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Neelie Kroes

European Commissioner for Competition Policy

Getting more from financial services markets: greater competition for a better deal for consumers

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I am delighted to be here today to explain how the European Commission is working to strengthen competition in Europe's financial services markets.

I have spent enough of my life in academia to know how prestigious it is to study here at the LSE. As I look around this room and see the faces of the new generation of business leaders and opinion formers, I have a bit of advice for you all.

There are probably two types of services which you can't avoid in life. One is the undertaker. The other, banks. And whilst you can't insure yourself against death itself, you might want to take out insurance to pay for your funeral!

Joking aside, financial services are vital to the functioning of our economy and they matter directly to each and every one of us as consumers.

They enable us to engage in the most basic economic activities - buying and selling - with not just the people in our village or town, but with people anywhere in the world.

What's more, when financial services markets are integrated and competitive they enable the most efficient allocation of economic resources. That means better economic performance, better prices and better services for consumers and businesses.

This year marks the fiftieth anniversary of the Treaty of Rome, and the twentieth anniversary of the Single European Act. We've come a long way in that time. But the world – our world – is changing. Globalisation is a reality. Some people use this as a reason to look inwards, to protect what we have and close the door to the outside world.

Fear is of course a natural human reaction. But that does not make it right to give in to that fear. Now is not the time for looking inwards. Now is the time to look outwards, to seize the opportunities and benefits that global markets can offer. And what better illustration of this is there than the UK - there are more foreign banks operating here than any other country, and the UK has the largest trade surplus in financial services of any country in the world.

European competition policy has a crucial role to play in creating and maintaining integrated, open and competitive markets in Europe. The European Commission, together with national competition authorities, is working to ensure a level playing field for all providers, small and large, by enforcing EU competition rules. We believe – and the economic evidence proves – that the most successful companies are the ones who face fair but tough competition, which drives them to innovate, invest, grow and win.

But there are some core sectors of our European economy where competition does not appear to be working as well as it should. Financial services is one of them. In 2005 I launched a major sector inquiry into the retail banking and business insurance sectors, working closely with Commissioner Charlie McCreevy. We recently published our final report as concerns retail banking, including payment cards, and interim findings about the business insurance sector. Today I will outline the key findings of these inquiries and the conclusions I draw from them.

Banking sector

I'll take the three parts of the financial services sector inquiry in turn: the retail banking sector, payment cards and business insurance.

Core retail banking

The state of competition in Europe's retail banking markets is, quite frankly, a cause of real concern. Retail banking markets largely remain national in scope: it is proving difficult for foreign banks to really challenge the big domestic players in many European markets.

Much of this can be explained by obvious differences between countries – such as different languages, laws and tax systems. But there are also barriers preventing banks from accessing important facilities that they need if they are to compete in new markets. The most prominent examples of this are payment systems and credit registers. Payment systems in some markets still have unfair access rules or high joining fees that deter new members. If you can't make or process payments, your prospects as an operator in the financial sector are probably limited – to put it mildly!

In many Member States banks can't get hold of credit information on new borrowers. Sometimes this reflects legitimate privacy concerns, but in other cases it seems that these systems were set up to favour the incumbents. Would you lend money to someone without any idea of their creditworthiness? Of course not! Again, it's bad news for potential new entrants.

The European Commission is already acting to remove these problems. The Payment Services Directive should tackle a number of national barriers in the payment systems market. The proposed provisions of the Consumer Credit Directive should ensure that all banks can enjoy open and fair access to vital credit data. Creating a level playing field for banks should encourage more players into the market in the coming years. But my colleagues in national competition authorities and I will not hesitate to act to enforce the EC competition rules if unjustified barriers to new entrants remain.

A second area for concern is the terms and conditions imposed by some banks on their customers. Our investigation points to several types of what I might – generously - call 'bad practice'. These include high fees for closing an account. Too often consumers are forced to buy extra products such as insurance or current accounts, when all they really want is a mortgage. These practices are intended to encourage customers to stay with their current bank, even if they could find a better, cheaper service with a competitor.

If you want to buy a loaf of bread, you go to the supermarket and choose one. You may look at the label because you want a certain level of fibre. You may check the thickness of the slices to see that they will fit in your toaster. If one supermarket does not have what you are looking for, then you'll go along the road to another one. And you'll certainly never be forced to buy your butter and jam at the same time!

In markets where each consumer is able to act upon a well-informed choice in this way, companies - in this case bakers and shops - are able to respond to consumers' signals about what they want and are willing to pay, keeping the market competitive and consumers happy. We think changing bank accounts should be as easy as deciding to buy a different type of bread or going to a different supermarket. But for most European consumers this isn't the case. As a result, competition is subdued, prices are high and product offerings don't always match what customers actually want.

But it's not all doom and gloom. Our report also points to some good practice. Banks in several countries, including here in the UK, have put in place codes of conduct which make it easier for customers to move from one bank to another. Several Member States are encouraging industry to provide clear and simple product and price information. I am convinced that these types of initiative will help inject more competition into high street banking throughout Europe, to everyone's benefit.

Payment cards

Let me now turn to our findings on payment cards. The annual volume of retail sales paid for by cards is around €1.350 billion per year. But what most people don't realise is that every year European consumers are paying fees worth €25 billion to banks for providing payment card services. That's quite a bill we all share!

From a competition perspective, the sector inquiry identified several problems in the market for payment cards. They stem from the way the industry sets card fees and rules intended to keep new entrants out of this lucrative market.

First, there is a huge variation in payment card fees across the Member States. Retailers in some countries pay fees that are up to four times higher than in other countries for accepting the same major credit card. In the course of our inquiry, we did not hear a convincing explanation of why cost structures differ so greatly across the EU. I have an answer: high fees may well be the result of lack of competition in the market. 95% of cross-border card payments in Europe are made by just two companies. In some Member States there is only one company servicing retailers. How can there be competition in a market where retailers cannot choose their supplier?

Secondly, there is the question of the interchange fees charged by some payment card schemes. Interchange fees are charges a retailer's bank pays to a card-holder's bank. The banks and the payment card networks claim that without these fees, issuing banks will not make enough money and will be forced to charge consumers more. Our inquiry has gathered the best empirical evidence yet available. But it does not lead us to the same conclusion. As a matter of fact, several payment card networks in Europe currently operate very well with low fees. And in some cases issuing banks remain profitable even without interchange fees.

The costs of high interchange fees are of course being passed onto all customers through higher retail prices. Prices you pay whether you use cash, by cheque, debit or credit card. More transparency would enable customers and retailers to see the real cost of using their cards, and then make an informed decision on how to pay. Why should customers paying with debit cards or cash subsidise customers who pay with expensive credit cards?

I'm interested to see that others are thinking along these sorts of lines. IKEA in the UK applies a surcharge for payment by credit cards, to reflect the higher costs they incur for such a payment. How have customers responded? Unsurprisingly, many customers are now choosing to pay with debit cards, which are less expensive. This is an example of giving correct price signals to consumers, thus promoting the use of less expensive payment instruments. This is what I call transparency.

Let me be clear. I am not saying that interchange fees are always illegal. But I am saying that the way these fees are currently set raises costs for Europe's businesses and consumers. The European Commission has an open case against MasterCard addressing precisely this issue. At this stage I cannot elaborate further on this specific case. But I will say that when our exemption decision on Visa expires at the end of this year, we will look again at the effect of their interchange fees on competition.

Fortunately, I can also conclude this topic on a positive note. Some players in the market have already started to modify some of the anti-competitive rules which the sector inquiry identified. Going forward, our investigation into existing payment systems provides guidance on how a more competitive payments market in Europe should look. And of course the creation of the Single European Payments Area, SEPA, offers a great opportunity to enhance competition. But it should not be used as a pretext by the banking industry to raise prices or lower service quality compared to existing national payment products. We are working with industry and national competition authorities to help resolve potential competition concerns upstream. But I reserve the right to come back using competition tools if there are any nasty surprises later on.

Business insurance inquiry

The third and final part of the financial services sector inquiry is focused on business insurance. We published our preliminary findings last month, as the basis for public consultation. We are also further investigating some of the potential competition problems we have identified, including fixed long duration contracts, horizontal cooperation between insurers and a lack of transparency in brokers' commissions.

An area of particular concern is that insurance companies tend to display consistently higher underwriting profitability in the services they offer to SMEs, compared to the services they offer to large corporate clients. This suggests that there may be more transparency and competition in the market for larger clients, making it easier for these larger companies to change insurance provider where this might save them money. This is worrying because SMEs make up 99% of all EU companies - it is important for our economic competitiveness that they can enjoy equally competitive insurance products.

Conclusion

Ladies and gentlemen, this evening I have spoken about why ensuring effective competition in Europe's financial markets is important for consumers.

It is in everyone's interest that all market participants in the financial services industry play by the rules. By giving consumers a better deal, better-functioning markets save us all money in the short run. By contributing to economic growth, better-functioning markets make us all better off in the long run.

Be assured, that I, together with my colleagues Internal Market Commissioner Charlie McCreevy, and Consumer Protection Commissioner Meglena Kuneva, are doing all we can to work with consumers and industry to deliver the successful markets from which we all can benefit.

I look forward to hearing your thoughts on how we can best achieve this.

Thank you for your attention.