MasterCard Europe: Different, But Not Better

As MasterCard restructures into a public company, only in Europe are bankers guaranteed local control. Will this turn out to be a mistake?

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With its IPO, MasterCard will convert from a registered private share corporation controlled by banks into an independent public company-almost. The cutover will be clean except in Europe, its second-largest market. In Europe, a board of bankers will continue to manage most meaningful aspects of MasterCard's business. This will put a bridle on the global payment network's growth and IPO valuation prospects.

MasterCard will keep a regional banker board in Europe as the price of major members there going along with the IPO. MasterCard Europe and its predecessor Europay operated as a cozy bankers' club, and have long been more distrustful of unfettered market solutions than their American peers

Continental European bank cartels ring-fence national markets and block nonbank competitors. The IPO will plunge MasterCard headfirst into the free market. Many European banks feel they were bullied into the IPO to fix an American problem: the avalanche of U.S. lawsuits threatening to destroy the franchise. They want to hold back.

The European banker board will supervise MasterCard membership in Europe. Elsewhere management and the global board will be strongly motivated to woo nonbank businesses that can help increase MasterCard issuance and utilization. Mobile phone operators; retailers, insurance carriers; consumer portals, such as Yahoo and Google; and even governments may be powerful new classes of customers that can issue and acquire MasterCard products. In Europe, banks will decidedly not be keen to welcome potentially formidable new competitors into what they continue to regard as their club.

Mobile phone operators are illustrative. They have enormous reach and longstanding, to date, largely unrealized ambitions to provide payment services. Orange, Telefónica Móviles and T-Mobile have 64 million, 81 million and 83 million customers respectively. Few banks have more. Vodafone has a mind-numbing 450 million customers.

Mobile phone operators have undertaken a variety of projects to develop payment systems, largely without collaborating with established global payment systems, such as MasterCard and Visa. These efforts have failed, or been lackluster. For instance, in June 2004, Orange, Telefónica Móviles, T-Mobile and Vodafone pulled the plug on their joint venture, SimPay, which attempted to create a new payment network.

The mobile phone operators are loath to share customer relationships and handset real estate. Banks view mobile operator payment products as a competitive threat.

Telco Partners?

Now, however, outside Europe, MasterCard will be able to partner with mobile phone operators. Mobile operators could issue and acquire MasterCard payment products. For consumers, handsets can hold or serve as keys to credit, debit or stored value account numbers. On the merchant side, hybrid mobile phone devices can serve as payment terminals, enabling cost-effective acceptance in infrastructure-challenged emerging markets.

In Europe, however, bankers will stymie mobile phone operators working directly with the global payment network. And mobile telephony is not the only sector where the European board is likely to forestall payment market development.

With cobranded and affinity programs, card issuers and other organizations share economics, brand space on the card, and a variety of cardholder rewards. A majority of U.S. credit cards are now cobranded. In Europe, cobranding and affinity rules will continue to be approved by the regional banker board. An independent MasterCard will become more accommodating while the European region stonewalls, trying to impede competition from innovative retailers. In some countries, rules governing cobranding and affinity programs are particularly restrictive. In France, for instance, the national card-governing body Cartes Bancaires bans cobranding.

Impact On Interchange

European assessments and fees will be set by the regional board. This includes interchange, the pricing system that balances the card issuing and merchant acquiring sides of the network. Regulators have looked at MasterCard's interchange system as a bank cartel fixing prices. They will continue to have a powerful rationale to tightly regulate interchange, because banks, principally, will control it. This will hamstring MasterCard's freedom to grow.

The planned Single Euro Payments Area, or SEPA, may be one area where it isn't European regulators who curb MasterCard's growth. The European Commission has pressured banks to create a single euro payments infrastructure that harmonizes payment card rules throughout the region. Fearing revenue loss, banks, for the most part, have dragged their feet.

MasterCard can support high-volume payments throughout the euro-zone. Unfettered by bank interests, it would be freer to pursue this opportunity. But a board beholden to national bank cartels and networks is likely to oppose such initiatives.

The European board will supervise regional operating rules. Post-IPO MasterCard will be motivated to more quickly adapt operating rules to market realities. But the European board is likely to behave as it has in the past. Since much of MasterCard's value derives from its coherent global brands and rules, MasterCard may have to move more slowly elsewhere so as not to get too far ahead of Europe. However, decisions of MasterCard's European board can be overruled by the global board.

In short, MasterCard is trying to have it both ways: to enjoy the benefits of independence, a public currency, and easier access to capital, all the while retaining in Europe its legacy association governance.

The regional board poses legal and regulatory risks because it incarnates a bank consortium fixing prices and restraining competition, which has been the rationale for so many of the most damaging legal and regulatory assaults on MasterCard.

So, at almost every level, the unique regional European board is likely to hamper MasterCard's growth. Out of the gate, it bears the seeds of its own unraveling.

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Editor's Note: MasterCard International declined to respond to this column, citing a regulator-mandated "quiet period" in advance of its initial public offering of stock, now scheduled for the second quarter.

HOW MASTERCARD EUROPE WILL BE DIFFERENT

Post-IPO, a board of European bankers will oversee:

Membership Assessments, interchange, transaction pricing

Operating rules

Affinity and cobranding rules

Intraregional product enhancement

Elsewhere, MasterCard will manage all aspects of the business, subject to independent board supervision.