

The New Way to Pay

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One year into the most sweeping regulatory reforms to the payments industry, how much has really changed for consumers and merchants? Has complexity surrounding this new legislation made merchants more apprehensive about how they should try to capitalize on the opportunities PSD2 presents?

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Bank transfers present a compelling commercial opportunity, but require a combination of superior experience, consumer education and creativity to be realized.

Payments – From the back office to center stage for the travel industry

A collision of forces is revolutionizing how we pay for travel. Are you prepared for the changes ahead?

01

Traditionally, payments have been largely an afterthought in the purchase process for the travel industry. They have been the final hurdle for consumers, rather than adding any form of value in the customer journey. Innovation was limited to incremental improvements in speed, security or acceptance, but all transactions ultimately still relied on the same mechanism invented many decades ago – the plastic card in our wallets.

No longer. Today we're witnessing a collision of forces – spanning changing consumer behavior, privacy concerns and new regulation – that have been building in momentum for several years. And together they're creating opportunity and risk in equal measure.

An ever more demanding consumer

We live in an instant gratification culture where people want it all – and they want it delivered same-day. After all, if your favorite coffee brand can do this, why can't your hotel? If your bank can do this, why can't your airline?

Today's consumer doesn't distinguish between one sector or another – they only see experiences, which translate to expectations, and they'll happily (and quite easily) take their wallet elsewhere if these aren't met. They want businesses to meet their needs on their terms – and increasingly payments are playing an influential role in who customers choose to buy from. The payment journey is becoming a central, rather than peripheral, part of the customer experience.

The rise of the millennials

Already the world's largest demographic, the millennial generation is undeniably an economic force to be reckoned with. And while blanket stereotypes for an entire generation are both imprecise and already overdone for this cohort, two characteristics set them apart from preceding generations.

First, their attitude towards money and debt is different from their parents'. They've grown up during a severe and far-reaching economic crisis, along with its protracted recovery and – for many – an era of pain-

ful austerity. They've seen the hard consequences of questionable lending, and, as a result, tend to be financially more risk averse and less likely to favor traditional credit cards.

Second, they are the first generation to grow up in a truly digital era. A mobile-first, hyperconnected world where technology has seemingly permeated all aspects of their lives. Where a wallet isn't defined by its physical constraints but is a concept in their digital existence. This not only shapes their behavior, but also their expectations. And this tech-savvy audience is demanding. While their parents may fondly remember a world of slow connection, limited choices, fragmented payment journeys and poorly designed iframes, this is often foreign to millennials.

In fear of fraud

While the pervasive nature of technology and our connected society has many benefits, it also has a major byproduct: lots of consumer data. And, this data paints intricate details of our lives. Over the past couple of years, due to several high-profile

cyber attacks, data breaches and misuses of personal information, consumers are more conscious of both the value of their data, and the risk inherent in allowing organizations to access or store it. This is having a very real impact on how people pay.

How many businesses do they really want to store their card details, in the name of convenience for a future purchase? How trusting are they in the security around transaction processing? Will parting with financial information online risk losing their identity if a business can't guarantee to keep it safe?

Game-changing regulations

Perhaps most important is the shifting regulatory landscape affecting payments. In Europe, often considered one of the most progressive policymakers in data and technology, seismic changes are shaking up the payments ecosystem.

The latest legislation is the Second European Payment Services Directive (PSD2), a multifaceted piece of regulation, designed to create a more competitive payments ecosystem by bringing the bank account back in to play – by enabling third-party access for both data and functionality. It is hoped this will encourage more competition through new market entrants, foster innovation and collaboration, and improve consumer protections. But even



greater significance lies in the detail of the directive's Regulatory Technical Standards (RTS), which aim to all-but eliminate fraud. Almost all card transactions will be subject to mandatory two-factor authentication, further heightening the tension between user experience and security.

While PSD2 provides a welcome opportunity to reshape the payments landscape through regulation, we shouldn't underestimate the scale of this task. The payments industry is no stranger to regulation focused on addressing market inefficiencies and introducing more competition, ultimately to the benefit of consumers. However, looking at the consequences of two pieces of legislation introduced in recent years it is unclear if they fulfilled their brief and suggests that regulation alone might



not be the panacea that the market needs to have a competitive and thriving environment.

Consider that in 2015, regulators seized on interchange fees – the charges levied when consumers make a card payment. Citing serious competition concerns, the Interchange Fee Regulations (2015) introduced a cap on these charges, estimated to have led to a 50% fall in average EU credit card interchange over 18 months, at an annual cost of approximately €2bn for credit card issuers.

However, according to some people, the interchange fee cap was unsuccessful, and didn't directly translate into lower prices for consumers as was hoped. Instead, many credit card issuers responded to their revenue losses by reducing consumer loyalty

programs or introducing new card fees to compensate. While it was a step in the right direction, it's widely felt that there's some way to go before the market becomes truly competitive.

As another example, in 2011, following an official super-complaint, the UK's Office of Fair Trading mandated that card surcharges for consumers must reflect the true cost of processing. This resulted in the Payment Services Regulations of 2017, which finally killed card surcharges, a practice widely found in the travel and aviation sector. However, it is contended by many that the legislation has been ineffective and it remains to be seen whether this results in a better deal for consumers or simply higher prices.

These pieces of legislation attempted to

tackle the dominance of the card payment ecosystem by limiting the amounts consumers and merchants could be charged for their participation, rather than actually fostering competition by introducing a credible alternative. Bank transfers can be that challenger.

PSD2 provides the regulatory framework to allow banks and fintechs together to really offer a new way to pay for European consumers. Couple this with the technological advances in instant payment schemes, such as SEPA Instant being rolled out currently across the Eurozone and Hungary's instant credit transfers set to go live in 2019, as well as upgrades to banks' online systems and mobile apps, and you almost have the perfect conditions to mount a challenge to the decades-old reliance on cards.

Should anyone be surprised that bank transfers are forecast to overtake traditional card payments for online purchases in 2021?

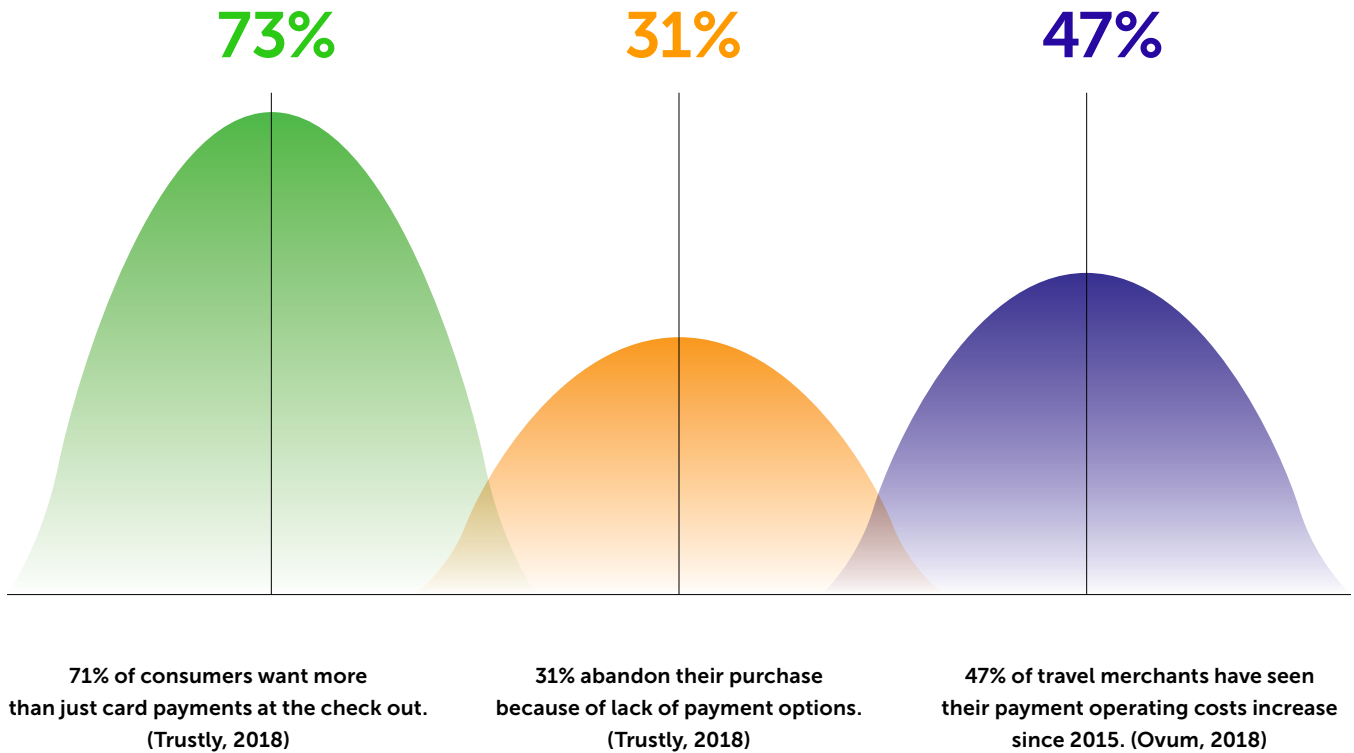
Reducing cost, creating value

Exponential increases in consumer expectations. Shifting attitudes to money across generations. The growing cost, reputational risk and consumer awareness of fraud and data loss. A dynamic regulatory environment heralding the era of open banking.

In concert, these forces have elevated payments to an issue of strategic and commercial prominence, not merely technical. Together they are unlocking opportunities for improvements in operational efficiency (particularly for global businesses), cost reduction, fraud and chargeback prevention, and wider consumer appeal and reach.

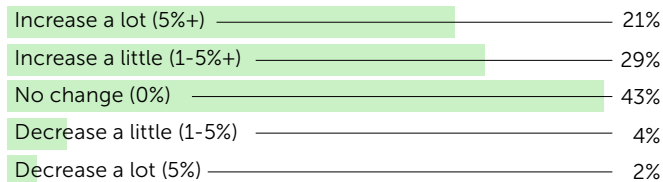
But are they opportunities that your organization is primed to capitalize on? Are you ready for the changes already underway, as well as those that will follow tomorrow? After all, the customer doesn't stand still – and neither can you.

The increasing pressure to invest in payments

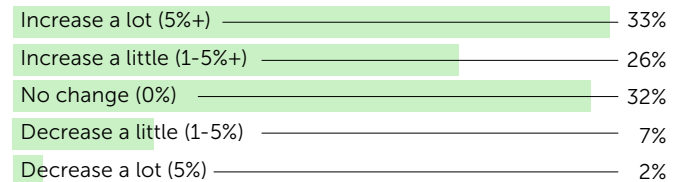


How do you forecast your investment in payments to develop in the next 18-24 months?

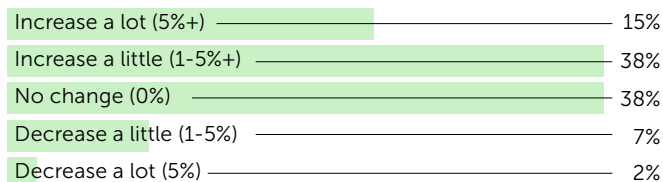
2018



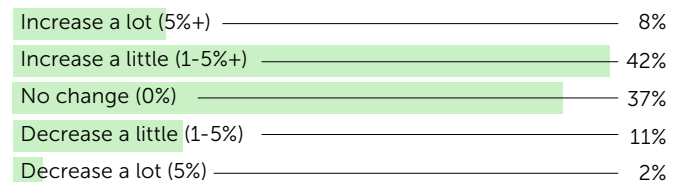
2017



2016



2015



Source: Ovum, 2018, Global Payments Insight Survey - could only show 'Increase a Lot/Little' to group together

As APMs take off, will you be left behind at the departure gate?

With a payments revolution permeating all corners of e-commerce, is travel at risk of being left behind?

02

By 2021, more than half of all online transactions around the world will be conducted using alternative payment methods (APMs). You can't help but pause to reflect on that number and its profound implications.

Not only is cash continuing its slow decline in the offline world, but even online it appears the reign of the credit and debit card may indeed have seen its heyday. Today, e-wallets and instant bank transfers are seeing the fastest growth among the more than 300 APMs and Worldpay predicts that bank transfers in particular are predicted to become the second most popular payment method globally by 2021.

Alternative payment methods are no longer alternative – they're on the verge of becoming the prevailing method.

Thomas Heldorff, Vice President,
Airlines and Travel, Worldpay

The travel and airline sector is far from immune to these changes in the payments

landscape. From low-cost airlines that generate 90% of their revenues through a direct channel, to flag-carrying airlines booking some 40% of distribution online, to online travel agents placing digital at the heart of their model, the sector is at the very epicenter of e-commerce and the digital revolution of the last decade (and indeed has seen some of its leaders usher in pioneering, industry-leading mobile and e-commerce innovations).

So, what do these shifting sands mean for leaders in travel? What's behind changing consumer attitudes and behavior towards payment? And what are the first steps for the industry to respond?

Not all payments are created equal

To say that all consumers are happy to pay in the same way is as naïve as to suggest that all consumers will choose the same brand or share the same need.

Our attitudes towards money, payment, technology and security are influenced by a few factors. Understanding them is the

first step in understanding your consumers, their preferences and expectations, and ultimately the right payment options that will help to win share, improve conversion and build loyalty.

At their most simple level, these factors fall into two groups: geographic and generational.

The geographic effect

Where a consumer is from is the first clue to identifying his or her likely payment preferences. It can also help identify opportunities for merchants, based on three different contexts.

Monetary context

A consumer's familiarity with different forms of financial services will have a direct impact on their attitudes towards APMs. According to the World Bank, credit card ownership in the UK and US is 65% and 66% respectively, whereas in Sweden and France, the figures drop to 45% and 41%. In the latter, therefore, more people might be predisposed to APMs because they reside in less card-centric nations, offering

greater reach within these markets for those merchants able to deliver relevant and flexible alternatives.

The UK and US are very card-centric, but culturally Europe has always seen a stronger bank proposition. Countries such as the Netherlands, the Nordics and Germany are more likely to favor bank transfers or e-invoices, supported by their comparatively high levels of digital maturity.

Mike Parkinson, UK General Manager and Director of Travel, Trustly

Technological and connectivity context

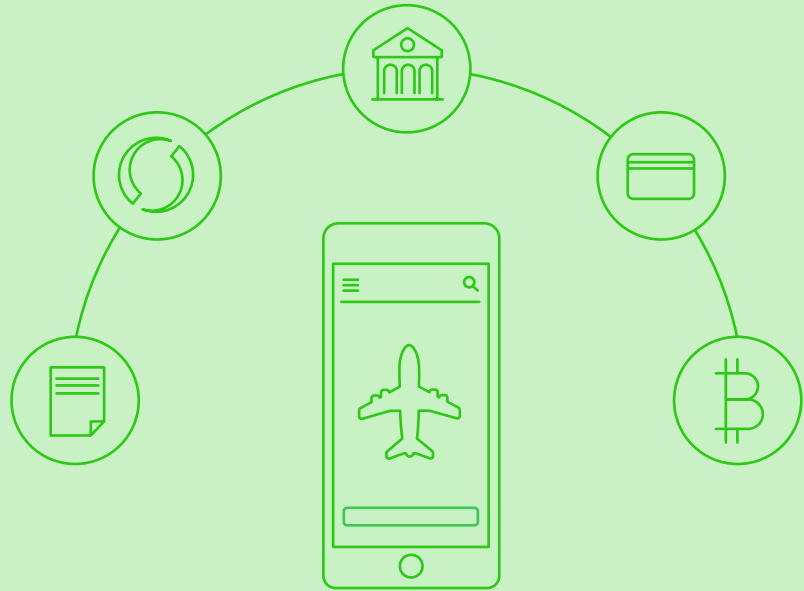
The maturity of a nation's digital infrastructure and its citizens' connectivity is another leading indicator of potential payment preference. In the UK and Sweden, for instance, smartphone penetration in 2018 reached 82% and 79% respectively, and, in 2016, the number of citizens using the internet to pay bills or to buy something online reached a significant 81% and 84%. In contrast, a market such as India may offer a greater populous, but its comparative smartphone penetration lies at 29% and its online purchasing at 4%, according to the same research.

This suggests how travelers in different markets may respond today to payment innovations or alternatives to traditional card transactions. But looking ahead to tomorrow, given urbanization and a burgeoning middle class in India, hundreds of millions of people are moving up the income ladder. Government policies such as the demonetization of the rupee in 2016 have helped to loosen cash's stranglehold on commerce and helped introduce millions to digital payments and banking for the first time. Millions of consumers will graduate from feature phones to smartphones over coming years, further improving digital equality across the nation.

Cultural context

Different behaviors in relation to payments are ingrained in a country's culture,

What are APMs?



The term Alternative Payment Methods (APMs) is used to describe a collection of new, technologically-powered ways for consumers to make purchases away from the mainstream card providers, such as Visa and Mastercard. According to Worldpay, there

are more than 300 APMs in operation around the world, and they typically take one of several forms: bank transfers, direct debits, e-wallets, mobile payments (direct carrier billing or mobile wallets), local card schemes, pre-pay, post-pay, and e-invoices.

although this is changing as its citizens' experiences and expectations change. According to Worldpay's 2016 report "Why do they pay that way?", 80% of US consumers surveyed said they preferred to book flights using a credit card, compared to just 37% of consumers in Germany. The same study also found that travelers choose their preferred payment types for varying reasons, with Australian consumers favoring travel-related benefits, US consumers prioritizing simplicity, and Chinese consumers sticking with what feels most familiar. Moreover, the research reported that almost half of consumers in Brazil, China and India prefer to pay for their trip in installments – more than twice that in Australia, Germany and the US.

The generational effect

Compounding the geographic effect is the impact of changing demographics and shifting generational attitudes and behaviors. While Gen Xers and baby boomers are by no means excluded from exploring new payment options beyond the plastic card, millennials and Gen Zers tend to exhibit markedly different attitudes towards credit than their parents. Indeed, Worldpay's 2016 research found, across six markets surveyed, that 26 to 35 year olds were the most likely to fund their flights using savings, rather than credit.

What's more, their familiarity with the digital world is reflected in their use of APMs. Worldpay's latest Global Payment

User experience and consumer education – the entry criteria

Successfully deploying APMs into your payment ecosystem and winning at the point it matters – customer conversion and loyalty – will be shaped by a number of factors. Without a doubt, it can be a complex and technically challenging endeavor, especially for those in the travel and aviation sector using legacy systems built on rules from decades ago. Yet the commercial arguments for doing so speak for themselves – both in terms of cost saving and operational efficiencies, as well as positioning an organization for growth.

But before complexity and technologies can be considered, success hinges on two fundamental factors. The entry criteria to even consider progressing your payments strategy.

The first is user experience. In today's mobile and app-centric world, consumers tolerate nothing less than a slick and seamless user experience. We hear these words time and again and while they're easy to say, they're not always followed through with execution. Introducing any changes – no matter how well-intentioned – to payments will likely fail at the first hurdle, unless it provides a superior payment experience, and offers the consumer tangible integrated value.

The second is consumer education. The travel and airline industry grew up

on the back of credit and debit cards, with which adult travelers are all but universally aware. But consumers are demanding more choice, more speed, more security and more convenience, and are showing by virtue of sheer numbers that they have an appetite for an alternative to the mainstream. However, implementing APMs alone – simply providing consumers with more options – is not the same as more choice. For consumer adoption to occur, consumer education is paramount. And given how diverse our consumers can be, this can be far more effectively achieved during the purchase journey than with above-the-line communication to the masses.

Together, a true commitment to a superior payment experience and meaningful investment in consumer education can provide the foundations for success.



Mike Parkinson, UK General Manager and Director of Travel, Trustly

Report reveals that while the proportion of the population to shop online in western economies such as the US and UK is consistent across generations, in emerging markets such as Mexico and China, millennials were significantly more likely to shop online than other cohorts. Moreover, the same research found that 28% of millennials had used a mobile wallet at the point of purchase, compared to a global average of 20%.

Understanding not just the geographic context of your traveler, but also the defining characteristics, expectations and behaviors of their generation, is therefore key to identifying the payments methods that will work best from one market to another.

Creatures of habit?

So, to our opening thesis: is travel at risk of being left behind in the alternative payments revolution? When it comes to booking flights and travel, are consumers indeed creatures of habit, destined to perpetuate a decade's old reliance on the plastic cards of yesterday?

It appears that habits can be broken, and change is already underway.

“The way people pay is ingrained in their culture and you have to tap into that to make a difference. KLM is selling online in 85 countries and we have a dedicated localized payment mix in every country. It is not about offering as many options as possible – it is about offering the relevant options per market.”

Maarten Rooijers, Senior Manager, Customer Payments, KLM

Breaking creatures of habit: APMs are going mainstream in travel

The charts below show the most popular e-commerce payment methods in different geographies. By 2022, bank transfer will be the second most popular e-commerce payment method.

EMEA (2018)*		EMEA (2022)**	
		*Estimated	**Forecasted
eWallet	21%	eWallet	24%
Credit card	20%	Bank transfer	20%
Debit card	20%	Debit card	17%
Bank transfer	16%	Credit card	14%
Charge & deferred debit card	10%	Charge & deferred debit card	10%
Cash on delivery	7%	Cash on delivery	7%
eInvoices	3%	eInvoices	7%
PrePay	1%	PrePay	1%
Pre-paid card	1%	Pre-paid card	1%
Other	1%	Other	0%
PostPay	0%	PostPay	0%

China (2017)	Germany (2017)	Netherlands (2017)
eWallet 65%	Bank transfer 27%	Bank transfer 59%
Bank transfer 11%	eWallet 20%	Credit card 14%
Credit card 9%	Credit card 18%	eWallet 10%
Charge & deferred debit card 5%	Charge & deferred debit card 11%	eInvoices 6%
Debit card 5%	Cash on delivery 9%	Cash on delivery 6%
Cash on delivery 3%	eInvoices 8%	Debit card 3%
Pre-paid card 2%	Debit card 2%	Charge & deferred debit card 2%
PrePay 0%	Other 2%	
Other 0%	PostPay & pre-paid card 1+1%	

Norway (2017)	Argentina (2017)	Indonesia (2017)
Credit card 28%	Credit card 27%	Bank transfer 30%
Bank transfer 21%	eWallet 22%	eWallet 24%
eWallet 12%	Bank transfer 14%	Cash on delivery 17%
eInvoices 12%	Debit card 10%	Credit card 14%
Charge & deferred debit card 10%	Charge & deferred debit card 8%	Charge & deferred debit card 7%
Debit card 9%	Cash on delivery 8%	Debit card 7%
Other 5%	PostPay 7%	PrePay 1%
Cash on delivery 4%	PrePay & pre-paid card 2+2%	
	Other 0%	

Malaysia (2017)	Poland (2017)	Sweden (2017)
Bank transfer 45%	Bank transfer 41%	Debit card 30%
Credit card 20%	eWallet 17%	Bank transfer 21%
Debit card 11%	Debit card 16%	eInvoices 20%
Cash on delivery 9%	Cash on delivery 12%	Credit card 12%
eWallet 7%	Credit card 7%	Charge & deferred debit card 9%
Charge & deferred debit card 6%	Charge & deferred debit card 6%	eWallet 7%
PrePay 1%	eInvoices 1%	Other 2%
Pre-paid card 1%		

All data from Worldpay, 2018, Global Payments Report. Numbers adjusted for rounding may impact totals.

Today's modern traveler

74%

66%

36%

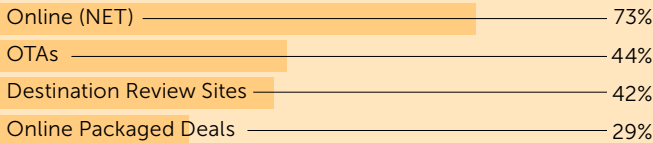
of global travelers prefer to book their travel via a digital device (computer, laptop or mobile phone).

of respondents find a lack of transparent pricing annoying.

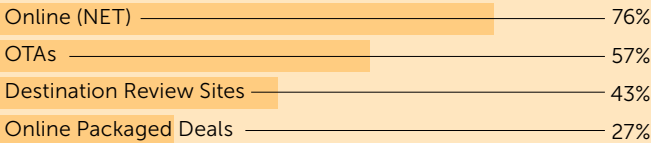
feel frustrated if they can't pay via their preferred method.

Most common forms of booking travel plans in 2017

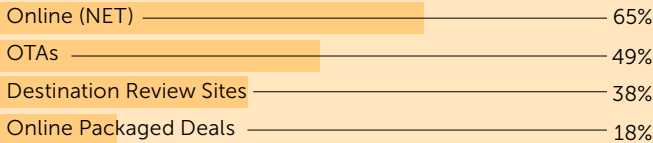
Gen Z



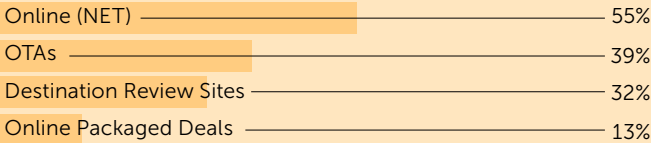
Millennials



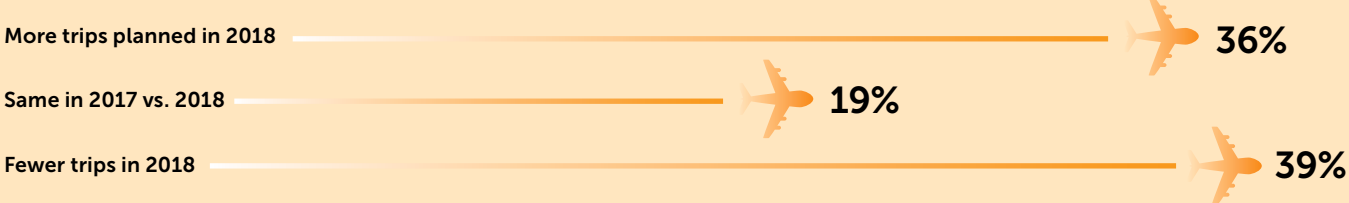
Gen X



Boomers

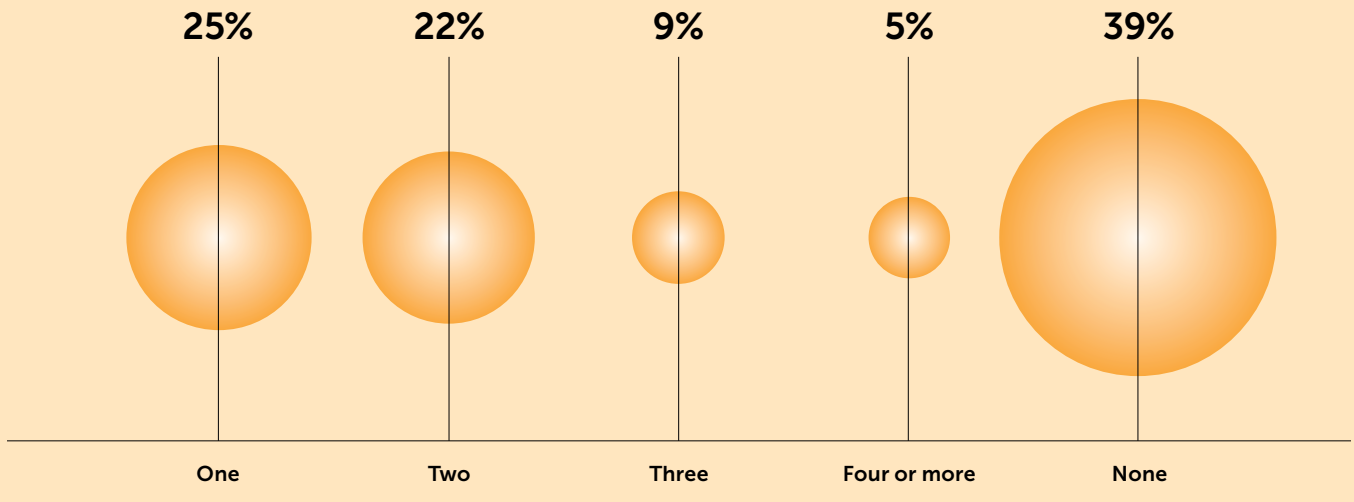


Frequency of travelers' planned trips from 2017-2018

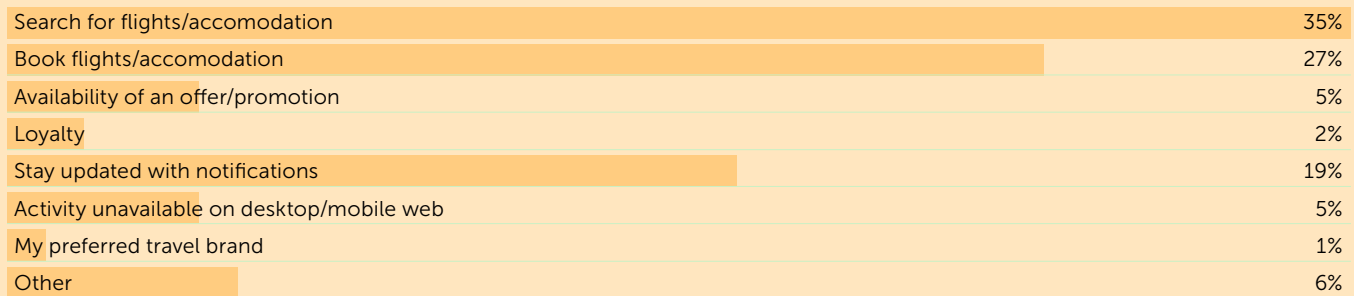


Source: Mastercard/WEX, 2018

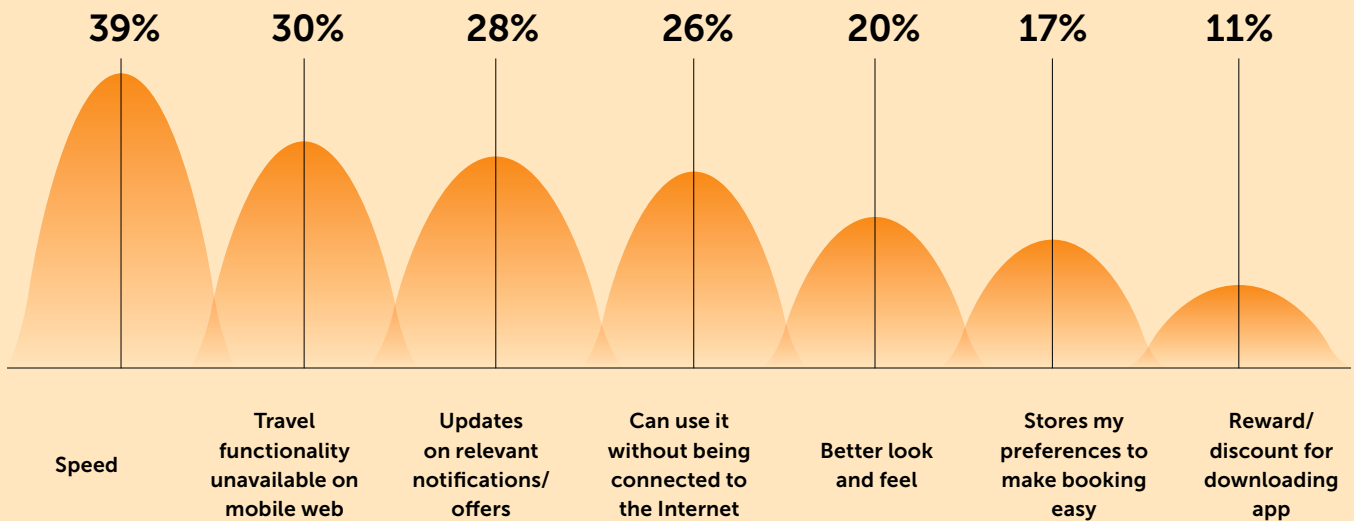
How many airline apps do you currently have installed on your smartphone



Which of the following best describes your reasons for downloading a travel app to your smartphone?



Why would you download a travel app and not just use a mobile site?



Speed vs. security: no longer a trade-off

Is your organization chasing user experience at security's expense?

03

Countless organizational decisions involve tension. Yet few carry quite the potential risk or reward as the tension between user experience and security. Almost paradoxical in nature, making progress on the one hand can often result in a step back on the other.

For businesses in the travel and aviation industry, finding an appropriate balance between experience and security is especially crucial given the competitive landscape, and new types of payments may provide one of the pieces in the puzzle.

How did we get here?

Leaders in the travel and aviation sector, much like many other industries, are at the mercy of these two opposing forces. Both have strong commercial drivers, but present potentially different outcomes.

On the one hand, user experience rules supreme. In the age of Uber and Amazon, all businesses are striving to create 'best-in-class', slick, and seamless digital customer journeys without a hint of friction. Conversion is king – removing any barriers or ob-

stacles to a customer progressing from intent to action, completing their transaction without leaving a digital shopping basket full of promise. In the face of frankly dismal conversion rates – pegged between 0.7% and 4.2% for the travel sector, according to industry analysis – even the most marginal of gains can yield a strong and compelling commercial outcome. A speedy booking experience, therefore, has become the holy grail in today's crowded marketplace.

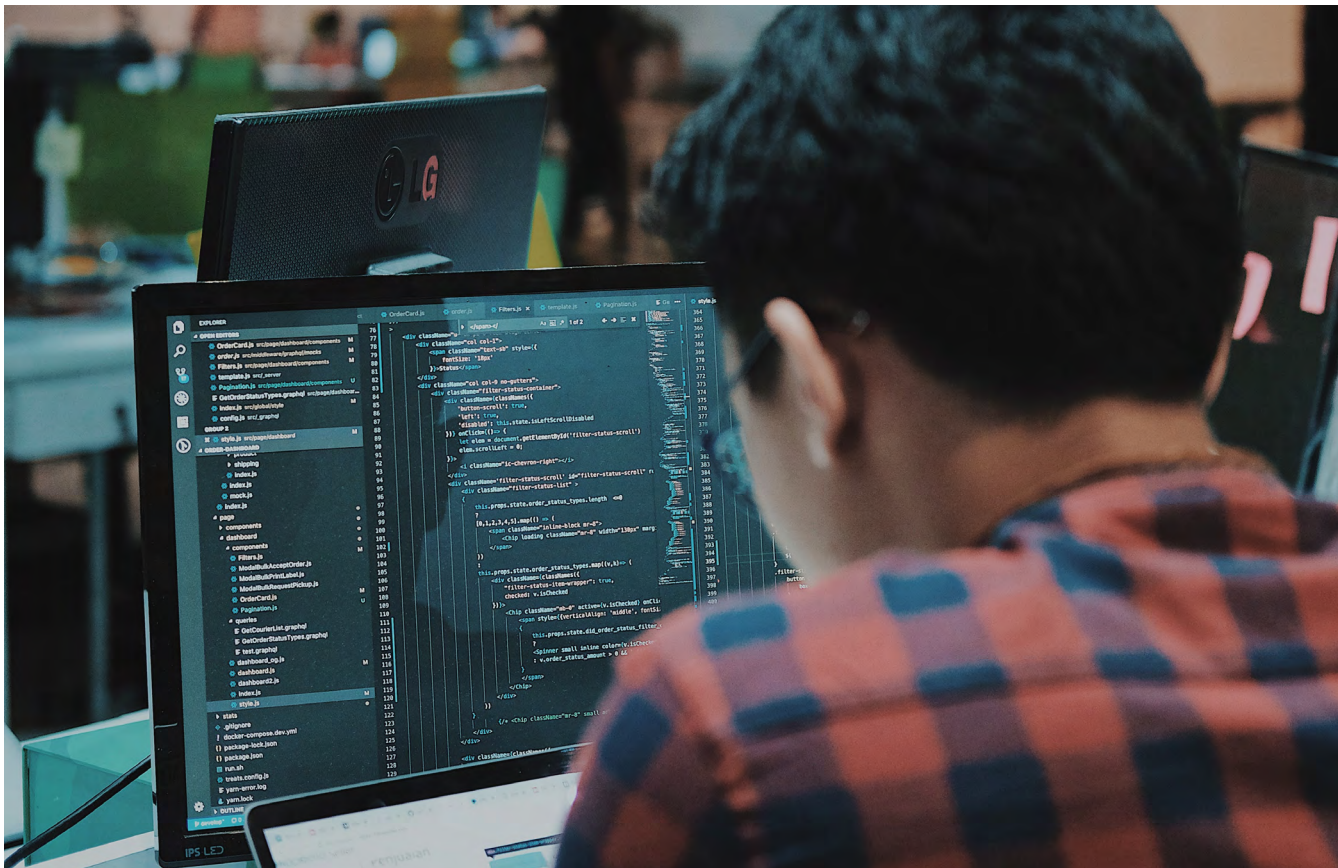
Moreover, consumer experiences aren't just built on speed and ease of use. The new battleground for the customer wallet hinges on relevance – with personalization at its heart. According to Google, "if a travel brand tailored its information and overall trip experience based on personal preferences or past behavior, 76% of US travelers would be likely or extremely likely to sign up for the brand's loyalty program, and 36% would pay more for more tailored information and experiences."

Consequently, merchants in the travel and aviation sector are hungry for data, keen to build ever-richer troves of personal information which, when combined with

the latent potential of machine learning, can deliver truly personalized experiences and propositions. Commercially, the rationale is clear: more data can yield greater relevance, which in turn can be harnessed to bolster both customer acquisition and retention. The downside? Travel and aviation organizations now find themselves the guardians of one of the fullest pictures of a consumer's life, second only to their bank. An attractive target, therefore, for criminal actors.

Which brings us to the counterforce: security. Its commercial rationale is equally compelling given several recent high-profile cyber attacks and data breaches. Fraud, whether "friendly" or the more nefarious kind, can cause great reputational damage to a business.

Few – if any – organizations would dispute the imperative that any data-collector faces today. Consider the implications of a cyber attack that results in the loss of travelers' personal and card payment information. The travel and aviation sector witnessed three examples of this in the closing months of 2018 alone, involving



data of more than half a billion travelers. Incident management and compensation costs alone can reach significant levels. In addition, you need to factor in the costs of lost revenue from reputational damage, erosion of customer loyalty and customer defections. And to top it off, the potential for punitive fines from regulators which can run into the hundreds of millions.

Seamless or secure?

These two opposing forces are difficult to reconcile. Without a superior seamless booking experience, travelers will defect to competing sites, causing conversion and revenue to suffer. But increasing security and fraud prevention may lead to deploying software that could accidentally block legitimate transactions, adding friction to an otherwise seamless payment process and adversely affecting conversion.

Further complicating the matter, many businesses are organized in siloes, where conversion optimization and user experience resides with one team and security with another. Rarely do they share a common accountability or decision-making process.

The legacy systems multiplier

Compounding the tension between speed and security are the legacy technologies and systems that plague the sector, particularly prevalent among airlines and hotels.

Merchants often find themselves building great, seamless digital and mobile experiences on top of old technology designed for a different payment era.

Mike Parkinson, UK General Manager and Director of Travel, Trustly

With the potential vulnerabilities in combining new and old technology, it's important to pause in what could otherwise be a breakneck pace of development, and consider the following questions:

- Are your user experience investments outpacing your security capabilities?
- Are you fully assessing the cost of maintaining these experiences, and the risks inherent in doing so?

- What is the true cost of deploying the security measures needed to adequately mitigate risk and provide reassurance to customers, all without disrupting the payment experience?
- Does the answer lie elsewhere?

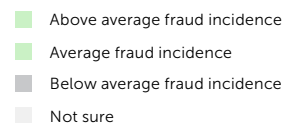
The looming authentication challenge

One of the more significant aspects of the Regulatory Technical Standards (RTS), which accompany PSD2, is the introduction of mandatory two-factor authentication.

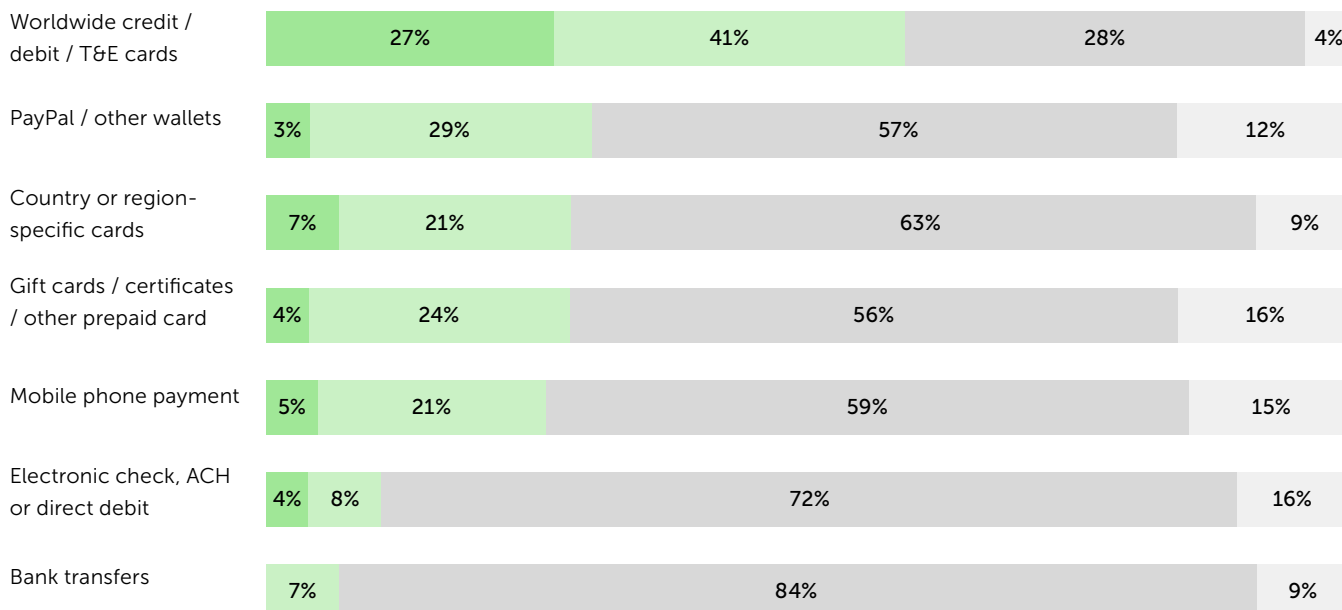
Despite a number of exemptions and exceptions, this applies to all forms of payment, including debit and credit cards, and will affect the majority of online transactions.

Regulators have set an aggressive timeline that requires implementation by September 2019. However, many acquirers and issuing banks are yet to grasp the full weight of this deadline and the scale of change it necessitates.

Share of global airlines with an average or above average incidence of fraud in 2017, by payment type



Airline bookings - fraud incidence by payment method worldwide 2017



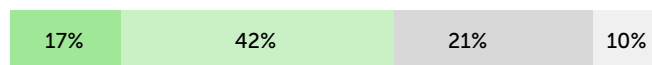
Source: CyberSource and Phocuswright, 2018 Global Airline Online Fraud Management

Across all sectors, 59% of merchants view abandoned baskets in digital commerce as a bigger concern than fraud or chargebacks

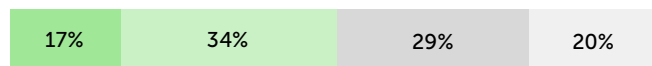
On a scale of one (strongly disagree) to four (strongly agree), please state your agreement with the following statements around fraud and data compromise



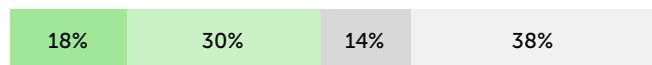
Abandoned transactions in online and mobile are a bigger concern than fraud/chargebacks.



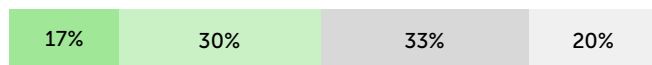
Concerns over the risk of data breach have limited our investment in the customer experience.



My organization would not invest in fraud solutions that add frictions to the customer experience.



We are happy to face an increased risk of fraud if it means sales growth.



Source: 2018 Ovum - Global Payments Insight Survey

Cast your mind back to the introduction of 3D Secure 1.0. We can all remember its tiny iframes and clunky user experience, designed for a far-less mobile world than we find ourselves in today. Unsurprisingly, many acquirers and merchants chose not to implement it for fear of disrupting the digital purchase journey and impacting conversion. Yet these new regulations re-

move such discretion. 3D Secure 2.0 – albeit designed to address its predecessor’s shortcomings – is mandatory, and implementation is looming.

Merchants who haven’t already done so need to take the conversation to their acquirers today. Here are the key questions you should be asking:

- Do you have 3D Secure 2.0 enabled?
- What does this mean for us?
- How will this manifest in the digital purchase journey?
- How will this affect conversion, and what can we do to mitigate any consequences?

- What alternatives should we consider as part of a fresh look at our payments strategy?
- What are the exemptions and how do they apply to us?

Thinking beyond the card

The security risks of card-on-file are widely recognized. But beyond the dangers of a data breach lies another significant headache for the travel and airline sector: chargebacks.

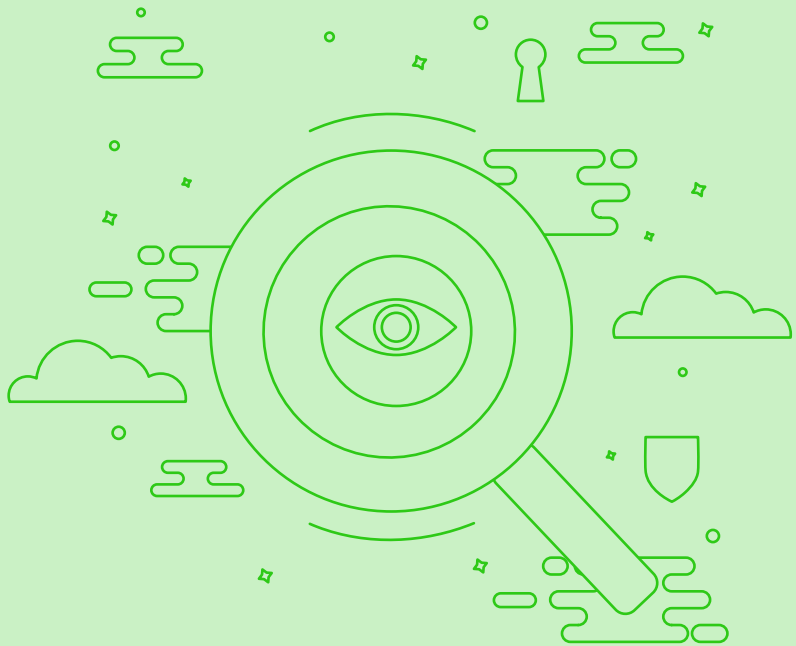
Often referred to as “friendly fraud,” chargebacks are estimated to cost merchants upwards of £8 billion a year in revenue loss. What’s more, it’s estimated that the true cost of fraud is actually £2.50 for every £1 of loss, in the administration and management of the chargeback process, making this a bottom-line relevant issue.

However, three factors have converged which present an alternative to cards: bank transfers. They are rapidly growing in popularity across a wide range of markets and offer the benefits of an irreversible transaction that cards simply cannot meet.

- Consumer appetite for alternative payment methods is booming, and only set to continue to grow at pace.
- Technology and better connectivity are enabling faster payment initiation, notification and settlement, facilitated through authentication methods that enable bank transfers to provide safer transactions without adding friction to the booking experience.
- The regulatory landscape – particularly in Europe but likely to spread further afield – is ushering in an era of open banking and greater collaboration, particularly thanks to the introduction of PSD2 and SEPA Instant.

Mitigating the risks inherent in processing and storing payment card information is a necessity for the industry, but it’s not the only solution. By responding to changing consumer behavior and offering payment alternatives that take sensitive financial information out of the equation, you can reduce both risk and cost without adversely affecting the consumer. In fact, for many it will do quite the opposite.

Hacking – travel and aviation far from immune



In late 2018, a major global airline suffered a sophisticated hack resulting in a breach of personal and payment card information of more than 250,000 travelers. In the immediate aftermath, the airline’s share price slid 3%, equivalent to a drop in market value of almost half a billion euros. Consumer sentiment towards the brand fell by 10 points compared to the prior month, according to YouGov BrandIndex (After a similar incident, UK telecoms firm TalkTalk took 10 months to recover to its previous level.)

Within weeks, a major global hotel group revealed it had been the victim of a four-year long data breach affecting an estimated half a billion guests. That ranked it as the second biggest data breach in history behind only Yahoo. Its share price plummeted by almost 7% on the news and the New York Attorney General launched an investigation.

Countless regulators around the world, including the UK’s powerful Information Commissioner’s Office, have been notified and will likely commence their own investigations.

In both instances, investors, regulators and travelers alike have been left asking: are complex IT systems to blame? Have layers and layers of different technologies and systems left data security too opaque to properly manage? Have e-commerce functionality and evermore sophisticated apps made the booking process easier, while simultaneously creating more vulnerabilities in the system?

It’s imperative that the industry take action, collectively, and embrace collaboration. The only certainty is that these two incidents won’t be the last.

PSD2 has arrived - What are you waiting for?

One year into the most sweeping regulatory reforms to the payments industry, how much has really changed for consumers and merchants? Has complexity surrounding this new legislation made merchants more apprehensive about how they should try to capitalize on the opportunities PSD2 presents?

04

A game-changer. A paradigm shift. A revolutionizing force set to accelerate industry disruption. But one year in from PSD2 coming into effect, can we really say that the payments ecosystem has actually been revolutionized for consumers and merchants alike? Have the transformational new initiatives, partnerships and technologies truly delivered change? Or have many existing and aspiring payments providers recognized the complexity of the full implementation of PSD2 and are waiting on banks to do the hard work for them?

Regulation vs. reality

January celebrations rang in more than just the start of the new year; they also brought the beginning of the largest structural change to the European payments landscape: PSD2. PSD2 has been the culmination of years of discussions and debates on how to introduce more competition into the industry, with a primary focus on allowing third-party access to banks' data and functionality. The starting gun went off on January 13, 2018, when PSD2 was transposed into national laws throughout

EU member nations. However, while the legal foundation has been laid, there are still some elements yet to come into effect that are limiting the full implementation of this game-changing legislation.

PSD2 is a great enabler for bank payments, explicitly allowing TPPs such as Trustly to provide safe and secure payments for merchants and their consumers.

Sara Berg, Chief Operating Officer, Trustly

RTS, SCA, CSC. These are three acronyms that you'll have come across if you've read any articles on PSD2 - and they're the most important ones you need to know if you're looking to capitalize on the opportunities this legislation presents. Regulatory technical standards (RTS) are the implementation requirements for third-party providers (TPPs) and banks to adhere to in order to comply with PSD2. While the deadline for PSD2 was January 2018, RTS will

only come into effect 18 months later in September 2019.

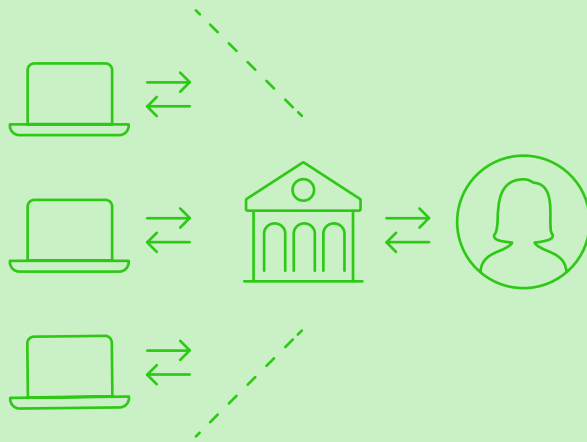
Two areas that RTS covers are:

- Security: SCA - strong customer authentication
- Communication: CSC - common secure communication

The principle of SCA is to make sure that consumers are protected when making online payments through mandatory two-factor authentication, whether they're card transactions or bank transfers. As mentioned previously, this is more of a headache for those in the card ecosystem where two-factor authentication was optional; this has been common practice for online banking for years.

The requirements regarding CSC regulates how TPPs access consumers' bank accounts and the consent from the consumer that is required to do so. Banks can either provide a dedicated API or direct access (secure screen scraping), or both. However, banks aren't compelled to develop an API; they just need to allow third-party access.

What is PSD2?



The Second Payment Services Directive (PSD2) is an EU Directive that took effect in January 2018 and governs both payment services and payment service providers. As part of the trends towards open banking and the growth of fintech start-ups around the world, PSD2 is designed to create a level playing field for all involved, while also making payments safer and increasing consumers' protection. It aims to encourage new entrants to the sector outside of mainstream banks and payment providers and

to enable direct bank payments, by requiring banks to open access to their application programming interfaces (APIs) to third parties, and adhere to minimum standards. Ultimately, it will give consumers more control and more choice over how they pay for goods and services online, and who they choose to access and manage their finances. And, through mandatory two-factor authentication, it will dramatically reduce card fraud to both the benefit of the consumer, and merchants subject to loss.

To add more complexity, should banks want to stop direct access for TPPs, they will need to prove to their local regulator that their APIs meet the qualifying criteria and have been thoroughly tested in the market. Finally, should the API go down for some reason, banks need to allow redundancy access i.e. direct access.

PSD2 for merchants feels analogous to Brexit. You know you have to prepare, but you're not quite sure what for.

Thomas Heldorff, Vice President, Airlines and Travel, Worldpay

The advent of PSD2 in January this year was heralded as a new dawn in payments - and it has been. Getting the legal framework and guiding principles transposed into law across all EU member states was a monumental achievement. However, the 18-month delayed implementation of RTS means business as usual until September for many in the industry, especially existing players that have been afforded transitional status. There is still a lot of potential to be unlocked, but it wouldn't go amiss to acknowledge complexity involved with the full implementation of PSD2 and the few unknowns left to be resolved. Bring on September.

Not all bank payments are created equal

Enhancing bank payments, payment initiation services (PIS) in PSD2 terminology, is a key tenet of PSD2. It offers the potential for reduced costs, improved operational efficiencies, and a reduction in the number of technology partners by peeling back layers of distribution for merchants, all the while providing a more secure payment flow with better consumer protection. But taking into account the delayed implementation of RTS, should we expect an immediate surge in PIS come September?

Before assessing the technical implications of RTS, especially CSC, on bank payments, it's worth taking a step back to understand how the bank payments fit into the wider payments ecosystem.

At present, bank payments are a heterogeneous experience, driven primarily by the differing authentication methods across banks and countries, as well as payment infrastructure through which the payments are made. While some may use biometrics such as fingerprint, voice or face, others may require a token, card reader or even a physical scratch card. When it comes to the legacy systems and the technology capabilities underpinning them, it is just as inconsistent. Not only do the national clearing and settlement systems vary between countries, but also banks' own systems executing these transactions differ, affecting the speed and risk of transactions.

"Payments are hugely complex, but over the years we've been working across a multitude of banks in Europe to simplify the payments experience, making it more consistent for merchants in the travel and aviation sector."

Mike Parkinson, UK General Manager and Director of Travel, Trustly

This results in an inconsistent user experience, and the risk of lowering conversion. Equally importantly, these differences provide a bit of headache for merchants



wanting to accept bank payments in relation to cash flow and settlement risks, all of which can leave an airline, hotel or OTA deterred from exploring it in their payments mix. Those merchant risks, in particular, have added weight considering the multitude of recent bankruptcies in the airline industry in Europe.

With card payments, it is estimated that for

every £1 that is disputed, merchants spend an additional £1.50 on fees and expenses related to resolving these disputes. While bank payments don't suffer from these exceptionally high chargeback rates and costs, there are some inherent risks that merchants need to be aware of, albeit the scale of them are significantly lower and can more easily be mitigated.

The success of card transactions for merchants is measured by the acceptance rate that acquirers can provide. Once authorized, the funds are guaranteed to be transferred at some point, although not immediately. For bank payments, it's the reverse. There's no risk of declines due to the secure nature of two-factor authentication, and so they can be seen as having a perfect acceptance rate. However,

depending on banks' infrastructure and systems, these can settle into merchants' bank accounts with varying speed and probability - sometimes these can be instant and almost always settle. Legacy systems, where payments can just "get lost," and extra AML checks required for bank payments that can block or slow down transactions, mean that the risk of unsettled transactions can't be disregarded, especially in an industry that expects guaranteed funds when issuing tickets last minute.

This highlights the problem with initiation-only providers of bank payments. Without the provider monitoring the actual settlement of these funds and instead just focusing on allowing the consumer to push the payment to the merchant's bank account, the onus is on the merchants and their partners to do it themselves or risk allowing consumers to travel for free. Being in the flow of funds mitigates these problems, yet few bank payments providers are willing to invest the time and effort in order to provide a solution that is well-suited to the travel and aviation sector.

Building out a full service payment initiation service, where you're in the flow of funds from initiation to settlement to reconciliation, isn't something you can do overnight; it's something we've spent the past decade building and perfecting with thousands of banks and merchants.

Mike Parkinson, UK General Manager and Director of Travel, Trustly

So, while there are some challenges for merchants and their partners in providing bank payments, there are clearly certain models of PIS in its current form that can solve these issues today.

Are banks ready for the API revolution?

And this finally leads us to RTS: will these new bank APIs somehow solve the complexity for merchants that want to accept

bank transfers and consumers who want more choice in how they pay?

It's well-understood that RTS is instrumental in unlocking the true potential of PSD2. However, while PSD2 sets out the general legal framework and principles and RTS sets out the legal technical requirements to implement them, they don't necessarily define the specific operational and practical elements of how banks and TPPs will work together. This was deliberate. The European authorities responsible for PSD2 did not want to stifle innovation or competition by prescribing detailed technical instructions, but instead wanted the market to come up with its own interpretations of the law that could benefit both merchants and consumers.

This has led to the proliferation of groups that you've heard of such as the Berlin Group, Open Banking in the UK and STET in France, which are mainly, but not exclusively, national initiatives. These initiatives are focused on defining every element of the payment flow from how consumers will consent to third-party access to their bank account to the technical messaging formats used to the actual user experience; essentially instructions for building PSD2 services for TPPs and banks.

So, heterogeneity in bank payments is here to stay while governed by the same overarching framework. But, are banks' APIs ready for the new PSD2 world? Will they not only be compliant but also provide the new way to pay?

Much has been talked about the API economy and the opportunities PSD2 offers. However, if banks aren't able to offer the full functionality that fintechs and start-ups have built their business models upon by September, it would seem like a lot would remain the same. On reflection of the first year of PSD2, Imran Gulamhuseinwala, trustee of the Open Banking Implementation Entity (OBIE) in the UK, sums up how the challenges of creating compliant APIs are affecting what can be delivered to the market. He notes that initially, the regulation was treated as "a typical compliance exercise championed only by a handful of fintechs", but that 2019 holds a lot of promise as "banks have very firmly moved from

viewing open banking as a compliance exercise to an opportunity to compete and innovate."

Yet, some warn of the scale of the task and banks are still grappling with how to capitalize on PSD2. Shahrokh Moinian, Global Head of Cash Products and Cash Management at Deutsche Bank noted that "many banks are yet to envisage how PSD2 can be transformed from a compliance burden to a business opportunity." Furthermore, there is some uncertainty as to how these initiatives will work together in reshaping the payments landscape, warning that "providing access to accounts in a disorganized or incongruent manner could endanger PSD2's opportunities for the entire market."

Despite these challenges, it is clear that banks are moving in the right direction and gathering speed, looking to be enablers rather than prohibitors. But the technology upgrades required to provide these enhanced connections, and effectively compete with new digital challenger banks built on state-of-the-art infrastructure such as Starling, N26 and Monzo, to name a few, should not be underestimated. Although the deadline for RTS implementation in September seems far away, banks that want to offer their own APIs need to have them ready for testing by March. Time isn't on their side.

Why play the waiting game?

While 2018 was filled with announcements of services and partnerships that were merely exploring how to take advantage of PSD2 and its full implementation through RTS, merchants and their consumers need not wait until September 2019 to start realizing these benefits. RTS will eventually, of course, bring about an enhanced payment flow in terms of user experience and security through official PSD2 APIs but certain existing bank transfer providers are already providing a great payment flow that is fully PSD2 compliant. As the travel and aviation sector is striving to lead in online payments, it's imperative you find an experienced provider you can partner with to navigate through the maze of payments and win the battle for the consumer. What are you waiting for?

Trustly viewpoint

PSD2 is a response to an opaque, complex and anti-competitive payments ecosystem. It goes further than many previous attempts to level the playing field and truly reshape the payments landscape – for the security and economic benefits of both consumers and businesses alike.

Yet in practice, the early response from banks, fintech players and others in the industry has been limited. While the regulations set the ground rules and provide much needed definition of the players in the world of payments, the reality is a complex and a slow-moving process.

At its core, PSD2 provisions for two different payment services – Account Information Services (AIS) and Payment Initiation Services (PIS). The former enables consumers to consolidate their accounts from different providers, view and manage their money and finances across different institutions and aggregate data to build a fuller picture of their financial lives. The latter allows for a host of new, lower-cost, faster and more secure ways to pay for goods and services online.

If we look at the early releases of apps and APIs from financial institutions and fintechs, or read the media commentary and buzz from our industry, the majority of today's focus is on AIS. And while AIS can undoubtedly offer consumers valuable insights or simply a time-saving on daily banking tasks, PIS represents an even greater opportunity

to create tangible value for merchants and consumers. Just think about how often you check your bank account online, versus how often you pay for something online. The latter offers far greater potential yet seems to be lagging behind the basic account information tools beginning to be rolled out by various players.

At Trustly, we caught the proverbial wave long before today's regulatory reforms were even in first draft. We've spent a decade reimagining payments and creating our proprietary banking network to enable real-time bank payments in Europe, with industry-leading coverage across a multitude of banks. All delivered through one consistent partner with an experience designed to optimize, rather than disrupt, the purchase experience and conversion. And we've not been pushing innovation for innovation's sake. We saw the shifting sands of consumer behavior, technological and connectivity advances, and regulatory reform ahead of time, and responded by creating a platform to meet the traveler where they'd be tomorrow, not where they were yesterday. And in doing so, we have amassed an almost unmatched depth of experience of the realities of execution. So much so, that we're already processing bank transfer payments for multiple airlines and several OTAs, with many more eager to remain one step ahead of their competition.

If you want proof that bank transfers can thrive with the right conditions, look no further than the Netherlands.

The iDEAL payments system, established by the country's leading banks more than a decade ago, has become the predominant payment method by a country mile. Today, more than 6 in every 10 online transactions are processed securely through the iDEAL system, far outstripping debit and credit card payments. Consumers benefit, as do merchants. It's the strongest evidence yet of the potential in bank transfers when the right infrastructure and legislation is in place.

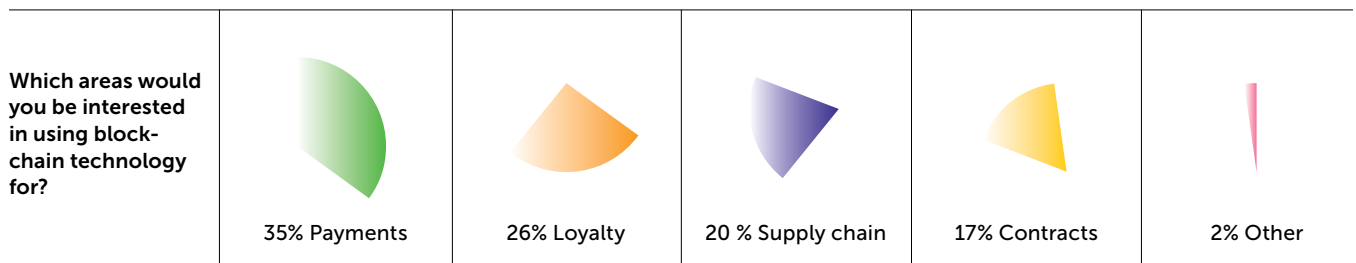
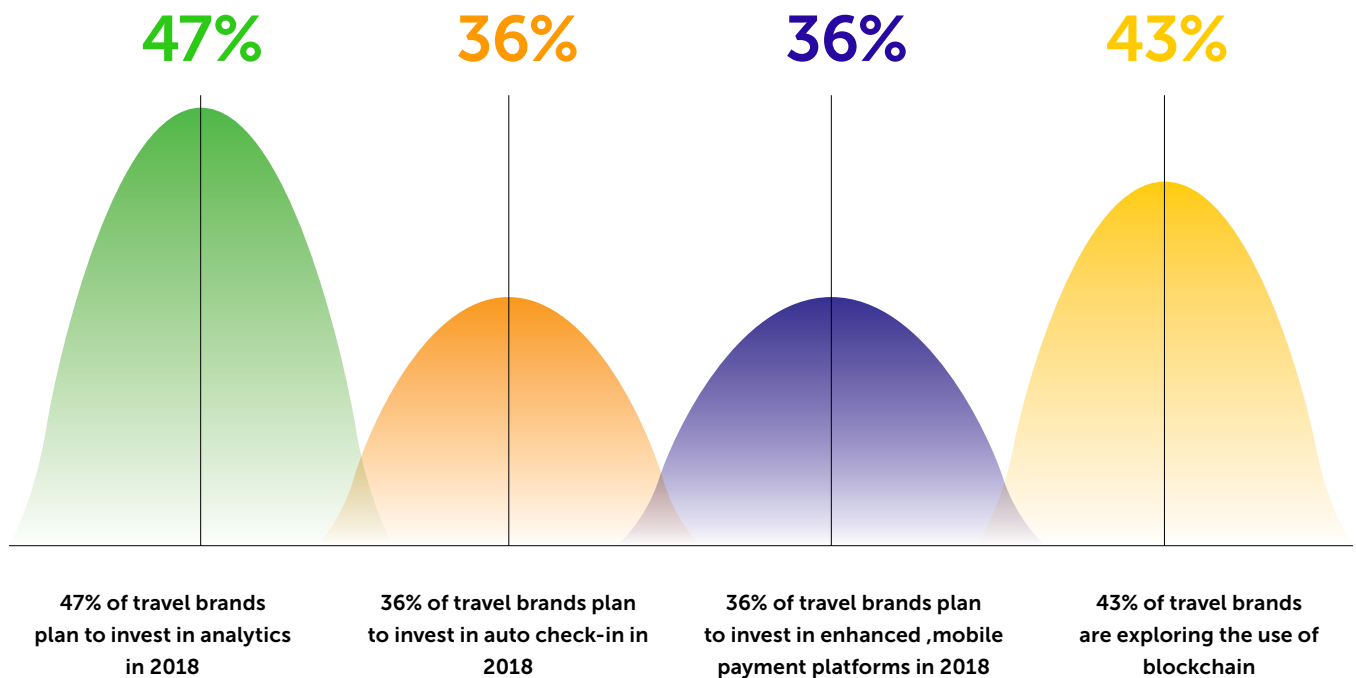
The commercial arguments behind bank transfers are clear. The security arguments are clear. The consumer demand is evidenced in its growth trajectory. And the regulatory framework is now in place. It's time for the merchants to be put back in control. PSD2 is the framework that could give the travel industry the push into the future by implementing the next generation payment method.

The clock on PSD2's full implementation timetable is ticking and those that are slow to embrace change will be left behind.



Sara Berg, Chief Operating Officer, Trustly

Areas of greatest investment for travel merchants in 2018



How can airlines capitalize on the mobile-first generation?

In 2018 what areas of mobile development do you intend to invest in?

Business intelligence/analytics	47%
Chatbots	39%
Auto check-in	36%
Enhanced mobile payment platforms	36%
Voice technology	31%
PWAs	28%
Chat with representative	17%
Blockchain	17%
Virtual reality	8%
Augmented reality	3%

What mobile goals are important to your organization in 2018?

Customer service	62%
Revenue generation	53%
Customer engagement & acquisition	48%
Owning the entire customer journey	47%
Cost savings/operational benefits	44%
Innovation/mobile first	35%

Are you ready to think differently?

Bank transfers present a compelling commercial opportunity, but require a combination of superior experience, consumer education and creativity to be realized.



Among the myriad alternative payment methods available today, let alone those that will emerge tomorrow, bank transfers are set to take center stage, alongside e-wallets such as Apple Pay, AliPay and WeChat Pay.

All around the world, consumers are seeing the benefits of a more secure way to pay for travel. A method that feels as natural as the card transactions they've grown up with, but one that doesn't compromise their identity and privacy.

The benefits for the travel and aviation sector are clear, and present a compelling commercial opportunity. To name a few:

- Reduced processing costs, particularly pertinent given the potentially high average transaction values common in the likes of business class flights and family holidays
- Immediate settlement that removes cashflow lag and uncertainty
- Improved operational efficiency, making cross-border transactions simpler and reducing the cost and complexity (while increasing acceptance) of

managing payments in multiple markets and currencies

- Incremental reach among consumers without access to credit or debit cards, or a preference not to use them
- The elimination of chargebacks and so-called "friendly-fraud," and the associated cost and resource burdens required to administer them

But to fully capitalize on these opportunities requires more than the introduction of a new payment option alone.

It calls for creative thought to motivate consumers to change the habit of a lifetime. For decades, they've paid by credit or debit card without a second thought, or even the awareness that a better and safer way now exists. You can do so by offering tangible value to overcome customer objection or inertia.

If a traveler opts for a credit card to spread the cost of paying for a trip, could installments by bank transfer provide a convenient, flexible and affordable alternative? If it's possible for a sofa or a fridge, why not a flight?

If a traveler chooses credit cards to benefit from additional air miles or loyalty points, could bank transfers be reimagined and given their own equivalent perks?

If security and privacy alone won't motivate a traveler to break with their payment norms, would value-added services such as a welcome drink on arrival at their hotel, or speedier boarding on a flight, both motivate the change as well as adding a "wow" to the customer experience?

As I opined earlier in this report, a superior payment experience and consumer education are essential ingredients to make APMs a success for your business.

Add in a little creativity, with a proven partner you can trust, and you've got the perfect recipe.

Mike Parkinson, UK General Manager and Director of Travel, Trustly

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