

AN RS2 WHITE PAPER  
JULY 2016

---

# HOW TO POSITION YOUR BUSINESS FOR SUCCESS IN CHANGING TIMES



# CONTENTS

---

|                                      |       |
|--------------------------------------|-------|
| INTRODUCTION                         | 03    |
| THE MERCHANT PAYMENT ECOSYSTEM TODAY | 04    |
| CHANGE AGENTS                        | 05-06 |
| OVERLAPPING FUTURES                  | 07-08 |
| HOW TO NAVIGATE CHANGE SUCCESSFULLY  | 09    |
| SUMMARY                              | 10    |
| ABOUT RS2                            | 11    |

## INTRODUCTION

---

*Card acquiring and acceptance are becoming increasingly commoditised. As such, organisations are looking to new sources of value to improve margins and improve the 'stickiness' of relationships.*

At the same time, the incumbents face disintermediation threats from both look-alike and non-look-alike competitors, who are offering more services along the value chain. Add to this, cyber threats, changing technology and increasing regulation, and it feels as if everything is changing, including the nature of change itself.

We step back to take stock of the merchant payment ecosystem today. We present our take on the state of the nation, and consider how various futures may play out. We also reflect on partnership and how best to partner to mitigate changing, external risks and position your business to take advantage of future opportunities.

# THE MERCHANT PAYMENT ECOSYSTEM TODAY

The payments industry has a long tradition of outsourcing, partnership and collaboration across a wide range of organisations. Consider how many parties are involved each time a customer buys something with a plastic card, pays a bill or sends funds overseas. And how all the parties work together behind the scenes before, during and after the transaction to make it happen.

If anything, the merchant payment ecosystem has become even more dynamic and interconnected in recent years. The ecosystem has grown in terms of the number of players, each providing their own piece of the puzzle. The mobile point of sale (mPOS) phenomenon is a perfect illustration of this. In the traditional POS ecosystem, a terminal vendor linked via a comms integration out to the merchant acquirer. In the mPOS ecosystem, there are many more parties involved: a hardware vendor to supply the PIN entry device (PED), an application developer to create the app for the merchant's mobile device, an intelligent gateway provider, a POS gateway provider and an acquirer. There may not necessarily be

many parties in each area – and fewer still that can provide the whole turnkey solution – but the ecosystem is undoubtedly more complex. The industry is also witnessing more ‘shape shifting’ as organisations integrate themselves forward and backward in the value chain. Companies are offering more and different services as they try to capture more value from customers and increase the ‘stickiness’ of relationships. The ‘shape shifting’ continues in that while companies may outsource to others, they may also act as outsourced service providers for others. The roles they play, as well as what they are called (e.g. terminal vendor, payment facilitator, acquirer), may depend on the particular partnership at the time. The greater fluidity between parties is creating a new competitive dynamic.

Then there are the new entrants and non-look-alike competitors. The new organisations emerging are very nimble, fast and technology-driven. They are the challenger banks, the alternative finance providers and the crowdsourcing platforms. Such organisations are challenging the incumbents. Either by targeting un-served or under-served customers. Or by providing a better, more efficient or cost-effective version of an existing product or service.

“The wider business world is beginning to wake up to the concept of the extended enterprise. It is not just a matter of longer or more international supply chains, but sub-contracted relationships, outsourced back-office functions and licensed intellectual property. The extended enterprise allows various organisations to come together to achieve something that none of them could have realised alone. This is in the DNA of the payment industry.”

– Radi El Haj, CEO, RS2.

## CHANGE AGENTS

The merchant payment ecosystem is being shaped by external factors. These are presented individually below, but they overlap. It is these overlaps that help create the ripple effect of change and innovation. This may be breakthrough or incremental innovation, both of which have a role to play in shaping the merchant payment ecosystem.

## CYBERSECURITY

Financial institutions are being pushed to step up their defences against cyber attacks. Speaking in May 2016, the chairman of the European Banking Authority called on domestic regulators to stress-test local banks to understand the possible risks. The European Central Bank is also setting up a central cyber crime database as an early warning system for banks as to possible attacks. The moves come at a time of heightened alert in view of the cyber attacks against banks participating in the SWIFT system.

*"The cyber threat is one that will not go away. There is no silver bullet solution to mitigating risk. Our advice though is to move from a focus on preventative perimeter controls, to a blended approach including detective, responsive and recovery measures,"* says Radi El Haj, CEO, RS2.

## DATA

The term 'information explosion' has been in use since the 1960s, so the idea that we are living in the age of a data surge is not new. However up until about a decade or so ago, the scientific, industrial and corporate

communities produced the majority of the world's data. Nowadays it is individuals.

Around 44.4 million Whats App messages are sent every minute, 400 hours of YouTube video uploaded, 3.3 million Facebook posts made and 55,555 Instagram photos shared, according to statistics from Smart Insights. We are definitely living in Big Data times.

*"The challenge is to process more data faster, to do more with your own data and help customers do more with theirs. This could be in the area of data analytics, dashboarding or benchmarking,"* comments El Haj.

## INTERNET OF THINGS

The term Internet of Things (IoT) was first coined in the late 1990s to refer to machines talking to each other. A decade-and-a-half later, and thanks to the falling cost of RFID tags, the scope of IoT expands far beyond home appliances and the oft-cited self-stocking refrigerator. It encompasses cars, people, industry and business, which in turn impacts our cities, infrastructure, homes, health and so on.

*"When the internet extends into the physical world and machines communicate with each other, this opens up a whole range of new possibilities. I think it's still early days in exploring IoT for payments and the elusive 'killer app'. But there's no doubt that IoT, including M2M and smart cities, has the potential to be a major disruptor and agent for change,"* says El Haj.

# CHANGE AGENTS

---

## MOBILE

2015 was a year of continued growth in the mobile industry, with more than 7.6 billion mobile connections (representing 4.7 billion unique subscribers) and operator revenues of more than \$1 trillion, according to the GSMA. The trade body also noted that the third quarter of 2015 saw the largest amount of venture capital activity on record into the mobile sector, with a particular focus on mobile commerce and software and services.

*“Who thought 20 or even 15 years ago that we would be using our mobile phones to wake us up in the morning, keep in contact with family, friends and business associates all over the world, shop, bank, navigate our way around foreign cities and take photos? It is difficult to overstate the point: mobile is and will continue to be a game-changer,”* explains El Haj.

## NEW BUSINESS MODELS

Airbnb has become the world's largest hotel group, which owns no rooms. Uber the largest taxi company, which owns no taxis. And Task Rabbit a major freelance employer with no employees. Welcome to the somewhat confusingly-named 'sharing economy', which connects buyers with sellers via internet-enabled platforms. And in the process has disrupted ideas around ownership, employment and traditional business models.

According to research from Juniper, sharing economy platforms are to witness a trebling of revenues from \$6.4 billion in 2015 to \$20.4 billion by 2020. Expansion into emerging markets, coupled with growth in more established

regions, will drive returns for investors. It will also inspire further me-too and downstream innovation in new business models.

## REGULATION

The payments industry is at the confluence of much regulatory change. This covers everything from the Payment Services Directive 2, strong customer authentication, anti-money laundering, data protection and privacy. Sometimes the provisions overlap; sometimes they conflict. Yet every organisation must grapple with the impact of regulation.

Regulation can act as a catalyst for innovation. It can also provide the impetus for a mindset re-set internally around people (culture), processes and technology. In this way, regulation is an opportunity as well as a threat. And failure to adequately address regulation within an organisation can lead to a high opportunity cost.

*“Regulation is the archetypal external risk. It affects every organisation. But the impact may depend on how well an organisation identifies its risks, manages and mitigates them in advance. And how adaptable it is once new and updated regulation appears,”* explains El Haj.

***“The challenge is to process more data faster, to do more with your own data and help customers do more with theirs. This could be in the area of data analytics, dashboarding or benchmarking,”***  
comments Radi El Haj, CEO, RS2.

# OVERLAPPING FUTURES

---

Commoditisation occurs when the market perceives products or services to be substitutable.

Generally, there are two main drivers for commoditisation. Firstly, the emergence of a standard design or technology in the market. Various companies may compete to set the market standard initially. But as the market matures over time, companies converge on the standard. This makes substitution easier across various similar offerings.

Secondly, the increasing transparency around features and prices. When customers can compare the features and prices of various competitive offerings more easily, they may be more inclined to switch providers. This is naturally easier in the internet age with the rise of product review and price comparison websites.

Commoditisation may lead to slowing growth, falling prices and increased competition. However, there are ways to create and sustain a competitive advantage. Naturally these are not mutually exclusive. We set out some of the possible overlapping futures.

## 1. BUILD SCALE

Sometimes commercial Darwinism prevails where only the fittest companies survive. Often fit means big, and it is a case of buy or be bought out. Several large merchant acquirers have a global footprint thanks to merger, acquisition and joint venture activities. Fit can also mean fit-for-purpose. Companies consolidate for scale but also to expand their core competencies and to leverage innovation to a wider base.

## 2. SPECIALISE

Pursuing the path to specialisation can help a company differentiate within one or a small number of target market segments. The specialised needs of the segment produces an opportunity over competitors who may be targeting a broader group of customers. Examples of this include merchant acquirers who have focused on the specialised needs of the T&E or airline sector, or of e-commerce merchants looking to expand their businesses globally.

## 3. DIVERSIFY

Diversification can also help with differentiation. It can be achieved through internal investment in staff, product development and service delivery. However if a company realises that supporting customer needs goes beyond what they are able to supply acting alone, sometimes it is more time-efficient and cost-effective to buy a company that is already doing this – hence the overlap with M&A activity.

## 4. INNOVATE, BUNDLE AND SEGMENT

Innovation is a strong way to create and sustain competitive advantage. This may be through investing in R&D, developing patented products or proprietary methodologies. Product lifecycles are getting shorter though. And a new breed of competitors is emerging, who are fast, nimble and technology-driven. Incumbents have to try and stay ahead, and investing in innovation is one way to do this. It also helps keep barriers to entry high.

# OVERLAPPING FUTURES

Bundling products and services together is another classic way to extend convenience to customers and lock in loyalty. The growth in managed services and 'as a service' propositions reflects this trend. Such services are becoming increasingly common, so much so they are gaining their own acronyms, for example software as a service (SaaS) and compliance as a service (CaaS).

Segmenting the customer base, particularly in mature markets, can be a way to extend the product lifecycle and profitability. A needs-based segmentation allows a company to create differential advantages based on the value to the customer, rather than being focused on features.

## 5. CREATE SUSTAINABLE DIFFERENTIAL ADVANTAGE

Competing on price is often a race to the bottom. Low prices can be easily copied by competitors, so any advantage is often short-lived. To create sustainable differential advantage, focus on elements that are not easy to replicate. For example, high levels of service by well-trained staff, fast reaction times, superior implementation and de-bugging, and close relationships with customers.

## SMART PARTNERSHIPS

Smart partnerships are increasingly coming to the fore. However you choose to create and sustain competitive advantage, smart partnerships underpin the overlapping futures set out above.

One definition of a smart partnership is focusing on what you do best and expanding capabilities by using partners for what they do best. Another definition is choosing partners

wisely to minimise risk exposure. After all, choosing the wrong partners at the outset may make it more difficult to recover over the lifetime of a contract, irrespective of whatever 'fail faster' policies either party implements.

Choosing the right partners is not just about conducting due diligence on the counterpart's financials, legal and competence to conduct the contracted services, although this is important. Nor is it just about agreeing a scope of work, a robust contract and a project plan. Choosing the right partners is also about the strategic fit and chemistry between organisations.

Are your strategic goals aligned? Are there synergies between your leadership teams, governance and cultures? How much time and resource do you plan to dedicate to communicating effectively and managing the partnership? Tellingly, it is the people and partnership-related factors, rather than the process and procurement-related ones that contribute most to a successful working relationship.

***"We advise dedicating sufficient resources to managing any partnership. This should involve almost every part of your organisation from colleagues in the finance and legal departments to those in frontline customer-facing roles. Share business plans and any changes in direction with your partners, and encourage them to do the same," - Radi El Haj, CEO, RS2.***

# HOW TO NAVIGATE CHANGE SUCCESSFULLY

---

Whether your business is looking to build scale, specialise or diversify, here are some of the ways in which RS2 can help you and your merchants navigate changing times – and make payment happen.

## ARCHITECTURE

Built on state-of-the-art IBM infrastructure, our architecture is flexible, service oriented (SOA) and modular by design. This gives you faster speed-to-market, lower set-up costs and full tailorability irrespective of sales channel.

## AGNOSTIC

No matter what terminal hardware or applications merchants run, our systems are agnostic. They integrate with everything and everyone for maximum efficiency. This makes it quicker, simpler and cheaper to roll out to new stores, new countries and new channels.

## ALTERNATIVE PAYMENT METHODS

Convert browsers into buyers wherever they are in the world by accepting a wide range of payment methods. Our APIs make switching on new payment methods pain-free, either at launch or later in the project.

## MULTI-NATIONAL

Payments is almost multi-national by default. We offer domestic and international clearing and settlement of payments with full multi-currency facilities in more than 120 currencies to power business internationally.

## LEGAL AND REGULATORY

We take on the legal and regulatory burden on our core systems, so you don't have to. BankWORKS® is compliant with EMV standards, PCI DSS (version 2.0) and PA-DSS, the SEPA card framework (SCF) and EPC requirements around acquiring and clearing.

## MODULAR

Take the modules you want, leave the ones you don't. With our parameter-based, modular structure, it really is that simple to tailor existing modules and add new ones with minimum time, cost and effort.

## MANAGED SERVICE

Outsourcing to a trusted partner via a managed service saves all around. It saves you having to make your own internal investment in capabilities. It saves having to recruit, train and retain in-house experts. And it saves time in having to keep up-to-date with industry standards and changes.

## RESILIENT

Whether your customers trade across one channel or many, if they are unable to accept payment at any time, that's bad for business. We process on behalf of some of the largest multi-national banks and retailers. Our systems have 100 percent availability, are able to cope with sales peaks and troughs, and have back-ups to every element for maximum resilience.

## SUMMARY

We live and work in changing times. The external agents of change include the growing cybersecurity threat, the data including from the Internet of Things, mobile, new business models and the ever-expanding scope of regulation.

These factors are creating the external context for all actors in the payments industry. However, while every organisation has to contend with the same external factors, the impact on each may be different, depending on how it identifies and addresses its opportunities and risks.

In the face of commoditisation pressures, organisations are advised to create and sustain competitive advantage. They can do this in a number of overlapping ways, including building scale, specialising, diversifying and innovating. Most of all, however, they can do this through smart partnerships – knowing how and with whom to partner.





## ABOUT RS2

RS2 Software plc is the publicly-listed company behind the BankWORKS® payment processing software used by major banks, payment service providers and other financial institutions. The company has a head office in Malta and offices in Germany, Jordan, the Philippines and the US.

Established in 1988, RS2 Software plc has continually focused on developing and implementing highly scalable, reliable and flexible card payment processing solutions. As an industry-leading, end-to-end solution provider for card acquiring, card issuing and ATM services, we support all aspects

of authorisation and message switching, transaction routing, domestic and international clearing. Full multi-currency facilities in more than 120 currencies are available for the cross-border clearing and settlement of payments.

BankWORKS® is the transaction processing power behind some of the world's most innovative and fastest growing payment companies. It is deployed by more than 100 banks, payment processors and financial institutions around the world.

For more information visit [www.rs2.com](http://www.rs2.com)