RETAIL BANKING SECTOR INQUIRY
PRELIMINARY REPORT II
CONSULTATION FEEDBACK FORM

Name of organisation: Italian Banking Association (ABI)

Type of organisation: banking association

Address: Piazza del Gesù 49 – 00186 Rome

Country: Italy

Have you received a request for information as part of the sector inquiry:

☐ Yes

☑ No

Specific questions from Executive Summary:

A. Market structure and fragmentation

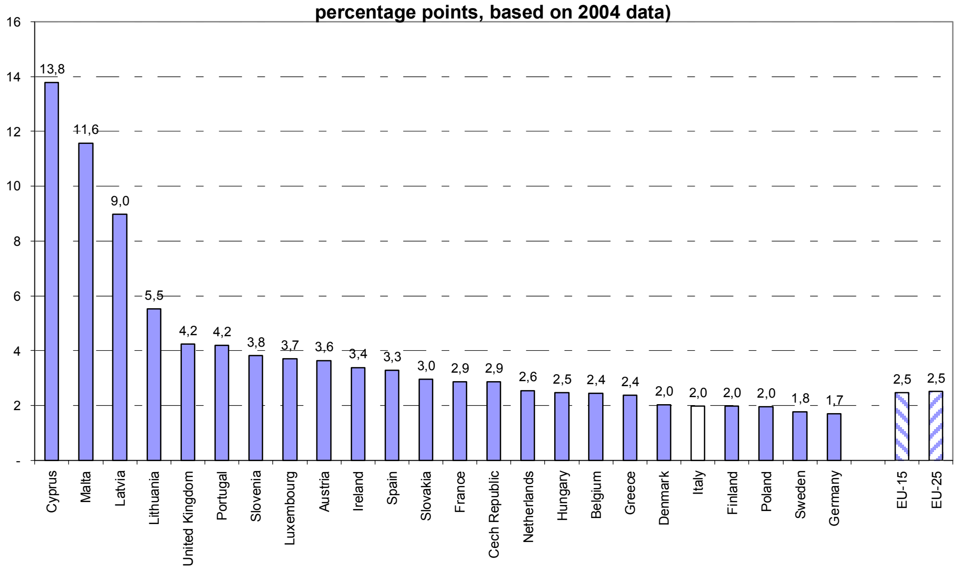
1. What are the main reasons for market fragmentation in Europe's retail banking sector? Please identify whether they are mainly of regulatory, structural or behavioural nature.

In Italy the discussion on the relationship between banking sector regulations and barriers to competition has recently focused on secondary legislation which – transposing Article 16 of Directive 2000/12/EC – instituted the requirement of prior notification to the Bank of Italy of the acquisition of significant holdings entailing control of a bank of a banking group holding company, so that the Bank of Italy could "consider the possible existence of impediments to the transaction."
The requirement for prior notification – essentially a sort of moral suasion that reinforced the Bank of Italy's supervisory action – has now been removed from the law. This is a significant change, enhancing transparency and broadening the scope for free business choices and market forces.
More transparency and legal certainty may be added to the supervisory authorisation process as a result of the revision of Art. 19 and 129 of EU Directive 48/2005, currently under discussion in the ECON Committee of the European Parliament.

From a corporate viewpoint, the Commission may devote its attention to individual legal structures the use of which is common in individual Member States, where such structures constitute actual hindrances to M&A transactions, particularly in a cross-border context (see, in particular, public banks in Germany).*

*With reference to structural issues, the DG for Competition has estimated an overall income in the EU25 generated by the retail banking sector of between 250 and 275 billion € (in 2004). Italy stands at between 25 and 30 billion €, a figure identical to that of Spain, but lower than Germany (35-45 billion), France (45-50 billion) and the UK (45-55 billion). Based on the ratio of total income generated by the retail banking sector in the EU countries to the nominal GDP, the situation is as described below in diagram 1. Italy – with a ratio of about 2% - ranks among the countries with the lowest retail banking to overall GDP ratio; the EU15 and EU25 average, in fact, is 2.5%, half a percentage point higher than the Italian figure. Among the principal competing countries only Germany ranks behind Italy, with a ratio of 1.7%, while France (2.9%), Spain (3.3%) and the UK (4.2%) all feature much higher figures. With reference to the profitability measure considered by the DG Competition, the ratio of pre-tax profits to banks' assets generated by retail banking activity, we can see that in EU15 countries, but also in EU25, we had an increasing trend: the measure utilised raised from about 23% in 2002 to almost 29%. The profitability in Italy was at the same level of the European average only in 2002, while in 2003 and in 2004 it showed a gap (a lower value) of about 5-6 percentage points (in comparison with the cluster of countries with a higher profitability level, namely Ireland, Spain, Finland, Sweden, Denmark and UK, Italian level shows a higher gap).
On the contrary, the cost income measure, represented by the ratio of operative costs to total revenues generated by the retail banking activity, results higher in Italy than EU15 average both in 2003 and in 2004.*

Diagram 1 – Gross income to GDP ratio in the retail banking sector in the EU25 countries (figures are in percentage points, based on 2004 data)



Source: EU Commission and Thomson Financial Datastream data processed by the ABI Study & Research Centre.

These results reveal that Italian banks do not impose overly costly economic conditions to their retail clients. It is important to underline that the structural issues are strongly influenced by the behaviour of consumers and SME among European countries. In particular, multi-banking, joint accounts, use profiles of payment services (for example in Italy the use of *cheques and cash is very diffused) and financial services (for example in Italy there is a low degree of use of loans by consumers), the different number of very small entrepreneurs and, as consequence, the different level of credit risk among European countries, and the cultural differences in the knowledge of financial markets are all factors that produce an intense degree of fragmentation in the retail banking market.*

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2. What are the main causes and implications of the different level of concentration in the EU retail banking markets?

One of the main causes of the different level of concentration in the EU retail banking markets is the different presence of public ownership in the European banking system.
The concentration process in Italy is quite recent and still in progress. We can observe that until 1993 about 72% of banks' total assets was controlled by the State and this share was higher in comparison to the other main European countries. In 2004, this rate was about 1%, a level well below the other countries.
After privatization, in the last fifteen years about 629 M&A deals were concluded, which involved about 66% of banks' total assets.
Concentration in the Italian banking system is continuing as evidenced by the last important deal announced in August, namely the merger between Banca Intesa and San Paolo IMI.

B. Banks' financial performance and pricing

3. What are the main reasons for the varying rates of profitability and income in retail banking across the Member States?

As showed in the report, the income from personal bank accounts in Italy averages € 204 per consumer (ranking second – in absolute terms – after Luxembourg), compared to the EU15 and EU25 averages of 133 and 119 euros, respectively. The report also highlights that this figure should be interpreted with caution, because it is affected and characterised by a number of different practices. Following is an overview of the principal critical aspects:
1. The figure in question does not represent the cost per customer because the Commission has surveyed the income generated by the bank, which is significantly affected by the number of services rendered and loans paid out. On the contrary, the cost per customer is the result of a combination of many factors, the principal ones being: yield on deposits (not included in this survey), multi-banking, joint accounts (a typically Italian practice) and use profiles.
2. the figure does not express the profitability of each product line, because the related costs cannot be isolated. This means that a higher income per account does not necessarily translate into higher profits for the banks because bank account services differ considerably from country to country: some include very developed services, such as online banking services, others, as in the Italian case, provide a larger proportion of conventional services, such as personal cheque and cash management services (in Italy, cash transactions account for 90% of overall transactions, while in the major European countries this percentage barely reaches 70%);
3. the income generated by each account is distorted by the practices of multi-banking and joint accounts. With respect to the latter, the DG for Competition itself underlines how Italy

features the lowest number of current accounts per capita in the EU15 (precisely, 0.63 accounts per person, this figure is practically the same as the one reported in the research commissioned by ABI to Mercer Oliver Wyman). The report also mentions that the practice of joint accounts too is more widespread in Italy, suggesting that the effective cost of a current account, for Italian consumers, may be lower than the 'per customer' average of € 204 mentioned above (see page 68 of the report in question);

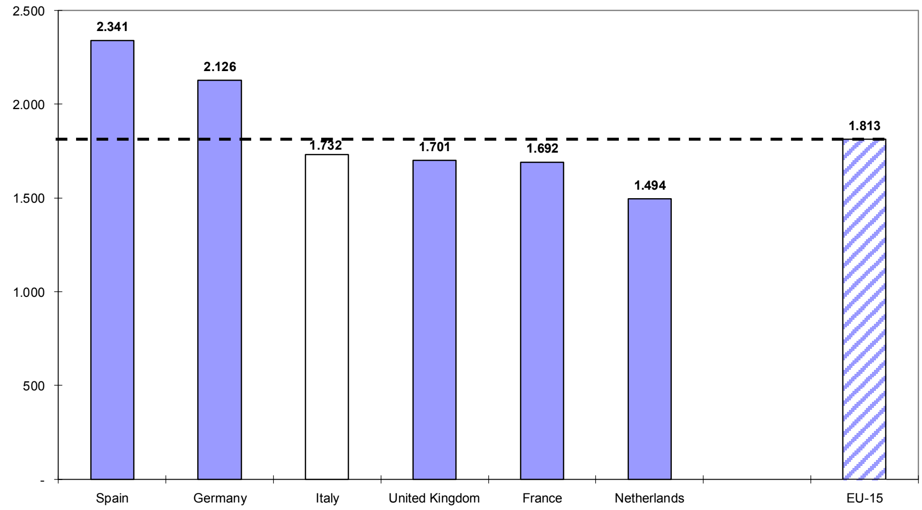
4. the income figure also includes the interest yielded by the product in question, i.e. loans tied in with current accounts (overdrafts). Because this form of loan is particularly widespread in Italy, the income from current accounts per consumer is higher than the European average. Please note that, considering the total loans to households equal to 100, the proportion of overdrafts is 37% in Italy, while the average in the Euro area is only 18%.

Moreover, income from savings deposits stands at € 67 per consumer, in line with both the EU15 and the EU25 averages of € 69 and € 64, respectively; income from consumer credit per consumer, in Italy, ranks among the lowest in the sample, standing at € 337 (€ 421 euros in the EU15 and € 367 in the EU25); income from mortgages per consumer is € 1,083, compared to the average of 1,126 euros in the EU15 (€ 1,015 in the EU25); income from credit cards per consumer is € 41 in Italy, much lower than in the average of both the EU15 (€ 64) and the EU25 (€ 65).

Assuming that a consumer uses all 5 types of products listed above, the average income generated in Italy from such a customer would be € 1,732, compared to € 1,813 of the EU15 average (€ 2,341 in Spain, € 2,126 in Germany, € 1,701 in the UK, € 1,692 in France and € 1,494 in the Netherlands - see diagram 2).

In conclusion, the behavioural factors represent one of the main reason of varying rates of profitability and income in retail banking across the Member States and they represent different banking business models. The ranking based on the average income generated by a consumer using all the product lines available in the retail banking sector is very different from the one based only on income from current account analysed in the report which gives a partial and limited view of the European retail banking business.

Diagram 2 – Average income generated by a consumer using all the product lines available in the retail banking sector in the major European countries (figures are in euros)



Source: EU Commission data processed by ABI Study & Research Centre (Tab. 19 on page 69, sum of columns 2-6).

C. Entry barriers in retail banking

4. Are there other types of entry barriers in retail banking that have not been identified in the preliminary report?

A specific focus by the Commission should be devoted to lifting entry barriers of a legal nature. Reference is made, in particular, to the lack of harmonisation in community legislation (and, hence, in the respective national legislation of EU Member States) in fields such as that of consumer protection. The cost of compliance to of the relevant mandatory legislation is so high for market operators that it discourages cross-border offer of retail products. Increasing the current level of harmonisation would significantly contribute to erasing the barriers in question or at least minimising their anti-competitive impact on the relevant market. Along the same lines, Member States should be particularly careful in avoiding goldplating, which can amount to a legal barrier when it becomes a factor that carries an adverse impact on harmonisation.

Moreover, a harmonization of the taxable base among European regimes remains a fundamental condition in order to assure the realization of an European wide market.

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5. Where and how does competition law have a role in tackling barriers to entry in retail banking?

Harmonisation at community level is a fundamental pre-requisite for the functioning of a single European market for payments and for the creation of a cross-border competition environment. In this regard, a strong cooperation between the Commission and the EPC, the dedicated forum for the pursuing an integrated payment system, is most necessary.

If, notwithstanding the achievement of an European level playing field, a number of structural and behavioral barriers to entry still exist at national level, competition law may play an important role. With reference to structural barriers, national authorities should conduct sector enquiries and release non-binding position papers in order to focus the competition issues to be tackled mainly at regulatory level.

Only when such actions do not effectively solve the antitrust concerns and thus it cannot be excluded that the lack of competition is a result of behavioral barriers achieved by market players through collusive agreements, concerted practices or abusive conducts, then the exercise of enforcement powers (i.e. starting an investigation under artt. 81/82 of the EC Treaty and/or corresponding national provisions) seems appropriate.

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6. Access to credit databases and payment infrastructures are sometimes cited as a barrier to entry in retail banking markets. Are there significant barriers to access which merit further investigation?

In Italy all the banks have access to credit databases.
Access to credit databases may constitute a barrier to entry where market operators are inhibited access to the necessary information on non-resident clients and are therefore prevented from assessing the relevant risk. Generalised access to credit databases on a non-discriminatory basis throughout the EU should constitute a viable remedy to lifting any such barrier.

As to payment infrastructures, in Italy, the collection and payment services and the related inter-bank procedures are offered to customers by banks participating in the SITRAD system (System for the transmission of data), which is managed by CIPA1 and ABI (Italian Banking Association), and in the national clearing and settlement infrastructure (BI-COMP), which is managed by the National Central Bank. In this respect, it may be noted that there is no regulatory or infrastructural constraint that is likely to limit or prevent the participation of any EU bank to the aforementioned inter-bank procedures or even their use for the execution of transactions originating from other EU/EEA countries.
The members (direct or indirect) in at least one of the inter-bank procedure in the SITRAD system are around 800 banks. The participation of small banks, which are either not able or find it uneconomical to interact directly with the system from a technical and operational perspective, is possible thanks to the indirect participation status envisaged by the system's rules.
Moreover, access rules to clearing and settlement infrastructures limit participation to supervised entities in view of reducing the risks originated by the operation of said systems (credit and liquidity risks, operational risks). As such, access criteria are in line with oversight principles established by national authorities and the Eurosystems.

D. Customer choice and mobility

7. What are the main reasons for the low mobility of retail banking customers?

The Italian scenario seems to confute the thesis of a low inter-bank client mobility for both retail and small business segments. In particular, on the ground of evidence emerged within "Interim Report II – Current accounts and related services", published by DG Competition, it is showed how Italian banking clients are characterized by a mobility rate of yearly 7,68%, indicating how more than two million clients switch bank every year. Such a figure is then in line with the weighted average mobility rate registered for EU-15 countries, which equals 7,55% (see Chart 36 - Interim Report). As far as small business is concerned, it must be observed that the small size of Italian firms, with respect to European average, justifies the presence of a slightly lower mobility rate compared with average EU-15 (Italy 11,23% versus Europe 12,12% - see Interim Report's Chart 36) and closer to that registered for retail clients.
Anyhow, the fact that every year one out of thirteen Italian retail clients changes his bank account, has not discouraged the banking industry from the objective of developing and projecting new solutions to enhance mobility.
In particular, the so-far implemented measures or those next to be completed, have involved important aspects aiming to make information available to clients even more clear and comprehensible. The 2007 scheduled operations will instead focus on the simplification of some procedural steps.
The Italian Banking Association, in September 2003, has supported the creation of an independent consortium, named Consorzio PattiChiari, to which as of today have joined 167 banks amounting to 83% of all Italian bank branches, with the goal of promoting initiatives

[1] *The Interbank Convention on Automation is an association whose primary concern is to plan initiatives in the field of interbank automation with regard, in particular, to telecommunications systems and interbank applications. It also co-ordinates the implementation of joint projects, particularly with regard to the development of the payment system. CIPA comprises the Bank of Italy, which acts as chair and provides the secretariat, ABI, 90 banks and 14 bodies and companies working in the field of interbank automation.*

aiming to develop a positive relationship between the banking system and its stakeholders through communication and knowledge tools and financial education plans.
Thanks to some of such initiatives indeed, launched on January 2004, banking clients have been offered the possibility to easily acquire all available information, enabling a clearer and complete comprehension of bank accounts. In particular, through the initiative named "Bank Accounts Compared" clients are able to compare, on the Internet and through some simple standard forms, the cost items of more than 500 packaged bank accounts, offered in 21,000 branches amounting to 67% of the whole system. The "Bank Accounts Compared" initiative allows clients to access information also through a customized search by product type and geographic location.
Recently, on June 20th 2006, the Italian Banking Association and Confindustria (the Confederation of Italian Industry) have launched a similar initiative called "Business Current Account Compared" aimed to support SMEs in comparing the principal conditions of SMEs "packaged" current account products. Each product is described through a detailed form counting 74 items which are homogenous, transparent and easily comparable. As of today, 18 banks (42% of all Italian bank branches) display on the web site www.bankimprese.it the features more than 21 current account products. Participating banks commit themselves to provide clear information to SMEs; a guide will be available at the bank counter and on the bank's web site.
Since June 2006, PattiChiari has been furthermore hosting the website http://edu.pattichiari.it, in addition to the official www.pattichiari.it launched on September 2003, which presents a series of educational paths to better understand financial products and services.
The Italian Banking Association has scheduled for February 2007 the launch of an inter-bank procedure enabling clients to transfer, maintaining continuity, direct interbank remittance directly authorised by the new bank. Such a procedure, affecting yearly 503 million operations like utility billings, for example, will contribute to improve and simplify the process of transferring a bank account.
Meanwhile, PattiChiari is preparing a set of informative instruments aiming to support clients who are willing to close their bank account. On October 2006, a guide named "Switching bank: Guide to transfer bank account services" presenting all relevant information, in a clear and simple way, to transfer services related to a bank account, will be available at the bank counter. On December 2006, a list of the services (e.g. credit and debit cards) related to each client account will then be available and will ease, for the client, the process of monitoring such services. At the same time, a procedure to monitor average closing times will be launched by each participating bank with respect to its own products.
From a legislative perspective, Italy has recently implemented Law no. 248/2006 provides that a customer – regardless of his/her capacity as a consumer or professional – has a right to withdraw from a "duration contract" (i.e. a contract that tends to establish a durable relationship with clients. The exercise of the right of withdrawal shall carry nor penalties nor other costs for the closing of the account. The right of withdrawal in question shall apply, under the same conditions, following notification of a unilateral variation of the terms and conditions of contract, in which case it must be exercised within 60 days from said notification.

E. Development of payment infrastructures in the context of the Single Euro Payment Area

8. Are there features of the payment industry that limit competition either at the level of provision of clearing and settlement services or the provision of retail banking services? Please indicate areas that merit further investigation.

Concerning the payments infrastructure, see answer to question 6 above.

As to developments of the payment infrastructure in the context of SEPA, it should be noted that the local reach of payment services within the context of the various EU Member States and the fragmentation of the payment systems through which such instruments are offered (infrastructure, national regulations, inter-bank agreements, technical standards) is consistent with the requirements of national markets. As such, cross border needs are only partially covered by such instruments.
This is the reason why the work carried on within the EPC (European Payments Council), of which ABI is a member, is designed to define new harmonized Credit Transfer and Direct Debit Schemes for both national and intra-EU transactions (SEPA Credit Transfer Scheme and SEPA Direct Debit Scheme). Indeed, the integration of existing national services proved to be unfeasible.
Therefore, the solution outlined at this stage by the Pan-European banking community – that had to consider such diversities – leaves out of consideration the specific requirements of the various countries and is represented by basic schemes on which each bank or banking community will succeed in creating its own offer with additional services.
In this connection, it should be stressed that the usefulness of the inter-bank agreements as specified above becomes even greater within the context of a program – such as the realization of SEPA, which represents the answer of the banking industry to requests voiced first of all by the European institutions – that aims at giving rise to a harmonized, efficient and innovative area of payment instruments and services for all citizens in Europe and that, therefore, requires the active intervention of all the banks in Europe.
Moreover, in general terms rules, standards and interchange fees are all important pieces of agreement among payment services providers. The nature of such agreements is so peculiar and they must be adopted by so many companies (payments service providers) that they should be evaluated by EU Competition Authority under a special procedure, resuming the modalities already in place in the past for this kind of dossiers: a formal clearance to be granted after a detailed analysis of the content and after sharing the methodology for defining an adequate interchange fee.
A last – but not minor – remark concerns the methodology adopted by the different Competition Authorities operating throughout Europe for the evaluation of payments service agreements. We are fully convinced that this kind of agreements should be assessed using the same philosophy, the same approach and the same methodology by all the authorities competent both at national and EU level.

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9. Are interchange fees necessary for the development of payment instruments (credit transfers and direct debits) in the EU?

Two sided networks, such as the SEPA Direct Debit Scheme and the SEPA Credit transfer Scheme, create economic benefits because of the so-called network effects (positive externalities). The greater the reach of the network, and the wider and more numerous the membership, the greater the economic benefits for all network members. Such benefits are in the form of transactional and cost efficiencies.

The benefits and costs of network membership are often unevenly distributed, with one-side benefiting more than the other side. In such circumstances, a mechanism which addresses the imbalance by redistributing costs and benefits between members is often required to attract the widest possible network membership. Re-aligning costs and benefits of network members provides incentives for participation, enabling network reach to be widened, network costs to be reduced, and benefits maximized, for all network users.
The need to re-balance the asymmetry of benefits of network membership could require the development of interchange fees between banks, in particular for SEPA Direct Debit.
In fact, in order to encourage debtors to use the Direct Debit, in particular in the start-up phase, in most countries debtors are often not charged specifically for a direct debit transaction. In practice, this may mean the debtor's bank is unable to recover its costs from the debtor. The creditor bank therefore compensates the debtor bank for its costs via an interchange fee. This mechanism encourage banks focused on debtor customers to join the Direct Debit network.
Also for the SEPA Credit Transfer Scheme, it may be convenient to set an interchange mechanism to make it possible for the beneficiary bank to recover its cost from the ordering bank in those cases where fully automated payment processing is not possible, e.g. because STP requirements are not applied. This could happen, for example, if there is a lack of or an inconsistency in the information provided by the ordering customer to his bank.
To make the interchange fee mechanism efficient, so that the prices charged to customers by individual banks can be reduced, it is important to set interchange fees at a multilateral default level (related to costs that fees are intended to cover). As a matter of fact, in a network of over 5000 member banks, such as that of the SEPA banks a collective agreement regarding fees may provide efficiency benefits relative to bilaterally negotiated agreements (which may generate higher costs and less transparency). In any case, a multilateral default balancing mechanism does not prevent Scheme participants which wish to transact with other participants on a bilateral basis to do so.

10. Are there issues related to industry initiatives in the context of SEPA that should be assessed form a competition view point?

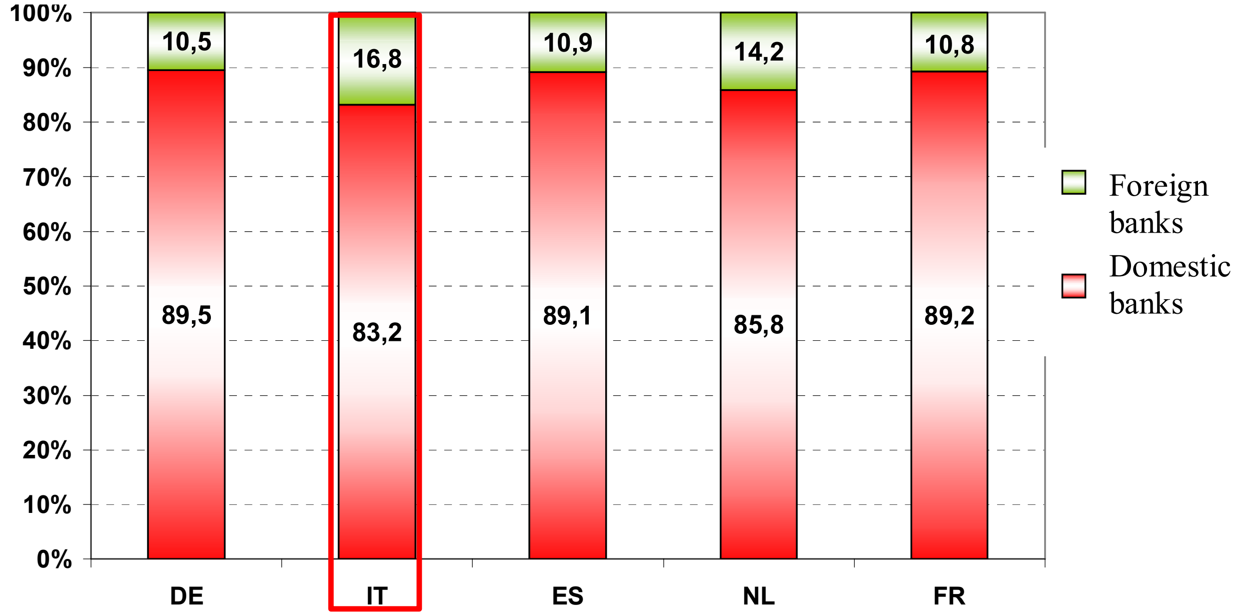
See answer to question 8.

F. Other issues

11. Please provide comments on any other competition-related issues in relation to retail banking markets.

With reference to the evidence provided by Claessens et al. (2001) that shows "that for most countries a larger foreign ownership share of banks is correlated with lower profitability and interest rate margins among domestically owned banks" (Interim Report, page 33), we can see that in Italy the percentage of total assets owned by foreign banks is higher than the other main countries (see diagram 3).

Diagram 3 - Banks foreign ownership, in terms of total assets, in main European countries in 2005



Source: ECB data processed by ABI Study & Research Centre

Moreover, the increasing offer of products/services by telephone and electronic channels contributes, in a meaningful way, to pull down national barriers and favours the development of competition also in the retail banking market. To that it must be added to the always greater spread of holding companies specialized in the fields of the mortgage and the credit to the consumption.

General questions:

1. Did you find the content of the report easily accessible and understandable?

☑ Yes, fully

☐ The report was too general

☐ The report was too technical

2. Did you find that the level of detail in the report was:

☑ about right

☐ not sufficiently detailed

☐ too detailed

3. Did the information contained in the report was:

☑ generally new to you/the retail banking industry;

☐ mostly known to you/the retail banking industry.

4. Did the market analysis in the report:

☐ confirm your views on the operation of the retail banking market;

☑ challenge your/industry's views on the operation of the retail banking market

☐ represent a mix of both aspects

5. Did the report raise the right policy issues;

☐ yes, covered most of the key issues;

☑ no, there were some significant issues left out.