VocaLink setting the pace in European payments market

One of the most ambitious payment services ever conceived, the UK's Faster Payments has exceeded its creator's initial expectations.

Following on from the success, an executive with service developer and operator VocaLink discussed implications of real-time payments with *EPI* and the company's bold expansion plans

Back in 2005, 13 major UK financial institutions set out requirements for a payments processing service that could guarantee that payments made via internet, phone and standing orders would be approved within a matter of seconds and be in a recipient's account within two hours.

Meeting these objectives on the scale demanded by the UK's retail payments market was arguably the most daunting challenge in the UK payments industry since the introduction of electronic payments.

It was a challenge entrusted to UK payments processor VocaLink, a company that had already built a reputation as the operator of the world's busiest ATM switching platform. The result was the UK's Faster Payments Service (FPS) running on VocaLink's Real-Time Payments Platform.

Launched on 27 May 2008 FPS was initially limited to internet and phone payments. Standing order payments became available on 6 June.

FPS has proved a roaring success, ending 2008 with transaction volumes running at five to six times levels envisaged at that stage, Paul Taylor, managing director for Europe at VocaLink, told *EPI*.

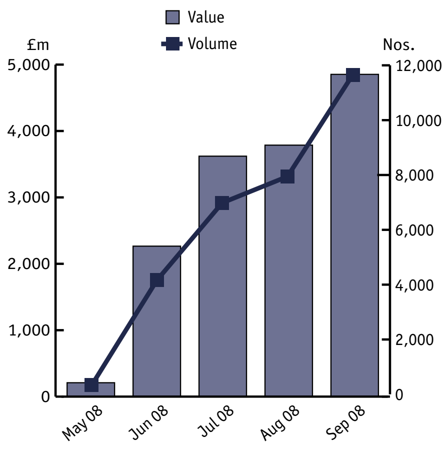
"The public has been very receptive of Faster Payments," Taylor said.

FPS has been the subject of a gradual phasing in process by the financial services providers involved, with an initial maximum limit of £10,000 ($15,500) on phone and internet payments and £100,000 on standing order payments.

Indicative of the potential scale of FPS, the UK industry body APACS reported that in 2007 124.5 million internet and phone payments valued at an average of £303 each and 347.3 million standing order payments valued at an average of £321 each were made in the UK. The number of internet and phone payments is forecast by APACS to rise to 300 million by 2017 and the number of standing orders to 422.3 million.

UK PAYMENTS MARKET

Faster Payments service



Source: APACS

Based on the most recent figures available from APACS, FPS processed a total of 11.66 million transactions in September 2008 – 6.28 million originated via phone or online and 5.38 million were standing payments.

Transaction volume in September was up 47 percent compared with August while total transaction value increased by 28 percent to £4.85 billion of which standing orders represented £442 million.

Future of the ACH

While real-time retail payments represent a major step forward in terms of customer service compared with the UK's previous three day settlement period, Taylor does not see faster payments forcing automated clearing houses (ACH) into redundancy.

"There will always be a need for a low-cost bulk payments service," said Taylor. "Not every payment needs to be settled instantaneously."

However, real-time payments cannot be ignored.

"In the future I believe all ACHs will be required to provide faster services," predicted Taylor.

Indeed, the UK's Faster Payments Service is already attracting what Taylor termed "remarkable interest" from other European countries.

The changing marketplace also presents Europe's 31 ACH's with new challenges. All ACH schemes were once exclusive to their particular country, now their activities are cross border, explained Taylor. In a seaming prelude to consolidation, he noted that ACH's are owned increasingly by the same banks.

Inevitably banks will be attracted by the lower cost economies of scale achievable by large ACHs.

"The cheapest ACH will get the business," noted Taylor.

He added that five countries account for 80 percent of payments in Europe.

Beyond consolidation, ACH's have another choice: outsourcing. This was the route chosen by Bankgirocentralen (BGC), Sweden's ACH, when in October 2007 it announced that it had selected VocaLink to assume responsibility for processing.

BGC took a rational decision to retain ownership of the ACH and identify a partner that could offer guaranteed lower transaction costs and development of new services, such as those for the Single Euro Payments Area (SEPA), commented Taylor.

This view was reflected in a statement made by BGC's previous CEO Eva Gidlöf when the partnership was announced.

"VocaLink is the leading European payment processor, with products that are modern, currency independent and ready for the European market with very competitive pricing," Gidlöf said.

Owned by eight Scandinavian banks BGC reported 620 million retail transactions valued at a total of SEK6.69 trillion ($880 billion) in 2007. Transition of BGC's processing to VocaLink began in May 2008 with completion anticipated in the beginning of 2010.

Just the beginning

Emphasising the significance of the BGC deal, Taylor said: "I believe it is the starting flag for ACH consolidation in Europe."

From VocaLink's perspective this would be a significantly positive development.

Taylor explained that VocaLink offers complete end-to-end processing incorporating ancillary services such as reformatting, authorisation, direct debit management and reject handling. For many ACHs it would be uneconomic to duplicate this fully comprehensive offering.

In the UK alone VocaLink's centralisation of services saves banks a total of £200 million each year, noted Taylor.

ACH consolidation is not the only bright prospect for VocaLink. SEPA also offers considerable scope for developing outsourced services, said Taylor who added that VocaLink has already contracted with a number of major non-UK banks to provide them with SEPA direct debit services.

"Having seen low consumer demand for SEPA direct credits they were not prepared to build an in-house SEPA direct debit solution that can cost tens of millions of pounds," said Taylor.

There is also no guarantee when it will become legally binding for all euro payments to migrate to SEPA, he added.

Introduced in January 2008 SEPA direct credits have garnered a market share of less than 2 percent. SEPA direct debits are due to be launched in November 2009.

However, despite SEPA's slow progress it has been a "huge catalyst" for new product development, stressed Taylor.

"We have built services around the SEPA core-capability that make it attractive," he noted.

Of particular significance is a solution offered to multinational companies who until now have been required to operate liquidity accounts with banks in each European country in which they operate.

This has had two serious consequences explained Taylor. Firstly, despite undertaking vast transaction volumes multinationals have not been fully rewarded by way of lower transaction costs. Secondly, having separate liquidity accounts has meant that multinationals know their overall liquidity position with, at best, 70 percent accuracy.

Taylor continued that a bank using VocaLink's solution can submit a multinational's payments via a single channel. This provides the multinational with benefits of lower transaction costs and enables it to have a completely accurate picture of its liquidity position in real-time.

VocaLink's solution which comes with the added benefit of a multi-currency capability also has wider applications. Because it offers the benefits of bulk pricing it can enable a local bank to compete on an equal cost-footing with multinational banks, said Taylor. It can also provide a multinational bank with the ability to compete on an equal cost-footing with a dominant bank or banks in another country.

On the overall thorny issue of SEPA, which has been the subject of much hand-wringing by European Bank officials and others, Taylor stressed that a migration end-date is vital. However, he added that an end date should be based on a consensus.

"The market must move holistically," he stressed. ■