower costs (as the dealer can offer an additional discount), and their bank benefits from new business and greater loyalty. And there’s more. Don and Deanna want to drive their new car home straightaway but don’t yet have insurance. While still at the POS, they arrange a policy from their preferred insurer and pay via a real-time payment to secure immediate coverage. This is not the first time they have bought last-minute insurance: Before going on vacation last year they bought travel insurance online just minutes before boarding the airplane.

USE CASE NO. 2
Instant payment for businesses – Cash management and reconciliation

Don and Deanna’s car dealer is also pleased that his bank offers instant payments. Instead of waiting for the money to be transferred to his bank account or paying fees on card transactions, the money is directly credited. Also, as the car dealer is part of a larger network and, like many businesses, has numerous bank accounts and makes hundreds of financial transactions each day, transferring money between accounts in seconds allows him to optimize his cash and liquidity management. There are further benefits for his supply chain: while nowadays a significant part of B2B payments are invoice-based and settled via bank accounts, companies spend a large amount of money and manpower reconciling orders, invoices and payments. Instant payments could help to solve this by instantly crediting money to an account the moment the order is submitted. Thus, instant payments will help to streamline processes and reduce highly manual administrative tasks.
## Buying and selling a car – instantly

Instant payments have several advantages for buyers, sellers and third parties such as banks.

### Selling
- Cash Payment
  - Must handle and pay in cash
  - Must withdraw and handle cash

### Buying
- Credit Card
  - Card fees and infrastructure
  - Transaction limit

### Loan
- Consumer Credit
  - Time between approval and payout of 1-2 days
  - Limited choice; complicated application

### Insurance
- Basic Car Insurance
  - Processing application
  - Limited choice; no immediate coverage

### Options
- Let’s buy a new car!
- Let’s get some cash by selling our old one!
- Let’s get a loan for something nicer!
- Let’s drive home safely!

### Traditional Bank Account
- Instant Payment
  - Secure transaction
  - No theft risk
  - Lower fees and fraud risk; optimized cashflow

### Modern Bank Account
- Instant P2P
  - Instant Payment
  - Instant Mobile Credit
  - Secure Immediate Coverage
  - Automated decision
  - Unlimited choice; immediate coverage
  - Unlimited choice; instant decision
  - Immediate payment, new business; improved loyalty

---

*Icons: Good Ware, monkik, mynamepong/Freepic*
The road ahead.

SCT Inst is not mandatory for banks: They can decide whether they wish to use the new payment scheme. Most banks have already introduced instant payments, even if only partially, for example receiving instant payments but not sending them. Others charge a fee to send instant payments.

How does this stand up as a strategy? Not very well, we believe. Introducing parts of SCT Inst but not the whole scheme is a risky approach. Customers will not be satisfied if their transaction partners can send them money instantly, but they cannot do the same. And charging transaction fees without offering anything more than what competitors provide for free is not a sustainable strategy.

If banks want to avoid becoming pure infrastructure providers and surrendering the customer interface to other players, they need a comprehensive strategy based around instant payments. Leaving the innovation to others will squander a valuable opportunity. Therefore, we recommend banks consider the following three actions:

1. Implement instant payments in the payment infrastructure — Do what you need to do!

Instant payments will become standard for payments in Europe. Thus, customers will expect banks to offer the service. If banks are front-runners in implementing instant payments, they might even have the chance to price the new service for a short period (as we currently observe in the market). However, in the medium- to long-run they will have to provide it for free. As such, banks should consider their clients’ expectations, their overall payment strategy as well as the backlog and prioritization of similar projects when addressing implementation. For example, clients might push a bank with a strong business and corporate client segment to implement instant payments as soon as possible. Below is a short checklist for management to consider:

First mover/Innovation leader:
What do our clients expect from us?

Value add:
Which use cases do we have, besides faster credit transfers?

Management attention/focus:
How is our overall project portfolio for IT initiatives?

Budget:
How much would we need to invest to update our IT infrastructure and processes?

Actions for the management agenda.
2. Develop new products and services by applying instant payment technology – Innovate using your existing assets!

Instead of implementing instant payment for simple account-to-account payments (as a substitute for traditional SEPA credit transfers), banks should leverage their wide product portfolio and combine instant payments with other products and services. For example, by using instant payments to offer on-the-spot consumer credit at the POS.

It is critical to take the user (for example, consumer or business) perspective when developing these new services and products. Do not put technology at the center of your thinking. The last thing consumers need is another payment solution. The new solution must be superior in convenience or add value for the client.

Applying product innovation techniques, such as design thinking, is one approach banks could use to identify client-oriented use cases (see graphic below):

After identifying real customer needs, an ideation phase of potential solutions (based on instant payment technology) is set up. Then, prioritization, prototyping and validation are done with potential clients before building the solutions. Don’t forget to involve all your client segments: There are many use cases for retail as well as business/corporate clients.

After successfully testing the ideas, the value creation and financial potential of the use cases should be evaluated before finalizing the rollout of the new product solution.

Keep in mind that banks have a strategic advantage over fintechs and other competitors. They can combine the instant payment technology with existing products from their current portfolio.

3. Revise the overall payment strategy – Reposition the bank account and win back your client!

Instant payments will very likely become standard for account-to-account payments and enable new products and services. The real opportunity for banks is to re-establish the bank account as the central payment method, and to establish the banking app as the main client interface for all their clients’ financial needs.

Thus, banks should take the opportunity to revise their payment strategies. This should involve outlining a clear path forward on where and how to play in the payment game. Several non-banking players (e.g. Facebook, Amazon, PayPal, Google Pay, Apple Pay) have entered this space, taking a significant part of banks’ margins while being more successful in occupying the client interface and collecting valuable client data. By supplying a new customer experience and extended functionalities, banks could win back the client. Deferred payments (as offered by credit cards) or payment by invoice (as with Klarna) could easily be replicated by the bank account (from a technical perspective). In addition, card-based payments at the points of sale could be replaced by instant account-to-account payments.

On this basis, banks should view the instant payment discussion not only as a technical update of their payment infrastructure, but also as a new chance to move into the fast lane.
Contact details

Sebastian Maus
Partner
sebastian.maus@rolandberger.com
+49 211 4389 2259

Edoardo Demarchi
Partner
edoardo.demarchi@rolandberger.com
+39 335 769 6954

Simon Keiser
Project Manager
simon.keiser@rolandberger.com
+49 211 4389 2993

Alessandro Grigolon
Project Manager
alessandro.grigolon@rolandberger.com
+39 331 687 7738

Publisher

ROLAND BERGER GMBH
Sederanger 1
80538 Munich
Germany
+49 89 9230-0
www.rolandberger.com

Roland Berger, founded in 1967, is the only leading global consultancy of German heritage and European origin. With 2,400 employees working from 35 countries, we have successful operations in all major international markets. Our 52 offices are located in the key global business hubs. The consultancy is an independent partnership owned exclusively by 230 Partners.

This publication has been prepared for general guidance only. The reader should not act according to any information provided in this publication without receiving specific professional advice. Roland Berger GmbH shall not be liable for any damages resulting from any use of the information contained in the publication. © 2019 ROLAND BERGER GMBH. ALL RIGHTS RESERVED.