

COVID-19 AND EUROPEAN RETAIL PAYMENTS

Actions and considerations for merchants, merchant service providers, and banks



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The coronavirus (COVID-19) health crisis has had a drastic impact on the nature of transactions. Online transactions have sharply increased, while point of sale (POS) transactions have shifted towards contactless. In Western European countries overall spending has decreased by up to 50 percent year-on-year, with offline transactions decreasing by 60 percent and online transactions by 20 percent. Our analysis has found that July 2019 transaction levels are unlikely to be reached again until Q4 2021, with significant differences among sectors.

Although many geographies are gradually ending lockdowns, consumers have now developed new habits that are likely to last. In order to address these new needs, and to help merchants develop digital capabilities, merchant services providers must provide solutions that can be implemented quickly and go beyond basic payments capabilities. This challenging time is an opportunity to differentiate by promoting value-added services, such loyalty program integration and instant financing at POS.

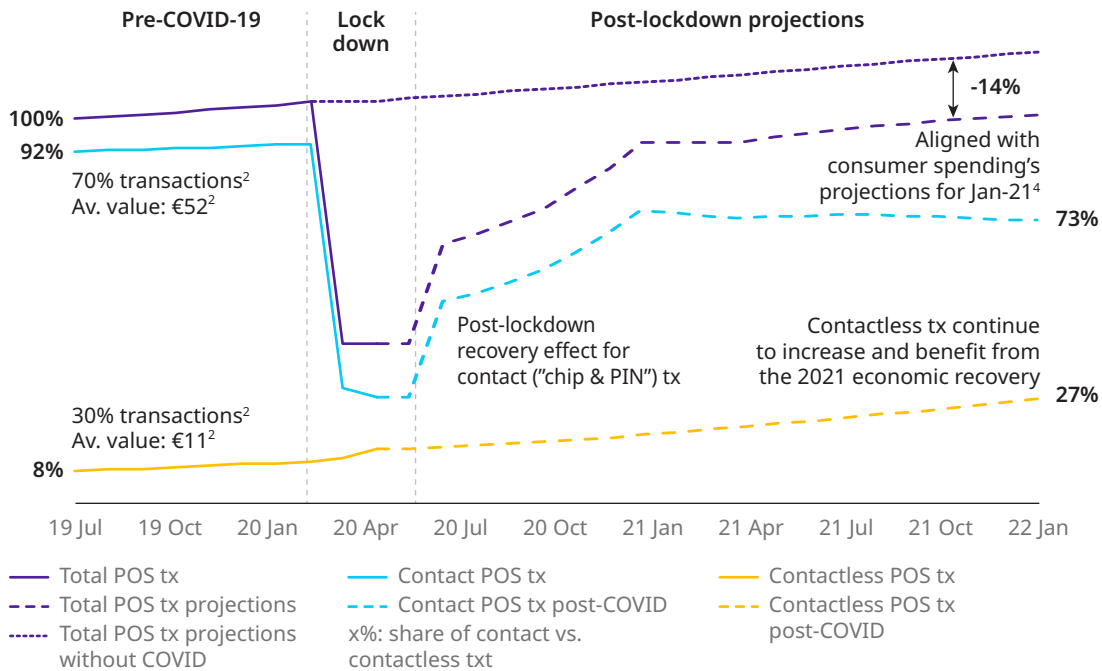
NB: This methodology is based on various sources, analyses, and press articles. Quantitative outputs rely on data from multiple countries as we track the evolution of the COVID-19 pandemic.

WHAT'S HAPPENING IN EUROPEAN PAYMENTS NOW

Although contactless adoption is accelerating, POS transaction values will take more than a year to reach pre-COVID levels. As a result, we expect contactless transactions to account for 27 percent of POS transactions (in value) by the end of 2021 (vs. 8 percent in July 2019). Under these assumptions, the level of total POS transactions would recover to July 2019 levels by October 2021.

Exhibit 1. COVID-19's impact on POS transactions in the EU¹

Index of value of transactions, 100 = total POS in Jul/19



Underlying assumptions

Pre-COVID-19

- Total POS transactions annual growth in value: ~7,5% annually (0,6% monthly)²
- POS Contactless transactions' annual growth: ~56%² (i.e. ~3,8% of monthly growth rate)

Lockdown period

- Total POS transactions: -60% y-o-y in value³
- POS contactless transactions:
 - 4% of additional monthly growth rate in March-20 contactless payments²
 - 5% of weekly growth rate in contactless payments in April-20²

Post-lockdown period

- From Jun-20 to Dec-20, POS transactions benefit recovery effect due to the end of lockdown measures
- From Jan-21, POS transactions are aligned with consumer spending (9,6% in 2021, vs. -8,9% in 2020⁴)
- Contactless transactions: pursuing historical trend (monthly +3,8%) with a premium due to consumer spending projections in 2021

1. Based on French case (GIE Cartes Bancaires);

2. Oliver Wyman (source: local banks)

3. Based on French case (INSEE, Point de conjuncture, April 9th) and Spanish Case (CEPR, Tracking the COVID-19 crisis through the lens of 1.4 billion transactions)

4. Euler Hermes projections for France, aligned with UBS projections for Eurozone

5. Based on French case (INSEE, Point de conjuncture du 9 avril 2020)

6. Oliver Wyman analysis

Source: Oliver Wyman

ONLINE TRANSACTIONS HAVE GROWN RAPIDLY, AND NOW REPRESENT ABOUT ONE-THIRD OF OVERALL TRANSACTIONS VOLUME VERSUS ONE-FIFTH A COUPLE OF WEEKS AGO

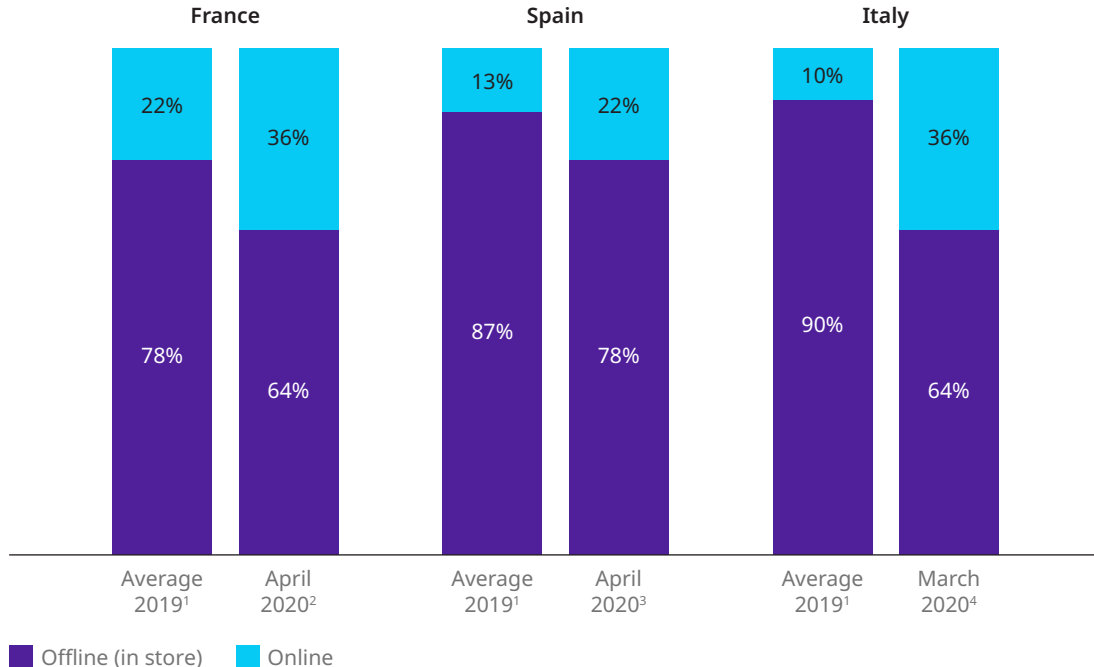
The use of cash is declining, as customers favor payment journeys that do not require contact at the point of sale. Merchants themselves are encouraging digital payments in-store, both for their own security and to respond to customer concerns. Germany, where cash accounted for 47 percent of all retail transactions in 2017 and 53 percent in 2019 according to our latest analysis, has seen its supermarkets and drugstores asking people to pay with cards instead of cash. Elsewhere, some retailers are reworking their payment journeys to be completely contactless, such as Walmart in the US which has introduced its proprietary QR code-based wallet.

In Western European countries heavily affected by the pandemic, offline transactions decreased by 60 percent year-over-year after the lockdown, whereas online transactions values have only been reduced by 20 percent, according to figures from INSEE and GIE Cartes Bancaires.

Exhibit 2. Lockdown significantly accelerated the shift from POS to E/M-commerce payment reaching up to 36 percent of all transactions in March 2020 in several countries

Domestic offline vs. online transactions

Domestic transactions in value, average 2019 vs. April 2020



1. OW analysis (sources: local banks)

2. INSEE, Point de conjoncture du 9 avril 2020

3. CEPR, Tracking the COVID-19 crisis through the lens of 1.4 billion transactions, 27 April 2020

4. Based on Nielsen data, adjusted with a 20% premium on offline to be adjusted with Spain and France methodology

Source: Oliver Wyman

SEVERAL DIGITAL PAYMENT SOLUTIONS ARE COMPETING TO GAIN MARKET SHARE AND CONSUMER ADOPTION

Banks and many merchants are pushing usage of contactless cards by increasing contactless payment limits and promoting simplicity of usage. In multiple geographies, banks have raised the contactless pay limit up to €50 in most cases. This represents approximately 15 percent of additional retail transactions that could now be performed contactless thanks to the new threshold. On top of the organic annual growth of 3.8 percent, contactless payments have increased by 4 percent in value in March 2020 and by more than 20 percent in April 2020 due to the lockdown, according to the article “Paiement sans contact — Des freins de bout en bout” in *L’Agefi*.

« X-Pay » digital solutions developed by original equipment manufacturers (OEM), such as Apple Pay and Google Pay, are seeing their usage increase due to the pandemic. These solutions, which are compliant in Europe with Payment Services Directive (PSD2) and Strong Customer Authentication (SCA) requirements, do not have a spending limit in most cases, although some POS devices do have a €300 cap. A big advantage is that the integration with merchants’ systems is seamless, as no specific contractual or technical work is needed if the merchant’s POS is near-field communication (NFC) equipped.

Elsewhere, some large retailers have developed their own payment methods to allow consumers to scan items by themselves and pay directly without waiting in a checkout line. Examples of this include Carrefour’s SelfSCAN, Monop’s Easy, and Billa’s Scan & Go. Due to the pandemic, some of these methods, such as Kroger’s Scan, Bag, Go, were suspended following the outbreak because the proprietary handheld devices that enable these solutions are too hard to clean. As a result, payment journeys conducted on the consumer’s device are considered safer, according to the *American Banker* article “Coronavirus brings lessons to retailers, issuers about contactless payments”.

As an alternative to large foreign payment solutions, and to avoid fragmented approaches by country, Europe could benefit from having its own pan-European digital solution. A group of European banks from multiple countries are working in coordination with the European Central Bank and the European Commission to come up with the European Payments Initiative (EPI), which remains to be confirmed.

OVERALL SPENDING HAS DECREASED BY UP TO 50 PERCENT YEAR-ON-YEAR, AND SPENDING BY CATEGORY HAS SHIFTED

There has been a strong downward shift in purchase volumes: instead of going to see movies, concerts or sporting events, consumers are at home watching TV and on-demand services, buying fewer clothes, and purchasing more cleaning supplies. Studies also show that consumers are purchasing less expensive products than before the crisis, and are shifting to home improvement projects and cooking more at home.

In short, consumers are limiting their purchases to what is strictly necessary. In France, the overall national expenditure is down 50 percent year-over-year, with several sectors particularly impacted. According to INSEE's, Point de conjoncture du 9 avril 2020 economic update, restaurants have seen a 95 percent decrease in volume and value of transactions, fashion a 90 percent decrease, and oil a 70 percent decrease. Whilst food saw a 25 percent decrease in the number of transactions, it also saw an increase in value of 8.5 percent.

How the pandemic will affect spending habits

For about half of consumers, only the availability of a vaccine would encourage them to revert to previous spending levels and habits, according to the article "COVID-19 Is Changing The Grocery Business" in *Pymnts.com*. Nonetheless, a recovery in transaction volumes is expected in Europe this year, and most sectors are expecting positive year-over-year growth.

Stay-at-home orders, self-service retail, and social distancing are likely to remain the norm for the foreseeable future and will impact spending behavior. As a result, merchants and payment providers need to prepare for these evolving customer habits, putting in place a frictionless, efficient, and touchless customer journey with flexibility in payment modes and associated services.

WHAT SHOULD HAPPEN NEXT

Public health requirements stemming from the pandemic are creating new consumer expectations that will require advanced digital solutions

The longer lockdown periods around the world last, the more the pandemic will have a lasting impact on consumer behavior. This crisis is expected to act as a catalyst for planned — but often delayed or deprioritized — digital transformations for banks, payment institutions, merchant services providers, and merchants.

As of a couple of months ago, cash transactions in Europe still represented almost half of total payments. New estimates show that these cash transactions are now set to fall at a compound annual growth rate (CAGR) of -2.3 percent in France¹ and -6.2 percent for the UK and for Germany².

Post-lockdown, we expect POS transactions to be driven by contact “chip & PIN” payments, with eight percent monthly growth in the three months immediately following the end of lockdown³ and roughly four percent monthly growth afterwards. However, contactless transactions will continue to grow faster than before the pandemic (3.8 percent monthly growth rate) and reach 27 percent of total POS transaction value by the end of 2021⁴.

However, there are behavioral, societal, and regulatory hurdles to the reduction of cash transactions. For many consumers, cash is still viewed as easier to use for smaller purchases. In addition, older consumers may be wary of digital payment methods, and unbanked/lower-income consumers may be excluded from non-cash payment solutions. Having a more physical connection to their money can also help some consumers with budgeting and managing debt.

During the COVID-19 crisis, ATM withdrawals in Western Europe have fallen by more than half. It remains to be seen to what extent this reduction will be sustainable post-lockdown, as consumers have had fewer spending opportunities with the closure of bars, restaurants, and shops. A survey of UK consumers conducted by LINK in April 2020 estimated that 51 percent will use cards more; 44 percent will use contactless and mobile payments more; and 34 percent will shop online more.

1 Source: The Paypers, France cash transactions set to decline by 2023, 20 April 2020

2 Source: Oliver Wyman analysis, Cash and non-cash evolution post-Covid in Germany, April 2020

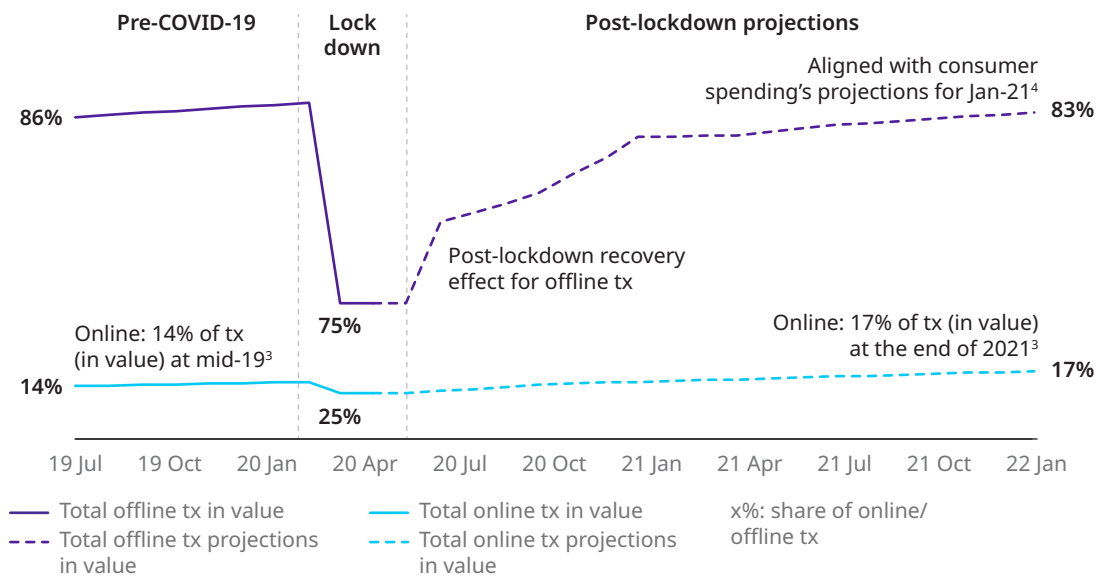
3 Methodology: Until December 2020: applying an economic recovery rate of 70% in June 2020, 72.5% in July 2020, 75% in August 2020, 78% in September 2020, 83% in October 2020, 88% in November 2020, 94% in December 2020, up to a « no recession scenario » multiplied by a recession factor (-8.9% in 2020). Until December 2021, aligning Total POS spending with consumer spending projections

4 Methodology: From May 2020 to September 2020, summing up consumer spending projections and contactless historical organic growth of contactless transactions (3.8%); from October 2020, keeping only the historical organic growth of contactless transactions (3.8%)

Exhibit 3. Payment mix and evolution of online vs. offline retail transactions¹

E-/M-commerce have performed relatively well during the pandemic, as online transactions decreased by ~20 percent (year-over-year, in value) whereas offline POS transactions dropped by ~60 percent (year-over-year, in value). Online transactions represent ~25 percent of retail transaction volume during the lockdown period, a sudden increase of 1,100 bps from a couple of weeks prior.

Index of value of transactions, 100 = offline tx in Jul/19



Underlying assumptions

Offline transactions

- Pre-lockdown: total offline transactions annual growth in value: ~7,5% annually (0,6% monthly)⁴
- Lockdown period: total offline transactions -60% y-o-y in value⁵
- Post lockdown: from Jun-20 to Dec-20, POS transactions benefit recovery effect due to the end of lockdown measures; from Jan-21, offline transactions aligned with consumer spending (-8,9% in 2020, 9,6% in 2021⁶)

Online transactions

- The rate of consumers who usually make more than half of their purchases online has increased between 25% and 80% depending on the country since March²
- Around 80% of respondents say they will start making so-called “non-essential” purchases online again in 2020²
- Assumptions for projections: monthly growth rate of 4%³ from Jun-20 to Oct-20 (post-lockdown effect); annualized growth rate of 20%⁷ applied from Nov-20 to Dec-21

1. Based on French case (INSEE)
 2. Kantar/Detail online, survey in Germany, France, UK (8/4/20)
 3. OW analysis of a recovery effect post-lockdown
 4. OW analysis (source: local banks)
 5. Based on French case (INSEE)
 6. Euler Hermes projections for France, aligned with UBS projections for Eurozone
 7. Keeping organic online growth of 14% with a “premium” of 600bps due to modification of habits post-lockdown

Source: Oliver Wyman

At the same time, on the regulatory side, some areas are proposing a ban on cashless stores (such as Philadelphia or New York City) or have made it illegal to reject cash payments (such as China).

A legal harmonization — or at least clarification — on the topic at the European level is likely to be required. Fabio Panetta, Member of the Executive Board of the European Central Bank (ECB), has stated that the ECB will ensure availability and continuity of cash. Ongoing discussions at the European level are also considering the development of a central bank digital currency (CBDC), which would allow the general population to obtain accounts directly with the ECB, which could be considered as an alternative to deposits at commercial banks. It remains to be seen how such an offering would fit into the payments landscape.

With respect to the implementation of SCA rules, the UK's Financial Conduct Authority has recently announced it will delay the implementation deadline by six months, from 14 March 2021 to 14 September 2021. It is likely that other national authorities across Europe will follow suit.

A public consultation was recently launched by the European Commission in order to prepare a retail payments strategy for Europe; this process will run from April to June 2020 and an outcome is expected to be published in Q3 2020.

VALUE-ADDED SERVICES WILL BECOME A STRONG DRIVER FOR GROWTH AND DIFFERENTIATION

A number of value-add features, services and alternative payment methods should be offered as part of the digital experience. In light of COVID-19, merchants are observing an influx of installment and buy now, pay later solutions, with consumers budgeting payments over a period of weeks, months, or even years, according to the article "Omnichannel No Longer Optional For Retail" in *Pymnts.com*.

Retailers must enable consumers to choose how to pay digitally and make it easy for them to select the payment method they prefer; so far only contactless cards have become largely accepted. Digital enablement should address other consumer pain points, such as checkout lines, loose receipts, and almost no loyalty program integration.

Beyond traditional payments transactions, holistic handling is becoming an expectation for consumers allowing handling and keeping of receipts, terms & conditions, ability to tip, guarantee documents, and the usage of loyalty points. So far, no major European or Western solution caters to these and, as a result, digital solutions have not reached their full potential. If Europe were to implement an exhaustive digital solution, **the current greater willingness of consumers to pay with this method** would boost uptake of cashless transactions and "beyond-payments" services.

OPPORTUNITIES FOR MERCHANT SERVICE PROVIDERS/PSPS

Equipping small physical merchants still not accepting contactless transactions and online transactions (such as for click-and-collect), SMEs which previously did not want to implement contactless/digital payments or online payment methods are now willing to offer these options.

Enabling omnichannel integration between physical and digital transactions including for small merchants, which with COVID-19 discovered a strong need for e-/m-commerce solutions.

Offering off the shelf solutions to allow merchants to quickly open digital stores (including landing pages, presentation of inventory, stock management, payment journeys, and associated services).

Further concentration of marketplaces that small merchants will increasingly need to use in order to be visible.

Focusing on merchant financing and credit risk services, and putting in place instant lending at the time of purchase for consumers since the economic downturn due to Covid-19 has increased the need for consumer financing at the POS, but merchants are not in a position to sustain counterparty risk and need themselves more often financing for their own liquidity.

“De-risking” of customers by providing more easily immediate settlement to merchants for goods sold to customers (in order to reduce liquidity risks on the merchant side). Some large providers, such as Alibaba in China, have expanded relief efforts to their SMEs by allowing them to receive payment from its third-party settlement platform as soon as orders are shipped, instead of after shoppers confirm receipt of their goods. Procedures for merchants that wish to develop an online channel are also being simplified and expedited.

Investigating opportunities to innovate on authentication and fraud prevention beyond cards, as online transactions see higher fraud since the pandemic started.

Increasing operational capabilities to handle chargeback and refunds and to keep track of payment movements, while remaining flexible in operations and adaptable to sector needs with an increased necessity to put in place an adequate pricing for these processes in order to not spoil margins overall by underpriced features with high volumes.

CONCLUSION

The COVID-19 health crisis has led to a strong increase in contactless and digital transactions. Consumers have gradually come to use more and appreciate these new payment modalities, which are expected to further develop and gain market share as economies recover from national lockdowns. In order to address new customer needs, stakeholders will need to develop solutions that promote seamless payment journeys and integrate and master “beyond-payments” services, such as loyalty programs and instant financing.

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