Nonbanks in the Payments System: Innovation, Competition, and Risk

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Session 4: Competition: Horizontal Integration
Panelist Remarks
Moderator: Ken Howes, Director, Edgar, Dunn & Company
Panelist: B.J. Haasdijk, Chairman, Equens

Mr. Haasdijk: [remarks correspond with handout]

Thank you, Ken. Thank you for having me here this afternoon. It was about two years ago that I was standing here as well. I was invited because at that time we were Interpay, bank-owned and operating in the Netherlands. We were facing an anticompetition issue that since has totally disappeared. The fact that I am mentioning it is because, since then, a large number of changes have occurred, SEPA being one of them. For us, that meant and means that our market – which was a domestic market – now is a European market. That has given rise to a large number of changes.

We all know why SEPA is in the making. We all know what is to be achieved. But I would like to share with you the views from a processor who all of a sudden found itself deprived of the natural protection of the own currency barrier because, after having gone through a giro Euro project in 1999, having done away with a "small" millennium project, we then faced the introduction of the Euro at the end of 2001, and by that time, everybody in our company took a deep breath and started looking around. The world had changed immensely.

We were aware of the fact, of course, that harmonization and standardization were in the works for us because we found the payment processing that we were used to was going to be done at a different and larger scale. Before I continue, I am talking also – or initially primarily – about what we call "giro," that is, clearing and settlement doing interbank transactions. Subsequently, we may spend some time on our debit card operation.

We were facing a situation, as I said, with changes in the making. And we said to ourselves, "If governance stays as it is, if we don't move at the end of the day, somebody will switch off the lights. We don't know who. We don't know when it will happen, but that it will happen is certain."

So we went back to our shareholders and said, "There is value in our company, in Interpay, and we want to be able to maintain that value or, even better, increase it." In the market that was developing, we said that scale is of primary importance. It is a very scale-sensitive business. Therefore, we felt, and we tried to convey, an urgent need to increase that scale.

As we were in our country the only provider of that sort of activities, the expansion possibilities in the Netherlands seemed to be fairly limited. That necessitated looking abroad into other areas and into other countries.

The reason behind all this is that we had and still have a clear view that, at the end of the day, when SEPA has become a reality – and we may touch upon when that will be – out of the 22, 23, 24 processors of giro transactions in Euroland today, we think that three to five will be the survivors. Why that number? Because it is sort of an optimum between competition, between suppliers on the one hand and the complexity of ensuring reachability throughout Europe as whole on the other hand. I will be coming back to that in a moment.

So, there we were. And we started looking around. We had a short fling across the Channel, but then we ended up – or started discussions with our German friends of Transaktionsinstitut.

Now, there we were, equal in size but not equal in market size. We, as I said, cover the whole of the Netherlands. But admittedly, it is a small country, so with well over 3 billion transactions, we were equal in size to Transaktionsinstitut, which has about 16 percent market share in Germany.

When we talk about horizontal integration in this sort of business and we talk about scale as being the driver, it is obvious you are talking in our business about doing the processing on one platform. You have to bear in mind, as Ken already mentioned, that in Europe, everybody had developed its own systems and its own platforms, so by virtue of bringing two companies together, one platform would have to be or will have to be sacrificed and done away with. And I can tell you that has been a very difficult but necessary decision.

When we announced the intention to merge in January of last year, we were talking about a company that had a potential of well over 7 billion transactions. And, by the way, if you realize or think about three to five survivors, then 10 billion transactions seem to be a level that should be attainable to have a sustainable future. So, we both made a giant step.

We were the first, and we really worked very hard to be the first, to announce that merger, not because we were saying, “Hooray, we are the first,” but because of being able to enjoy the benefits of what is generally known as a first mover advantage.

Some historical figures or data: We signed the agreements – rather, I should say, our shareholders signed the merger agreements in September of last year, and, as of the very next day, we started the integration project. The merger itself was closed on November 30 of last year.

Why did we start the integration? Well, obviously, large economies of scale can only be arrived at by integrating two companies, by doing away – as I said – with one platform, and by reaping the synergies that merger brings about.

Although we are not a big company in total size, we are about 1,200 FTEs. We have a program in place that will bring that down to somewhere close to 800 in the next couple of years, thereby at the same time increasing the volumes, not only by bringing the existing volumes together, but also by attracting new customers.

There is a paradox in this. When we looked at our future service portfolio, it was obvious that the products as they were derived through the European Payments Council, through what is known generally as the Rule Book, we knew of course the basic requirement is that we must be able to process those SEPA products. But, if you look at the geographical history in terms of payments and you look at the different countries, then all these countries are coming from a different, let me say, level of sophistication in their payments instruments, the payments services they have.

What we said is, “Okay, we have to have the basic platform in place to process all these SEPA products, but we also have to bear in mind that the gap—as we call it—between what people in the various countries and the various geographies are used to and what SEPA brings them may have to be closed. We want to be able to be in a situation to offer those additional services to banks as well.”

So, on top of everything that is standardization, the SEPA Rule Book products, we offer also and have a modular product available that allows us to give these additional services to our customers of today and tomorrow.

I would like to conclude with one thing that is equally important, apart from what I just said. That is reachability. I touched upon it when I mentioned the number of processors that we expect will survive in the long run. That is the reachability so that we can ensure our customers are guaranteed that whenever one of their customers sends in a payment and it has to go to some place or area at the other end of the Euro area, we must ensure, through cooperation with the other payment processors, that reachability is indeed achieved. For that reason, EACHA, the name has been mentioned already today, was founded to ensure that reachability will indeed be available. If we do not have that, then we miss out on a very important issue.

I could go on for a long time. We have been working at it very hard. It has been a very enthusiastic team that has been working on it, and I am very proud we have this merger in place. Indeed, through being the first mover, we are already in a position to be reaping those benefits that we aimed for by attracting new customers outside of the Netherlands, outside of Germany, so the effect is really there and it is really working.

Thank you very much.

Mr. Howes:

Just one quick question. Obviously, you are here as SEPA in action. Do you see SEPA coming about in the timeframes that have been scheduled for it? Or do you believe that in fact there may need to be some other measures taken at some stage to force SEPA?

Mr. Haasdijk:

We have said, and we will be SEPA-ready by the first of January 2008, so in 10 months or in just over six months' time. Then it starts. If you look at the various participants in the payment arena – now I am not talking about the providers of services, but the users of services – when you do get around to small and medium and also bigger corporations, you find that, for them, SEPA is something that they have heard about, that they know is coming about. What it brings to them is not always very clear. Admittedly, the big corporates that have cross-border activities and have their own cash management systems, they are – as was already elaborated today – trying to drive SEPA coming about.

But the other participants are somewhat reluctant, if I may say so. I think there has to be a momentum to be brought about in order to get things moving and really accelerating. You could argue it could be national governments that start using SEPA products as soon as they become available; that will help get the ball rolling. I would not put it beyond the possibilities that, if SEPA does not become a distinct reality in the next couple years, then we will see some regulatory intervention, if only also for the fact that keeping alive two different sets of processing systems next to each other is not very beneficial, to put it mildly.

Mr. Howes:

Thanks, Ben. Gerard, if you would like to begin.