PAYMENTS POLICY FOR EUROPE: DIRECTION FOR THE NEXT FIVE YEARS

Paper by the European Association of Co-operative Banks (EACB), the European Banking Federation (EBF) and the European Savings and Retail Banking Group (ESBG), collectively representing the European banking industry and together referred to as the European Credit Sector Associations (ECSAs).

The European payments landscape is at a crossroads. Payments are the bloodline of the European economy and are thus important for the sovereignty of the European Union. For an ambitious and unprecedented shared vision to materialise, an extensive investment from the banking sector is required but also unprecedented and concrete support from public authorities will be needed. A key success factor is a long-term sustainable business model that is beneficial to all stakeholders and will enable banks to finance the considerable investments to set-up new payment solutions. The relevant public authorities should assist the market players in finding the appropriate tools to create a strong business model that works from both an economic and competition perspective, and that matches the expectations of all stakeholders involved.

Brussels, Spring 2020

EXECUTIVE SUMMARY

The European payments market has undergone fundamental changes over the past years, sparked by a mix of changing customer needs, regulatory action, technology and innovation, and increased competition.

In coming years the banking industry will continue to face multiple – and sometimes opposing – challenges in providing payments services: the full deployment of instant payments and the call by regulators to create pan-European payment solutions based on instant payments; the ongoing transformation of the payments market with competition from new players; accelerated digitalisation coupled with its impact on specific customer segments; reaping the full benefits of PSD2 and the application of data economy principles in banking and payments; the constantly evolving requirements on anti-terrorist financing and anti-money laundering activities and the potential that stablecoins/central-bank issued digital currencies could have on the payments market.

The European banking industry shares the view of the strategic value of the payments market and the urgent need for action

European decision-makers have underlined payments as an area of political importance that is expected to contribute to strengthening the international role of the euro and improving the sovereignty of Europe vis-à-vis global competitors. We share the view of the strategic value of the payments market and the urgent need for action. This action however needs a coherent strategy on an Integrated EU Payments Market.

We consider that the following aspects are essential parts of such strategy to ensure the success of the European Union in the area of payments:

- **Instant payments** are the basis: there is a need to promote a European payment initiative that is globally recognised and that allows for both the differentiation of EU companies and the reduction of dependency on a small number of dominant providers. This move requires full alignment of industry efforts with full support from EU authorities underpinned by a clear business model. The industry is committed to delivering the basic underlying infrastructure for instant payments as a basis for innovative payment solutions taking into account the new challenges for control and quality checks that the immediate execution of payments brings along.
- **Reaping the full benefits of PSD2 and beyond**: the full benefits of 'open payments' beyond PSD2 and further expansion of data sharing can only be reaped if done on the basis of mutual benefits and a fair distribution of value across market players. It is important that financial services are not considered in isolation and that data sharing is not limited to financial services. Payment aspects beyond PSD2 should be developed through a coordinated market-driven initiative establishing a SEPA API access scheme.
- **Balancing digitalisation and inclusion**: The banking industry is keen to innovate in the digital space in order to meet evolving end-user needs but also to serve all customers irrespective of their digital abilities to ensure financial inclusion. It is important that banks are able to innovate and compete with other (non-bank, fully digital) players on an equal footing. Banks still assume responsibility on some societally important functions such as cash provision, deposit accounts and payment accounts availability among others. This calls for a

debate about how to balance the costs of those functions with the need to ensure inclusion and access.

- **Digital Currencies**: we support the EU in trying to define a common approach on crypto-assets and digital currencies while preserving the stability and integrity of our financial system. Any initiatives from central banks should be carefully considered and discussed with the industry.
- **A stable regulatory environment**: Payment services in the EU are highly regulated. The current regulatory framework guarantees adequate customer protection, promotes competition and innovation and provides a coherent EU single market for payments. Regulators should balance their choices and initiatives when requiring investments from the banking industry. They must carefully consider and prioritise regulatory interventions, taking into consideration the need to support European competitiveness.

The industry is faced with considerable challenges on the road to superior European payment solutions. With a view to contributing to development of a coherent EU strategy for retail payments we will elaborate on these challenges, on how banking regulators and banks should address them together and include some considerations on what consequently should be the regulatory priorities in payments for the new Commission

1. TIME TO DEFINE A COHERENT EU STRATEGY FOR THE RETAIL PAYMENTS MARKET

The European payments landscape has evolved greatly over the last decade. Changing customer demands, the development of SEPA instruments by European banks, an intense regulatory focus and increased competition, innovation and technological change have been drivers of an ever-advancing European payments landscape.

> *It has become clear that payments are considered an important factor for European sovereignty and are an important driver for the greater international role of the euro*

Over the past 12 - 18 months, the Commission and ECB have repeatedly stressed that payments play a strategic role for the development of the European economy. Payments are considered an important factor for European sovereignty and are an important driver for the greater international role of the euro. In line with this, they have put payments high on their respective agendas. We subscribe to the views expressed by both institutions. We have reflected on what is needed to build a strong European payments environment that can compete with what is on offer in other parts of the world, preserve European sovereignty, be innovative yet offer full reach. We see a number of challenges that require addressing:

- The need to meet the varying and changing demands of different customer groups across Europe;
- The call from policymakers to create pan-European payment solutions based on instant payments, in order to give European players an opportunity to compete against incumbent and emerging non-European players. This will require major investments for the completion of the instant payments roll-out in terms of adherence, reach and interoperability and - building on this infrastructure - to run the world's most efficient and functionally complete instant payments services;
- The accelerated digitalisation of payment and banking services and its impact on financial inclusion and access to cash;
- The application of the data economy principles in banking;
- The ongoing transformation of the market structure in the payments industry, that is seeing new players, new channels to access services and new business models;
- The debate about stablecoins and central-bank issued digital currencies, and their potential impact on payment systems and services as well as on financial stability and effects on long-term investments;
- The changing needs for AML and CTF checks for immediate payment execution in the Single Market encompassing all member states with some 500 million payment services users.

With a view to contributing to development of a coherent EU strategy for retail payments we will elaborate on these challenges, on how banking regulators and banks should address them together and include some considerations on what consequently should be the regulatory priorities in payments for the new Commission.

2. THE CHALLENGES

2.1. Customer demand

Customers are the ''raison d'être'' of banks. It is not possible to envisage a long-term strategy without putting banks' customers at the heart of any future evolution in the field of payments. Based on dialogues with our member banks and their different client groups, we understand that customers would like Europe's payment environment to:

- Meet the customer needs for easy-to-use payment functionality in multiple markets, channels and user environments;
- Allow customers to be in clear control of their personal and financial data and funds and have access to sophisticated and transparent consent management tools;
- Offer competitive and innovative payment solutions that have convenience as an objective but pay due attention to security risks and offer assistance for customers that welcome support in managing their finances;
- Offer convenient payment experiences across Europe and have pan-European reach (without losing sight of the need for acceptance outside Europe);
- Recognise that payments in many cases are part of a wider experience or objective (e.g. shopping, theatre, getting a life insurance) but not an experience or objective in itself;
- Acknowledge the expectation that different means of payment (cashless and cash) remain available to customers;
- Recognise that there is still demand for different types of payment instruments depending on customer interest and habits (pull vs push payments);
- Recognise the retailer's wish for the creation of an instant payment based omni-channel interoperable payment framework that can support multiple use cases and channels and offer an end-to-end payment experience.

2.2. The call to create pan-European payment solutions based on instant payments: completing the basics

The industry is looking to rapidly finalise the inter-bank instant payment infrastructure on which innovative solutions for end-users can be built by payment service providers. We are aware that some groundwork still needs to be done before the new, efficient and functionally rich European instant payments infrastructure can be used to bring new value and efficiency to the European economy.

> *The industry is looking to rapidly finalise the inter-bank instant payment infrastructures on which innovative solutions can be built*

When it comes to **adherence,** we recognise that not all payment accounts of EU consumers and businesses can be reached as not all relevant Account Servicing Payment Services Providers (ASPSPs, or banks) already adhere to the underlying scheme. At this point in time we consider regulatory action to enforce adherence premature as the banking industry is striving to get maximum adherence for SCT Inst in euro by 2021.

On the point of **reachability and interoperability**: it is acknowledged that currently not all banks that have adhered to the SCT Inst scheme are able to be fully reachable across Europe due to a lack of interoperability of the Clearing and Settlement Mechanisms (CSMs). We encourage the ECB, responsible for TIPS, together with the other CSMs to urgently resolve the issues related to the interoperability of the infrastructure layer. We have greatly appreciated the initiative taken by the ECB in February 2020 to organise a dedicated workshop between CSMs and a selection of banks to address this issue. We note in particular that several suggestions were made to move things forward and would welcome swift follow-up.

Whilst European banks have successfully developed and rolled out pan-European payment schemes for regular credit transfers and direct debits, certain areas of the payments market remain fragmented. Cross-border card payments in the internal market, for example, are only possible because of the solutions provided by a few global, non-European market players.

This creates a reliance on such players, which can become a risk from an economic, political, operational and privacy perspective. The threat of undesired dependency increases when considering the growing global BigTech interest in payments. Dependency on such actors for basic EU internal market functions underpinning the economy - starting from payments but likely expanding to consumer finance, mortgages and other financial services – may bring detriment to the European economy. As per the ECB[1], "*dependence on non-European global players creates a risk that the European payments market will not be fit to support our Single Market and single currency. It makes it more susceptible to external disruption such as cyber threats, and that service providers with global market power will not necessarily act in the best interest of European stakeholders"*.

From a data privacy perspective, global BigTech's existing data superiority combined with access to payments data should be concerning and could lead to unintended negative outcomes for EU citizens.

> *The banking industry is ready to embark on this unprecedented and ambitious challenge, but this challenge cannot succeed without the support from public authorities and regulators alike*

As a response to these challenges, the European banking sector is keen to provide Europe with a payments framework that can effectively compete within Europe but that can also ultimately have global recognition in order to cater for all the end-user needs in a globalised EU economy. The goal is to build solutions that will have the following key components:

- **Scope**: cover all major use cases at the point of interaction, e-commerce, m-commerce, bill payments and person-to-person transfers with a consistent leading-edge user experience.
- **Security**: real-time transactions must meet stringent security, fraud prevention and AML requirements. Trust is a major driver in evolving payment habits.
- **Consumer protection**: the service should aim to inspire consumer confidence.
- **Processing**: real time functioning, based on the SCT Inst scheme that requires availability 24/7/365.
- **Autonomy**: the solutions should maintain its independence and result in the creation of a strong European recognition mark that will ease customers' recognition.

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[1] Benoît Cœuré, Member of the Executive Board of the ECB, 'Towards the retail payments of tomorrow: a European strategy', speech at the Joint Conference of the ECB and the National Bank of Belgium on "Crossing the chasm to the retail payments of tomorrow", 26 November 2019.

- **Reachability and interoperability**: the foundation of any pan-European payment solution is reachability of payment accounts and that needs to be ensured by interoperability of the infrastructure layer.
- **Governance**: transparent and inclusive governance towards all relevant stakeholders.
- **Accessibility:** customer interfaces that support use by all types of customers also in accordance with the provisions of the Accessibility Act.
- **Reuse European building blocks**: the solutions should leverage on existing and upcoming European building blocks (such as SCT Inst, Request to Pay and PSD2 interfaces).

The banking industry is ready to embark on this unprecedented and ambitious challenge. However, the challenge to provide Europe with complete instant payment-based solutions spanning all types of payments requires the industry to cover completely uncharted territory and to compete with very successful existing providers.

For the banking industry to undertake this challenge, an extensive investment in time and resources is required from the banking sector. We believe however that also unprecedented and concrete support from public authorities will be needed. A key success factor is a long-term sustainable business model that is beneficial to all stakeholders, including banks. The relevant public authorities should assist the market players in finding the appropriate tools to create a strong business model that works from both an economic and competition perspective and that matches the expectations for all stakeholders involved.

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2.3 Digitalisation

2.3.1 Managing the market structure transformation in payments

PSD2-supported access to payment accounts data, digital transformation, open data initiatives and the entrance of BigTech players in the payments industry are factors that are transforming the payments industry. BigTech players are aiming to capture parts of the payments value chain acting as payment initiators or even payment service providers, driven by business models cross-subsidised by customer engagement and commercialised data profiling that enable pricing of the payment service that traditional banks cannot match.

While competition is a welcome element, policy makers but also the banking industry as a whole and banks individually, have to reflect on how to they want the current ecosystem to evolve. One question to address would be how to preserve the qualities of the present ecosystem, such as inclusive access to payments, and access to services such as cash and other physical products, for which demand is shrinking; that are expensive to manage and hard to price to meet increasing costs as volumes shrink. Another, more difficult one, relates to the more general role of banks which, beside PSPs, are also providers of the infrastructure that supports the execution of monetary policy goals. Additionally, we believe that non-discriminatory access by payment service providers to vital components (e.g. NFC or biometric identity readers) of mobile devices will contribute to a more competitive market.

2.3.2 Digitalisation and inclusion

Digitalisation is a major driver for innovation and will only accelerate in the future. Banks are keen to develop user-friendly, fast and innovative digital services for their customers. It is important that banks are able to innovate and compete with each other and also with other (non-bank) players on an equal footing.

Banks are also keen to service all their customers, regardless of their digital abilities. However, we observe that the growing digitalisation can bring up tensions and choices, in particular in the areas of co-existence of cash and electronic payments and providing services to customer segments that hesitate to or have difficulties in adapting to the digitalisation of payments and other financial services.

Co-existence of cash and electronic payments

Despite continuous growth in cashless transactions we observe an increasing concern about the need to ensure access to cash from certain parts of the stakeholder community with the expectation that this access should not need to cover its own costs. At the same time banks are requested to make heavy investments for the development of new means of electronic payments (most notably the development of pan-European instant payments). Furthermore, banks face competition from digital-only providers that do not support cash services or face-to-face services, do not invest in the required infrastructure and yet use the infrastructure provided by banks for the benefit of their own customers.

Banks therefore need to find a sustainable balance between consumer demand for cash, face-to-face services and social responsibility on the one hand, as well as efficiencies in the cash cycle and provision of physical services on the other hand.

Ensuring access to electronic payment services to all customer segments

Banks continuously need to balance between providing cost-effective services to the vast majority of their clients and maintaining services to more vulnerable segments at reasonable (low) cost. Recently this has become clear e.g. in the implementation of the legal obligations on SCA under PSD2, where consumers that do not possess a smartphone could be unable to fulfil SCA requirements. Legal requirements should at the point of inception take into account the need for financial inclusion and not put banks in an impossible situation of having to choose between legal compliance and discontinuing services to some of their clients.

2.3.3 Reaping the full benefits of PSD2 for payments and beyond

With the opening of payment accounts data and infrastructure, PSD2 has opened a new era in banking. We recognise that this is only the first step towards the wider development of data sharing, both in the area of payments and financial services and the broader economy.

A flourishing data-driven market – be it in payments, broader financial services or between different industries – should be based on principles of mutual benefits and potential monetisation of services and infrastructure by all market participants, and thus should take a different approach to PSD2.

With regard to payment functionalities that are beyond the scope of PSD2 (such as payment guarantee, delegated SCA etc.), these should be elaborated through a coordinated market-driven initiative within the Euro Retail Payments Board (ERPB) SEPA API access scheme work. The ERPB should seek to launch the work on a scheme as soon as possible building on the work already carried out within the ERPB.

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As to the potential development of 'open finance' extending beyond payment accounts, and the development of a European data economy, it is important that financial services are not considered in isolation and that data sharing is not limited to financial services. The current asymmetries in data access should be solved in a harmonised European framework. A multi-sectorial approach would be needed in order to fulfil consumer's expectations, ensuring a level playing field for all players, reciprocal benefits and the highest standards of consumer protection.

For all these developments, the guiding principles should be the following:

- Customers should be at the centre of an open banking market.
- All market players can benefit, based on mutual benefits that allow them to monetise and build business cases for the services they offer as well as for the availability of their infrastructure.
- Security and ethical use of data in a data-driven market is ensured.
- APIs should be the means of access to the data by third parties due to the security of data, scalability and interoperability they provide.

2.3.4 Digital currencies

Banks recognise that digital currencies, including stablecoins and CBDC, can be used for settling commercial transactions. We believe, as recognised by the EBA that these products, if used for that purpose, comparable to payment transactions, should be subject to the payment services regulation along the same lines as any other mean of payments e.g. EMD and PSD2 rules should apply. When it comes to security and customer protection, digital currencies providers should not only comply with those rules, but also with data protection and privacy requirements as stipulated in the GDPR, in addition to rules related to AML, KYC or CTF in order to ensure the protection of consumers, market integrity and financial stability. All players in the payments ecosystem should contribute to these objectives.

The ECSAs note that in some discussions, it has been stated that a global stablecoin could be needed in order to facilitate cross-border payments. In the European context we do not see such a need as cross-border payments intra EU within the SEPA area are considered domestic and already well developed and regulated. Instant cross-border payments are among them a reality that is being expanded. Pursuing the idea of stablecoins in the EU should carefully consider the business case for investments in the expansion of instant payments.

The ECSAs therefore welcome the Commission's ongoing work in this area and its aim to propose a common EU approach on crypto-assets markets and its commitment to protect the integrity and stability of the European financial system. The ECSAs have noted the Commission’s consultation on this topic and are looking forward to further engage.

When it comes to Central Bank Digital Currencies (CBDC), we believe that any policy dialogue on this topic should include the banking industry and should not seek to replace private sector actors but should be a common project between the European System of Central Banks and European banks. Central bank issued electronic money plans need to be aligned in the discussion on Europe’s payment ecosystem development, since a central bank issued and distributed digital currency could surpass the entire electronic payments market in Europe, even replace the current account business of credit institutions and have financial stability consequences. It is imperative to clarify the possible role and service of the central banks versus banks to end users in the retail market in order to provide justification for the continued investment in development of improved EU level payment instruments in the private and competitive sector. Moreover, any plan would need to be aligned with the discussion on pan-European payment solutions and provide certainty for banks developing improved EU level payment instruments in the private and competitive sector. Authorities should assess the long-term consequences for banks and the financing of the EU economy of an initiative such as this before engaging in it.

3. REGULATORY CONSIDERATIONS

In the past years, banks have faced major regulatory implementations in the field of payments, including the SEPA Regulation, Interchange Fee Regulation, the Payment Accounts Directive (PAD) and PSD2 in addition to the regular updates of the AML/CTF directives. The review of the Cross-Border Payments Regulation and reporting obligations on PSPs for the purposes of combatting VAT fraud will require implementation effort in the coming months and years. In several cases, implementing these new obligations require heavy investments from the banking industry which are not offset by new or additional revenues. With the busy regulatory agenda of the past years still resounding and the development of pan-European instant payment solutions having become a political priority going forward, any new the regulatory action of the new Commission in the area of payments should be carefully considered. Our considerations are the following:

- **The implementation of PSD2 RTS on SCA & CSC:** this has required a huge effort by the industry and has still not been finalised. The review of the RTS should not take place before some years, in order to provide for stability in the market. Uncertainty about legal obligations has been one of the major factors leading to a delayed implementation of parts of the RTS. Opening up a review would again create such uncertainty and divert important industry resources that are required elsewhere.
- **Reaping the full benefits of PSD2**: we recognise that the present market outcomes of PSD2 could benefit from further cooperation between market participants as well as further standardisation in order to deliver the full benefits of innovation and competition. But it is essential to move away from the logic of PSD2, whereby banks have to provide access to their accounts to providers of the newly regulated services without any contractual relation and without any fair distribution of value (i.e. without any compensation for the access to the payment account infrastructure and data banks make available). Instead, all market players should be able to benefit based on mutual benefits that allow them to monetise and build business cases for the services they offer. The most efficient way to foster this development is through coordinated market-driven initiatives and not regulation. A SEPA API access scheme would ensure wide market adoption and harmonization, while allowing innovative and competitive approaches by scheme participants.
- **The issue of customer mobility:** this topic is been discussed many times over in the past and is again a part of the discussion of the review of the PAD. We believe that the discussion on this topic needs to take place taking into consideration that customer mobility is a means to an end and should not become an end in itself. We understand, that in the eyes of the Commission, the level of bank account switching is seen as a measurement of competition in the market. But if the ultimate objective is to increase competition in the market and give consumers more choice, then the level of customer mobility is just one indicator, and possibly not the most relevant one. We firmly believe that the combined effect of EMD, EMD2 PSD and PSD2 have brought a lot of additional competition to the market, both in terms of the kind of institutions that are active in the market and in terms of the product they offer. There is strong competition in the retail payment sector and in the relevant cross-border areas among credit institutions on the one hand and between credit institutions, payment institutions, e-money institutions, AISPs, PISPs and even BigTechs on the other hand. This being the case, the level of competition in the market should not be measured by the number of bank switches but by for example, counting the number of new contracts concluded with PSPs.

  In any case, the members of the ECSAs would consider that – when it comes to the topic of customer mobility – options such as the introduction of account number portability should not

be pursued as they would overshoot the target by far, undermine the legal and account infrastructure built for SEPA, wreck the payments' routing systems, defy the goal pursued by AML and CTF reporting requirements as well as require once more important investments from the industry and national competent authorities alike.
- **The assessment of the impact of the Interchange Fee Regulation:** we believe that no urgent changes to the Regulation are warranted at this point. The market has successfully absorbed the changes prescribed by the Regulation, the impact of the Regulation has not yet fully deployed its effect on the market and there is no market failure that justifies a review. Opening a review at this point in time creates uncertainty in the market about underlying business models and will hence jeopardise important decisions being taken towards the developments of new pan-European payment solutions.

With the busy regulatory agenda of the past years still resounding and the development of pan-European instant payment solutions having become a political priority going forward, any new the regulatory action of the new Commission in the area of payments should be carefully considered

Overall, the ECSA members consider the current legal provisions are largely fit for purpose. They would urge the Commission to:
- Consider any further adjustment in the present regulatory framework on payments in the broader context of the different developments and subsequent investments required in the area of bank accounts/payments (see chapter 2 of this paper) and not treat them in isolation;
- develop fully fledged cost-benefit analyses in cooperation with the market of any measures to be considered with this bigger picture in mind; and
- prioritise at the broader level what it wants the banking sector to focus on accordingly.

4. RECOMMENDATIONS AND CONCLUSIONS

The challenges that the payments industry is currently facing require the definition of a clear and consistent strategy for the years to come, within a stable regulatory framework. The banking industry wishing to contribute to this discussion, considers that the following aspects are essential to ensure the success of the European Union in the area of payments:

- **Customers at the heart of payments evolution**: the focus of any payment related initiative or development should be a seamless customer experience meeting the needs and that takes into account instantaneousness, security, data protection, convenience and the existing diversity of payment means.
- **Instant payments are the basis**: there is a need to promote a European payment initiative that is globally recognised and that allows for EU companies to differentiate their payment offerings and allows for the reduction of dependency on a small number of global, non-European providers. This move requires full alignment of industry efforts with full support from EU authorities underpinned by a clear business model and long-term sustainability. The industry is committed to delivering the basic underlying infrastructure for instant payments as a basis for innovative payment solutions.
- **Reaping the full benefits of PSD2 and beyond**: the full benefits of 'open payments' beyond PSD2 and further expansion of data sharing can only be reaped if done on the basis of mutual benefits and a fair distribution of value across market players. Payment aspects beyond PSD2 should be developed through a coordinated market-driven initiative establishing a SEPA API access scheme.
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- **Digital Currencies**: we support the EU in trying to define a common approach on crypto-assets while preserving the stability and integrity of our financial system. Any initiatives from central banks should be carefully considered and discussed with the industry.
- **A stable regulatory environment**: Payment services in the EU are highly regulated. The current regulatory framework guarantees adequate customer protection, promotes competition and innovation and provides a coherent EU single market for payments. Regulators should balance their choices and initiatives when requiring investments from the banking industry. They must carefully consider and prioritise regulatory interventions, taking into consideration the need to support European competitiveness.

ABOUT THE AUTHORS

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The European Association of Co-operative Banks (EACB) represents, promotes and defends the common interests of its 27 member institutions and of cooperative banks, with regard to banking as well as to co-operative legislation. Founded in 1970, today the EACB is a leading professional lobbying association in the European banking industry. Co-operative banks play a major role in the financial and economic system. They contribute widely to stability thanks to their anti-cyclical behaviour, they are driver of local and social growth with 2.800 locally operating banks and 51,500 outlets, and they serve 209 million customers, mainly consumers, SMEs and communities. Europe's co-operative banks represent 84 million members and 713,000 employees and have an average market share in Europe of about 20%. For more info, please visit www.eacb.coop.

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Brussels, Spring 2020.

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