PSD2: DRIVING DIGITAL TRANSFORMATION IN BANKING

A joint Microsoft and Efma survey
The Second Payment Services Directive (PSD2) is one of the largest regulatory challenges that banks have faced in recent years. Compliance with the new legislation means that financial institutions, at the very least, need to make some significant changes to their processes. However, the new Directive also presents a range of exciting opportunities for those banks that are sufficiently forward-thinking and agile to take advantage of them.

Microsoft therefore approached Efma about conducting a joint study of the current situation in the financial services industry. The aim of this study was to identify the key issues facing banks; to understand the opportunities that PSD2 presents; and to explore how prepared banks are for PSD2 compliance.

This white paper presents details from three online discussions of a Think Tank involving senior banking executives. It also includes the results of a survey of selected Efma members, designed to pinpoint the current fears, hopes, expectations and preparedness of banks in relation to the new Directive.

We hope you enjoy reading the report, which highlights the need for banks to be prepared not only to comply with PSD2 but, wherever possible, to take advantage of the new possibilities that are opening up as a result.
Introduction

This study of the implications of PSD2 is a joint project between Microsoft and Efma, and involved three online sessions hosted by Richard Peers, who leads Microsoft’s worldwide industry team for retail/private and wealth banking. Richard is also the leader of Microsoft’s PSD2 and Open Banking initiative and works with regulators, clients and partners to learn, share and facilitate the move to this new paradigm.

Banks have been informed they will need to comply with the PSD2 regulations by January 2018. The new directive requires European banks to grant third party providers access to a customer’s accounts to initiate payment services or to provide account information in a regulated and secure way. This will enable seamless and safe payments across EU borders.

Along with Open Banking regulations, PSD2 aims to promote competition (as customers will have more choices); encourage innovation; and increase consumer protection whilst providing more choices for services.

However, there are still some complexities that need to be sorted out, particularly around the issue of the Regulatory Technical Standard (RTS), which defines how access to accounts will be implemented. This is still under debate and won’t come into force until November 2018 at the earliest.

Microsoft, in conjunction with Efma, therefore set up a series of online discussions with industry thought leaders to explore how banks are reacting to the need to comply with PSD2, its potential impact, and the challenges and opportunities it presents to financial institutions. A questionnaire was also sent out to Efma members.

This report seeks to draw together the presentations by Microsoft; the results of the survey; and the online discussions of the Steering Committee.
Based on preferences provided by Microsoft, Efma established an advisory Steering Committee of ten senior executives from the financial services sector, representing eight European financial institutions. They are all industry experts who have their own insights into PSD2. They also have specific interests in topics such as digital transformation, new business models and payments.

The key expectations of the Steering Committee members included:

- **Delving beyond the superficial** and exploring aspects such as expected customer behaviour; the likely effect of PSD2 on the market in three to five years’ time; and open banking.

- **Sharing a vision of the future** and understanding the hopes and fears of other banks and of the overall market. This includes exchanging ideas with people in other countries, especially in relation to the strategic side of PSD2 and the role that banks can play.

- **Discussing the opportunities** that PSD2 could create for banks, rather than just the risks and threats. PSD2 could act as a potential revolution in the banking sector – will it bring a transformation to digital channels? At the very least, it seems likely to provide opportunities for change. Some of the key opportunities include the potential monetisation of data, APIs and insight.

- **Understanding the possible consumer reaction** to PSD2. Some of the strategic responses to opportunities for both established players in the financial services sector and new entrants are becoming clearer. There are a lot of theoretical discussions taking place and numerous models, whether from consultants or think tanks or conferences. However, an exploration of how customers will engage with these new propositions seems to be lacking at present.

- **Complying with the new regulation** and benchmarking any progress so far with other members of the Steering Committee.

- **Examining the role of fintechs** within the legal environment of PSD2 and the potential threats and opportunities they present.
Various market authorities want to introduce greater consumer choice, better consumer protection and more competition in the marketplace. The result is PSD2, which has an explicit timeline and set of requirements. It has a key role to play in digital transformation, along with open banking and regulatory-driven application programming interfaces (APIs), which will evolve into a broader API economy. This also provides an opportunity for the transformation of banking products and services.

Digital transformation can be seen in terms of four stages: engaging customers; empowering employees; optimising operations; and transforming products. It involves thinking about aspects such as opportunities, choices and customer engagement. Engagement is important in the context of PSD2: even making aggregation platforms for customers is really about making things easier and more convenient for them. The question is whether banks will take up the challenge or whether they will leave it to others to occupy this space – including fintechs and new entrants.

The other key issue with engagement revolves around the ability of the bank to gain the customer’s permission to access their data. This isn’t always easy. However, banks can offer incentives by creating interesting added-value services derived from this customer information.

In terms of how banks respond to PSD2, there are four main scenarios. One of the questions that the joint Microsoft and Efma survey attempts to answer is where banks are on this spectrum and how ready they are to deliver any of these capabilities. All banks know that they will need to be involved in the first of these stages – basic compliance. Those banks that stop at this stage and refuse to go any further risk losing potential revenues as payment services opportunities for disintermediation appear.
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