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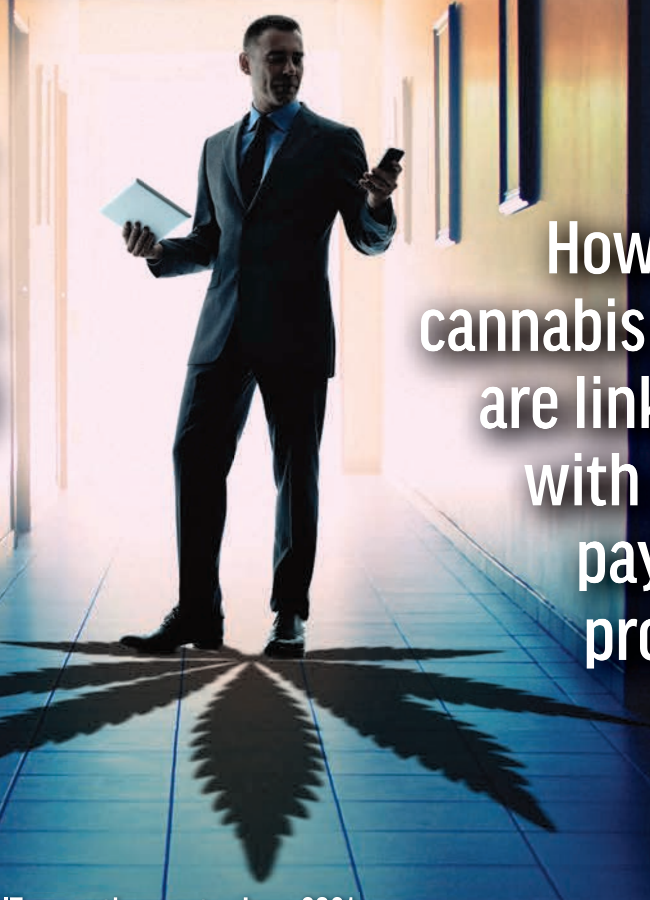
Trends in the Electronic Exchange of Value



POT PAYMENTS EMERGE FROM THE SHADOWS

How canny cannabis sellers are linking up with plucky payments providers.

Volume Eighteen, Number Six • DigitalTransactions.net • June 2021

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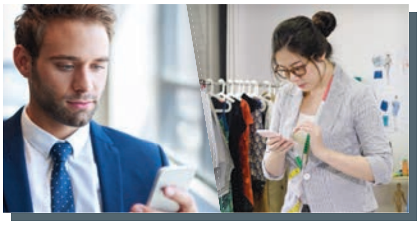

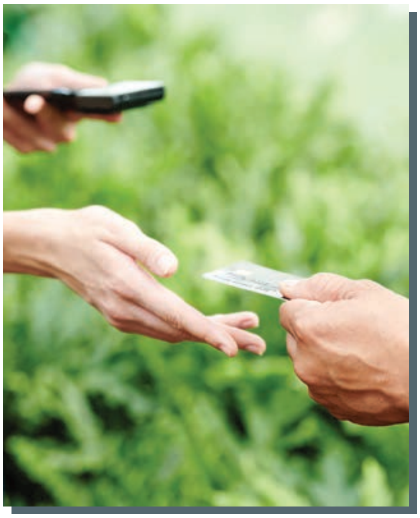

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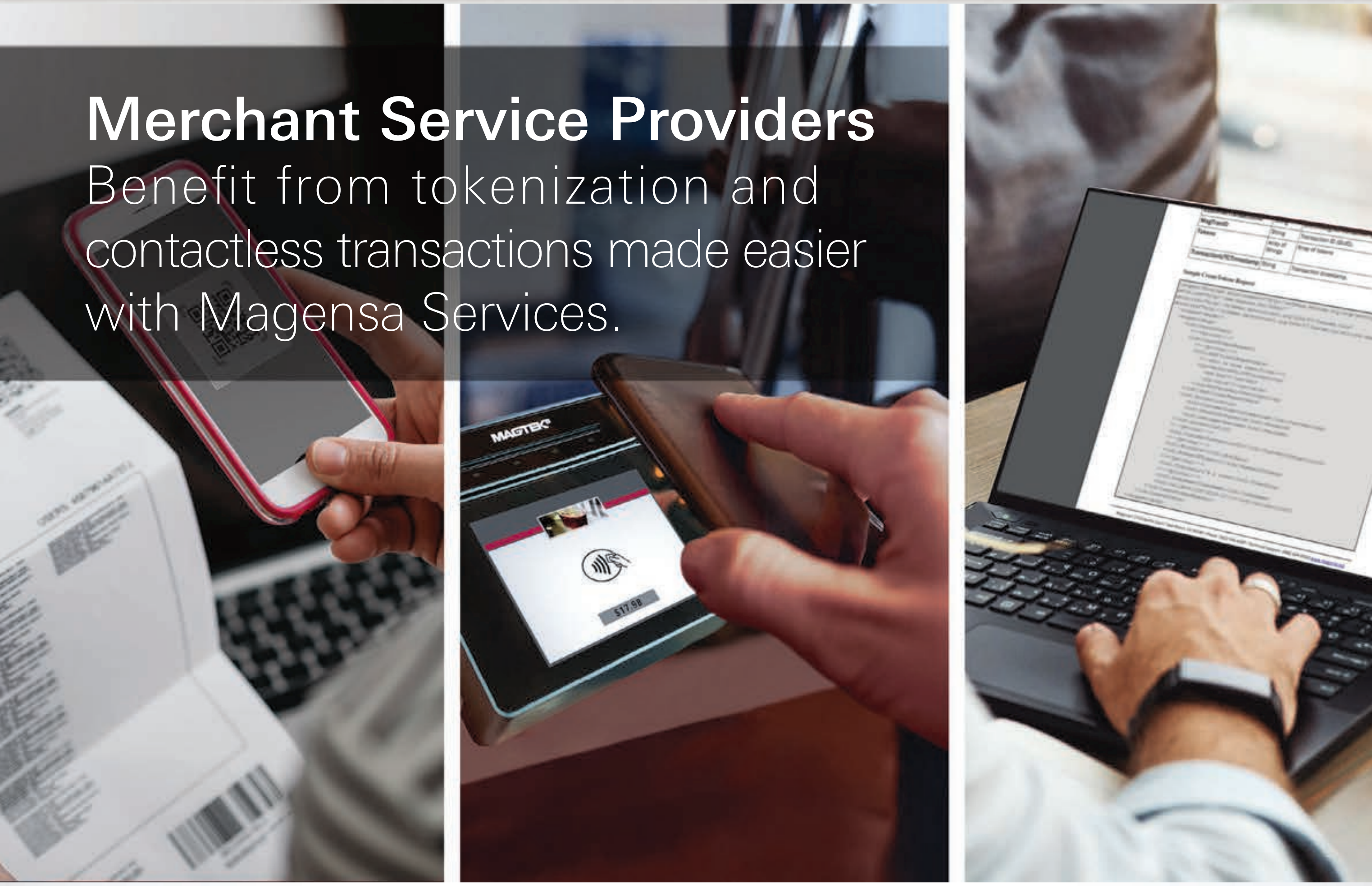

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A HUMBLE HOMECOMING

LIBRA—ER, SORRY, DIEM—IS COMING HOME to the United States, a bit bruised but also a bit wiser than when it left. Bruised but unbowed, the Facebook-inspired blockchain initiative announced in May it is quitting Switzerland and linking up with La Jolla, Calif.-based Silvergate Bank as it plots the next stage of its evolution.

The controversy surrounding Diem has been so intense—and its maneuverings to please multiple governments and regulatory bodies so serpentine—that it's easy to forget the project is a mere 2 years old. It emerged in the early summer of 2019 with backing from Facebook and a panoply of payments and finance companies in an effort to create a cryptocurrency and wallet that could bring digital currency to everyday people around the world.

It was a noble thought, but it was also political poison. Facebook was already struggling on Capitol Hill and elsewhere with trust issues in its social-media networks. Now, a new cryptocurrency venture hatched by that company along with powerful payments networks like Visa and Mastercard drew withering criticism from skeptical governments and central bankers worldwide.

Before long, Visa, Mastercard, and number of other original backers had abandoned ship. The Libra venture decamped to Geneva and began adopting various course changes trying to please the Swiss Financial Markets Authority (FINMA) and other national banking authorities.

It was time for a new name to go along with a new set of operating principles. But the authorities behind the venture didn't drop their affinity for Latin, rechristening the association "Diem" (or "day"). The venture soon adopted a single-currency stablecoin approach to avoid the wild swings in value that plague unmoored cryptos and said it would adhere to a stronger compliance regime.

Now Diem is coming to America, claiming 26 members, up from 21 a year ago. Several big names remain behind the project, including Coinbase, Lyft, Shopify, and Uber. Facebook remains involved, too, through its Novi wallet technology.

The new factor in the mix is Silvergate, a member of the Federal Reserve. It will exclusively issue a new stablecoin tethered to the U.S. dollar and manage its reserve. Diem Networks US will register as a money-services business with the Treasury Department's Financial Crimes Enforcement Network. At the same time, Diem is withdrawing its application to FINMA for a payments-system license.

What happens next is anybody's guess. Despite the turmoil of its early months, the venture has retained the backing of some powerful corporations and payments players. And the pivot to a USD coin—in concert with an established banking authority—can only help in the effort to placate regulators.

So bon voyage, Diem. Or, more appropriately, Carpe Diem!

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IS A LOWER DEBIT CAP COMING?

Pressure is building on the Federal Reserve to take action on a debit card interchange-fee regulation that it has left intact for 10 years despite sweeping changes in the payments business, including an onrush of e-commerce transactions over the past year.

In part, observers are reacting to a report the Fed released last month indicating that issuers' authorization, clearing, and settlement (ACS) costs for debit have declined dramatically over the years.

In 2019, those costs came to 3.9 cents per transaction, roughly half the costs in 2009, according to the report. At the same time, the 10-year-old Fed ceiling on debit card interchange, which flows to issuers, in 2019 was greater than total ACS costs plus fraud losses for nearly 79% of covered issuers and close to 100% of covered transactions, the report says.

The Fed set the debit cap at 21 cents, with an additional penny allowed for fraud-prevention costs and 0.05% for recovery of fraud losses. The ceiling, which applies to financial institutions with $10 billion or more in assets—the so-called covered issuers—came in response to the Durbin Amendment to the Dodd-Frank Act of 2010.

The latest Fed report indicates online transactions, known as card-not-present volume, sustained $12.40 in fraud losses per $10,000 in volume in 2019, up from $7.80 in 2011. Merchants absorbed 56.3% of these losses, up from 52.8% in 2017, according to the report, indicating that percentage could be even higher now with e-commerce volume booming since the onset of Covid-19.

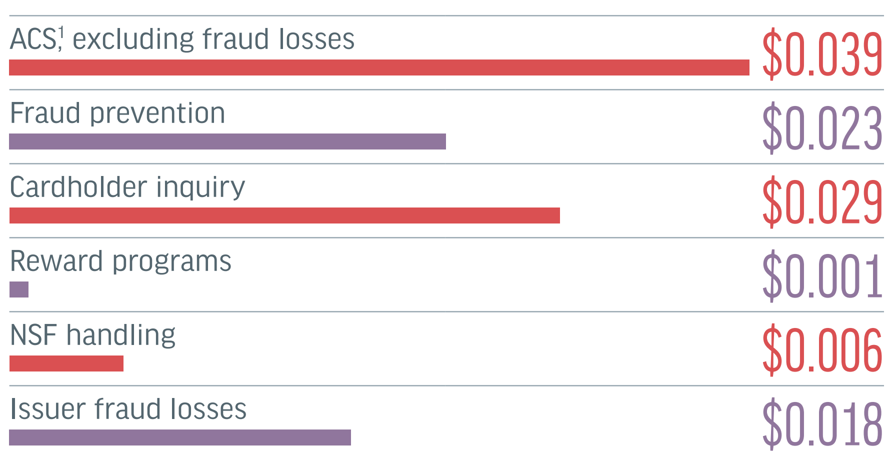
The report's numbers lead some observers to predict the Fed will approach covered issuers with a revised fee cap that could be significantly lower than the current one.

"There may be some horse trading," says Steve Mott, who follows the issue closely as principal at consultancy BetterBuyDesign. He predicts the Fed may ultimately lower the cap as much as 4 cents. The Fed did not respond to an inquiry from *Digital Transactions.*

Adding to the pressure on issuers is a lawsuit filed in April that claims

2019 DEBIT COSTS FOR COVERED ISSUERS

(Per transaction)



1. Authorization, clearing, and settlement Note: Covered issuers are those with $10 billion or more in assets Source: Federal Reserve

the debit interchange ceiling is now too high and seeking to force it down.

The case, filed in U.S. District Court in Bismarck, N.D., by the North Dakota Retail Association and the North Dakota Petroleum Marketers Association, argues merchants have paid "billions" of dollars more than they would have had the Fed followed the letter of the Durbin Amendment to the 2010 Dodd-Frank Act with respect to debit costs.

The action came as debit payment volumes skyrocketed last year with U.S. consumers' shift to debit cards in the face of the pandemic. On the Visa network alone, debit payment volume totaled $2.23 trillion in 2020, up 15.2% over 2019, a year that saw a 9.7% growth rate.

In a separate action, the Fed at the same time released a proposed rule that would seek to ensure that merchants can choose between at least two unaffiliated networks for card-not-present transactions in the same manner as for card-present ones.

The Durbin Amendment sought to boost competition by requiring a minimum of two unaffiliated networks for each debit transaction. But merchant groups have long complained that alternative cards presented for e-commerce transactions will work only with a PIN, forcing consumers to default to a global network and negating merchants' routing choice.

"[M]erchants are often not able to choose from at least two unaffiliated networks when routing card-not-present transactions, according to data collected by the Board and information from industry participants," the Fed document says.

—John Stewart

A $35-MILLION GAMBIT FOR UNBANKED HISPANICS

Welcome Tech, a provider of digital financial services to unbanked and underbanked Hispanics, plans to leverage $35 million in new funding it secured in April to grow its customer base by about 1 million.

It also plans to add more financial services, such as a pathway to credit, to help bring its customers into the mainstream of financial services. To date, Welcome Tech has raised $50 million.

In late 2020, the Los Angeles-based fintech launched a debit card issued through Green Dot Bank. Cardholders can deposit money into their card account through Welcome Tech's remote check deposit application, which the company developed in-house, or through the more than 90,000 merchants in the Green Dot network.

In addition to its debit card, Welcome Tech offers a mobile wallet—branded as PoderCard—that can store the debit card and access Welcome Tech's other services.

Consumers can sign up for a Welcome Tech account using their Matricula Consular card, which is an identification card issued by the Mexican government through its consulate offices to Mexican nationals living outside the country.

Welcome Tech differentiates itself from other financial-services providers focused on the unbanked in that the company concentrates on unbanked and underbanked Hispanics. Although this group represents the largest minority population in the United States at 62.8 million, less than half of Hispanic households are fully banked, according to Welcome Tech.

"We have built a bilingual user experience in which customers can receive statements in Spanish, English, or both," says Amir Hemmat, Welcome Tech's co-founder, president, and chief executive. "We also offer services beyond financial transactions to help customers improve their financial literacy so they can leverage that knowledge to obtain other financial services."

Welcome Tech, which was founded in 2010, has 3 million customers, about 75% of whom consider the company their primary financial services provider, Hemmat says.

"When you look at other [demographics] underserved by financial-services providers, many of those consumers don't have a primary relationship with a provider, they have multiple relationships," Hemmat adds. "Our aim is to build a banking relationship with our customers that delivers value to them as opposed to extracting value from them."

Welcome Tech also created a rewards program that pays cash to customers educating themselves about financial services. Customers can earn between $1 to $100 for completing a variety of financial services-related tasks, such as taking a survey or participating in a focus group. Earned rewards are immediately deposited into the customer's account.

The company also provides access to health-care services through a monthly subscription plan. Customers pay $10 for access to medical, dental, vision, lab-related, and pharmacy providers offering discounted rates. Discounts can be as much as 80% in some cases.

"We are aggregating a historically fragmented community under a single platform," says Hemmat. "The size of our user base gives us collective [bargaining] power to leverage, which in turn drives better pricing and experiences from service providers."

In keeping with its focus on bilingual services, Hemmat adds the company has partnered with a telehealth provider with bilingual physicians and patients in its network. Hemmat sees additional opportunities to offer access to insurance and legal services through its subscription plan.

"When it comes to customization and personalization in financial services, the underbanked and unbanked are an overlooked market," Hemmat says. "Our aim is to build a [financial-services] platform that focuses on customer needs first so that we can build trust and engagement, and deliver value that is relevant to our customers."

—Peter Lucas

MONTHLY MERCHANT METRIC

Total Gross Processing Revenue, in Percent

Sum of total discount, total transaction fee revenue, and total other fee revenue divided by total volume

Note: This is sourced from The Strawhecker Group's merchant data warehouse of over 3 million merchants in the U.S. market. The ability to understand this data is important as small and medium-size businesses (SMBs) and the payments providers that serve them are key drivers of the economy. All data are for SMB merchants defined as merchants with less than $5 million in annual card volume.

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ZELLE IS 'JUST SCRATCHING THE SURFACE'

Despite posting significant gains in dollar and transaction volume in the first quarter, Zelle, the fast-growing peer-to-peer network operated by Early Warning Services LLC, says it has just begun to mine P2P payments' growth potential.

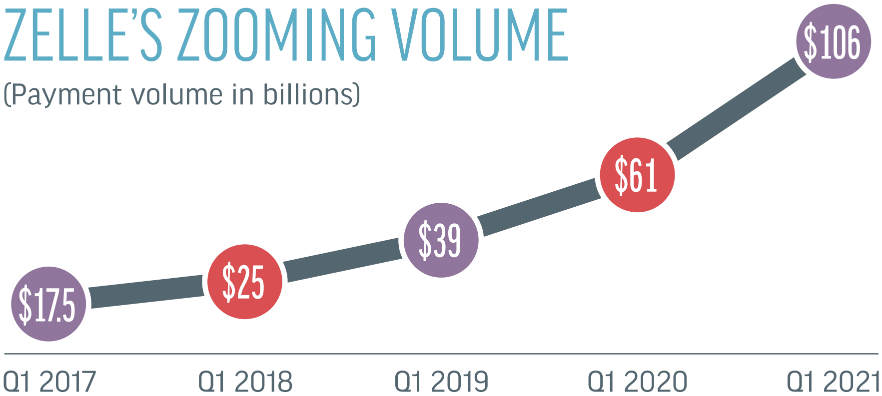
Early last month, Zelle announced $106 billion was sent through its network on 392 million transactions, representing year-over-year increases of 74% and 61%, respectively. Transactions through Zelle's small-business accounts increased 180% over the same period in 2020. Zelle is not disclosing dollar or transaction volume for small-business transactions.

The substantial growth is attributable to a couple of factors. Consumers have been looking for contactless ways to pay family members, neighbors, and landlords since the pandemic began. Equally as important is that, as the economy begins to open up, consumers are returning to old payment habits that were kicked to the curb at the height of the pandemic, such as splitting a restaurant check.

"We have seen a boost from consumers using Zelle as a result of the pandemic, but we have also seen a return of transactions that were displaced when the economy began to shut down," says Lou Anne Alexander, chief product officer for Early Warning.

ZELLE'S ZOOMING VOLUME

(Payment volume in billions)



Source: The company

With the economy reopening and with Covid vaccines becoming widely available, Alexander predicts Zelle will continue to see robust growth as consumers have become more comfortable with P2P payments.

"There are probably 9 billion or more P2P transactions to be had," Alexander says. "Many of these transactions are cash or check [that can be displaced by P2P]. We're just scratching the surface."

On the small-business side of the market, Alexander says a variety of merchants that provide in-home services are adopting Zelle as a way to receive payment that's not only contactless but also faster than if they were paid by check. Services providers accepting Zelle include physical therapists, tutors, and tradesmen. Currently, 12 financial institutions offer Zelle to their small-business clients.

To attract more consumers and make them comfortable with sending payments via a P2P network, Zelle is focusing on consumer education. The network's partnership with EVERFI—a social-impact education technology company—has enabled the network to reach more than 39,000 students in 47 states about the safety of P2P and digital payments, for example.

In addition, Zelle recently partnered with The Cybercrime Support Network to spread awareness and educate consumers and small businesses on avoiding financial fraud and scams. While consumers trust their financial institutions, which serve as their conduits to Zelle, Alexander says they still need to be educated about criminals trying to trick them into using Zelle to send them money. Nearly 8,000 financial institutions participate in the Zelle network.

"Our financial-literacy programs are intended to help consumers identify potential scams," Alexander adds.

Looking ahead, Alexander sees growth opportunities in bill pay and real-time payments. In February, Zelle announced payments can be cleared and settled on the Real Time Payments network, owned by The Clearing House Payments Co. LLC. "We don't think growth will slow," Alexander says. "Consumers are seeing the safety and convenience of paying by Zelle."

—Peter Lucas

CORRECTION

In "Parking Apps Look to Upshift," February, the number of users of the PayByPhone app was misstated. The correct number is 43 million. *Digital Transactions* regrets the error.

PAYPAL'S AIMS IN DIGITAL CURRENCIES

Skeptics abound when it comes to digital currencies, but PayPal Holdings Inc. is out to prove them wrong. Chief executive Dan Schulman, an early enthusiast, made it plain last month he sees the crypto trend not only as the company's big opportunity, but also as a potential liability if PayPal fumbles the ball.

"This whole idea of establishing a cryptocurrency and blockchain unit within PayPal is how we can be a shaper of that [trend], a leader of that, and not a reactor," he told equity analysts tuned in to hear the San Jose, Calif.-based payment company's first-quarter results.

While PayPal did not release numbers regarding its nascent cryptocurrency business, it has in recent months made headlines with its effort to allow users to spend Bitcoin and other crypto with PayPal-accepting merchants. The digital currencies are converted to local fiat money for merchant acceptance.

Now, Schulman said, the next big opportunity could lie in central bank digital currencies, which track local fiat money and are expected to avoid the turbulent swings in value that plague Bitcoin and other digital assets.

"We have had quite a number of conversations in the United States and across the world with regulatory bodies and in government," Schulman said. "We're understanding the concerns they may have, how CBDCs could be issued. Each government is going to go at a different speed, but there isn't one government that isn't envisioning a future with digital fiat currency."

Besides introducing merchant acceptance last year, PayPal has proved willing to invest heavily in building out a cryptocurrency capability, including security assets. Last month, it closed on its acquisition of Curv Inc., a crypto security firm based in Tel Aviv. PayPal has not disclosed a purchase price, but estimates have ranged from under $200 million up to $300 million. "Both crypto and CBDCs could play a critical role [for PayPal]," Schulman said.

Blockchain currencies aside, Schulman hailed the arrival of what he sees as a digital era that he said can only benefit firms like PayPal. Much of this momentum, observers say, has come from the Covid-19 pandemic, which forced many consumers to adopt non-cash payments.

"We are now seeing people live a digital life. It's just a digital world," Schulman told analysts on the call. "Cash is definitely being replaced. That's moving to digital, predominantly to debit, which is great from a funding perspective."

That "funding perspective" matters to PayPal, where active accounts by quarter's end had grown 21% year-over-year to 392 million, including 31 million merchant accounts. Payment volume reached $285 billion, putting the company on a $1 trillion annual rate.

PayPal's Venmo service, which for many years was almost entirely a peer-to-peer payments app, in 2017 also became another option to pay merchants in a service called Pay With Venmo. And in February, PayPal opened a Visa-branded Venmo credit card, issued by Synchrony Bank, to all comers.

Now, Pay With Venmo is "going to be the majority of revenue" in the future, Schulman said, without being more specific. "We've all been bullish on the potential of Venmo. We're now beginning to see it," he said. PayPal did not release numbers specifically for Pay With Venmo, but the Venmo service in total racked up $53 billion in volume in the quarter, up 63% year-over-year.

With respect to more recent initiatives, PayPal's entry in the fast-growing market for installment credit, or buy now, pay later, processed more than $1 billion in the quarter for 330,000 merchants, up from 250,000 in the fourth quarter last year.

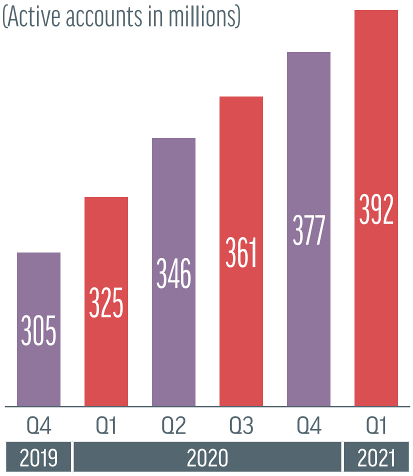
And QR codes, which PayPal launched last year as a contactless technology for in-store transactions, are now accepted by almost 1 million merchants, racking up $6.4 billion in volume in the quarter.

For the quarter, PayPal processed a total of 4.37 billion transactions, up 34%, and earned $6.03 billion in revenue, up 31%. DT

—John Stewart

PAYPAL'S ACTIVE QUARTER

(Active accounts in millions)



Source: The company

QUANTUM DIGITAL TRANSACTIONS

BY GIDEON SAMID
gideon@bitmint.com

LATE IN THE LAST CENTURY, there was lingering resistance from merchants to a new technology that shifted payments to credit cards. But early adopters were handsomely rewarded. For us today, the challenge is to welcome a remarkable new payment theater: the looming quantum.

It's quite a daunting challenge because quantum is veiled in an aura of mystery that makes everyone uneasy. Richard Feynman, the father of quantum computing, famously said that if someone tells you he understands quantum physics, you know right away that he does not know what he is talking about.

Quantum-computing technology is advancing on high gear. It stands to invalidate e-commerce as we know it because payment security today relies on the idea that computers cannot be faster than they are. But quantum computers are much, much faster.

After clearing away the debris of today's protocols, quantum will revolutionize efficacy, efficiency, and security, and accelerate progress in serving large social goals, helping, we can hope, the cause of international cooperation. My projection is that, in five years, or at most 10, the name of this publication will change to *Quantum Digital Transactions,* and the articles herein will be vastly different from today's offering.

Much as quantum is inherently mysterious, so is the future of its uses. But we have to put forth our best predictions and act upon them. I will give my take in upcoming columns. Here, I wish to focus on the core mystery of quantum.

Isaac Newton brilliantly used math to describe noticeable phenomena. His equations would predict how high and how far a ball is thrown, at what speed a wheel rolls downhill, and so on. Then, James Maxwell used math to describe electromagnetic forces. These were phenomena that were sensed without math, and then math described them.

But this paradigm broke down at the microscopic level. We no longer have a story we need to "math-quantize." All that we have is measurements, and indirect ones at that. We are hard-pressed to imagine a reasonable story to explain these measurements, but we can build a mathematical structure that takes in known measurements and predicts future measurements. The absence of a gratifying story connecting these measurements is the root cause of our unease about our dealings with the very small.

The fundamental idea of quantum occurred to Werner Heisenberg when he was walking one night in a dark park. He noticed a man walking under a lightpost. The man disappeared into the darkness, but a few seconds later reappeared under another lightpost, only to disappear again before being noticed under a third light. Based on this trajectory, Heisenberg could predict under which lightpost the man would show up next.

And then it hit him: "I have no idea what happens to the man between the occasions of visibility," he said. "My prediction of what I will see next is based on my records of past observations." This inspired Heisenberg to pioneer the notion of co-existence with the mystery of what happens between observations, and simply build the math that could predict with great likelihood what will happen next.

This coexistence with our ignorance of the reality between measurements is still the key to the new technology. But there is more. Quantum computing is probability calculus, not the deterministic calculus that Newton taught us. Since quantum is naked math without a story to animate the equations, it is necessary for us to tackle this math, at least in a conceptual way, if we want to feel at home in our evolving techno universe. I will take this up in upcoming columns. Stay tuned!

REGULATORS ARE ZEROING IN

BY BEN JACKSON

bjackson@ipa.org

THE REGULATORY CLIMATE for financial services is warming up, and even companies that have largely escaped notice are feeling the heat.

Regulators at the state and federal levels are taking a new look at everything from transaction routing to the ways companies market themselves. While it may look like they are dipping into regulatory arcana, recent enforcement actions and proposed rule changes could change the financial-services landscape.

The business model for financial-services companies focused on deposits and payments could face pressure as interchange threatens to become a hot topic. Late last year, a letter from The Clearing House, a trade association and payments company owned by some of the largest banks in the United States, asked the Federal Reserve to issue a new Frequently Asked Questions to clarify when a fintech or other third party is eligible for the small-issuer exemption to the Durbin Amendment interchange caps.

That seems to have presaged a wave of interest in the provisions of the Durbin Amendment. On May 7, the Federal Reserve Board proposed changes to Regulation II (Debit Card Interchange Fees and Routing) to require debit card issuers to allow merchants to choose from at least two unaffiliated networks for card-not-present debit card transactions. The Board said it felt the need to issue the rule because it had heard that online merchants were not getting a choice in transaction routing.

This may seem like a technical topic, but the costs of standing up a second network, and the potential reduction in interchange from competing networks, could eat into card issuers' balance sheets.

Additionally, retailers continue to look for ways to lower their payment costs, and they are turning to the courts. On April 29, the North Dakota Retail Association and North Dakota Petroleum Marketers Association filed a lawsuit in United States District Court against the Federal Reserve Board saying that the Board has not made sure that debit card processing fees are capped properly. In a local news report, Mike Rud, president of the North Dakota Petroleum Marketers Association, said the association would like to see debit card transaction fees go from 21 cents down to 3 or 4 cents.

At the state level, fintechs, which have largely gone untouched by regulators, have started to face scrutiny. Perhaps the best example of this is that in March, Chime Financial Inc. entered into settlement agreements with the California Department of Financial Protection and Innovation and the Illinois Department of Financial and Professional Regulation–Division of Banking.

Both agencies came after Chime because it was marketing itself as a bank, when Chime's accounts and cards are issued by the Bancorp. They independently found that Chime's usage of the words "bank" and "banking" in certain aspects of its business violated their respective state laws, and Illinois fined Chime $200,000. The company has agreed to stop marketing itself as a bank and clearly disclose its relationship with Bancorp.

All these examples are signals of a shift in the regulatory climate. It will likely warm up further when a new director for the Consumer Financial Protection Bureau and a new Comptroller of the Currency are confirmed by the Senate.

The financial-services industry needs to prepare for the storms that could result from these changes. As The Clearing House letter shows, the industry is not exactly on the same page about where things should go.

To stave off the worst-case scenarios, companies need to find common ground on what makes for good regulation and demonstrate to regulators and legislators—who will be focused more on helping individual balance sheets than corporate ones—how their products help consumers. DT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HOW THE PANDEMIC RESHAPED MERCHANT SALES

With less face-to-face sales in 2020, merchant acquirers quickly adapted to other selling methods. Some of these methods will stick around.

BY **KEVIN WOODWARD**

THE COVID-19 PANDEMIC has become known as the catalyst that gave contactless payments the adoption rate it once struggled to achieve. Now, a similar transformation appears to have happened in merchant acquiring.

As restrictions went into place last year, one sales method was quickly halted: face-to-face. But other methods, such as online and social-media marketing, gained importance. The question today is what methods seem like they will stick around once this pandemic—we can all hope—has been cocooned as a bad memory?

There's no doubt the industry adapted how it tries to reach merchants. "From a merchant-acquiring standpoint, how they're getting into some of these merchants, things have definitely changed," says Jared Drieling, senior director of market intelligence and insights at The Strawhecker Group, a research and advisory firm.

For example, when the pandemic emerged last year, it changed how Paysafe went to market, says Afshin Yazdian, chief executive of U.S. acquiring for United Kingdom-based Paysafe Group. "We really focused a lot of our attention, especially in the early days, on improving our infrastructure," Yazdian says.

GOING ONLINE

For Drieling, from his perspective at Omaha, Neb.-based Strawhecker, one of the big changes was the use of advertising and marketing through online channels, such as social media or developer platforms. "Probably most important here is that face-to-face selling changed quite a bit," he says.

Acquirers quickly adopted online methods to reach merchants. Face-to-face restrictions also meant merchants, especially small-business owners, turned to online resources to help them figure out how to navigate

the pandemic and keep their businesses viable.

That's where the advertising came in, Drieling says. Acquirers sought channels where merchants were. Payment companies like PayPal Holdings Inc. advertised on consumer outlets. As many bought paid search ads on Google, the importance of that channel increased, as did securing social-media advertising.

It was unheard-of decade or so ago for payments companies to buy national advertising spots or space, Drieling says. For many, Square Inc. might have been the most prominent payments provider seen in business-to-consumer advertising. "Typically, they've never heard of anyone but Square," Drieling says of small businesses.

Paysafe's marketing plan was retooled in 2020 to reflect the new way of selling, Yazdian says. "People were online more because they were at home," he says. While merchants may have sought out its services, many months of the pandemic necessitated a reactive approach.

"We definitely enhanced our entire online-marketing campaign, but the focus was not that different from what we would have done," he says.

Yazdian joined Paysafe in the throes of the pandemic in July. His goal was to simplify various aspects of how Paysafe does business and to improve the customer experience.

'I do see face-to-face coming back to the market. The process will be faster, cleaner, and more succinct.'

—**AFSHIN YAZDIAN**, CHIEF EXECUTIVE OF U.S. ACQUIRING, PAYSAFE GROUP

A SHORTER APPLICATION

On the merchant side, that translated into revamping the merchant application to enable quicker potential onboarding. It also meant adjusting the product mix to reflect merchant interest in mobile ordering, managing customer queues, and stronger reservations capability, Yazdian says.

The merchant-application review started with Paysafe staff learning what the experience was like to apply for a merchant account with the company, Yazdian says. To make the application shorter without increasing risk, Paysafe beefed up its automatic underwriting capabilities and boosted its risk teams, he says, adding, "It was a necessity."

Paysafe also created an online portal that made it easier to access the application and used terms were that were more mainstream.

That also meant adding more self-service tools, something especially useful for small businesses that might lack dedicated information-technology staff or budgets. And Paysafe revised its customer-service approach with a new phone system that resulted in more direct pick-ups of calls.

Ideally, when a merchant calls Paysafe a human will answer the phone, Yazdian says. "From a direct [sales] experience, it was about the customer experience," he says.

In the independent sales-agent channel, it was much of the same. While some focused on face-to-face sales, Paysafe helped them gravitate to phone or online channels, Yazdian says. Again, the merchant application was shortened by asking for less information up front. "All in all, our sales teams adapted incredibly well," he says.

CLOUD SOLUTIONS

The self-service notion, which many business owners became accustomed to as consumers when confronted with setting up their own mobile devices or activating an Internet service, extends into payments. Installations that used to be made with an on-site visit were adapted to meet the restrictions.

Typically, small businesses have 'never heard of anyone but Square.'

—**JARED DRIELING**, SENIOR DIRECTOR OF MARKET INTELLIGENCE AND INSIGHTS, THE STRAWHECKER GROUP

Many cloud-based point-of-sale system providers already used that model, but the pandemic prompted many others to adjust their processes.

"Think about how these cloud-based POS systems have been touchless from a maintenance standpoint," Drieling says. "They can be upgraded through the cloud." That means merchants don't have to pay for a technician to make an on-site visit, he says.

One trend that gained more ground was the adoption of a consultative sales approach, says John Jakobe, market intelligence manager at Strawhecker. "A lot of providers have seen the value of integrated payment providers," Jakobe says. "They have seen them become a sales channel."

It was happening prior to the pandemic, but the crisis sped up the shift to software companies having the conversation about payments in many instances. Payments originating from the software channel have grown at a rate of approximately 300% since 2017, outpacing most traditional channels by almost two to one, according to Strawhecker's Acquiring Industry Metrics database.

Prior to the pandemic, many payment providers sought merchants not only with face-to-face meetings, but by attending trade shows for various industries to meet merchants and developers catering to their segments. "That is no longer an option," Drieling says.

Now, many providers now will hire a firm like The Strawhecker Group to develop lists of prospects. "I get the feeling going forward we will see much heavier emphasis on the digital elements," says Drieling.

Bank and credit-union referrals also remained a valuable acquisition channel for payments companies. Merchants were looking for Paycheck Protection Program loans and guidance, and saw their financial institutions as resources, Drieling says, adding, "Banks still remain a very healthy, significant, and viable channel for acquirers."

A HYBRID MODEL

While it may be too early to know if face-to-face interactions will return to pre-pandemic levels, Yazdian believes a hybrid model will develop. "The general population enjoys face-to-face conversations," he says.

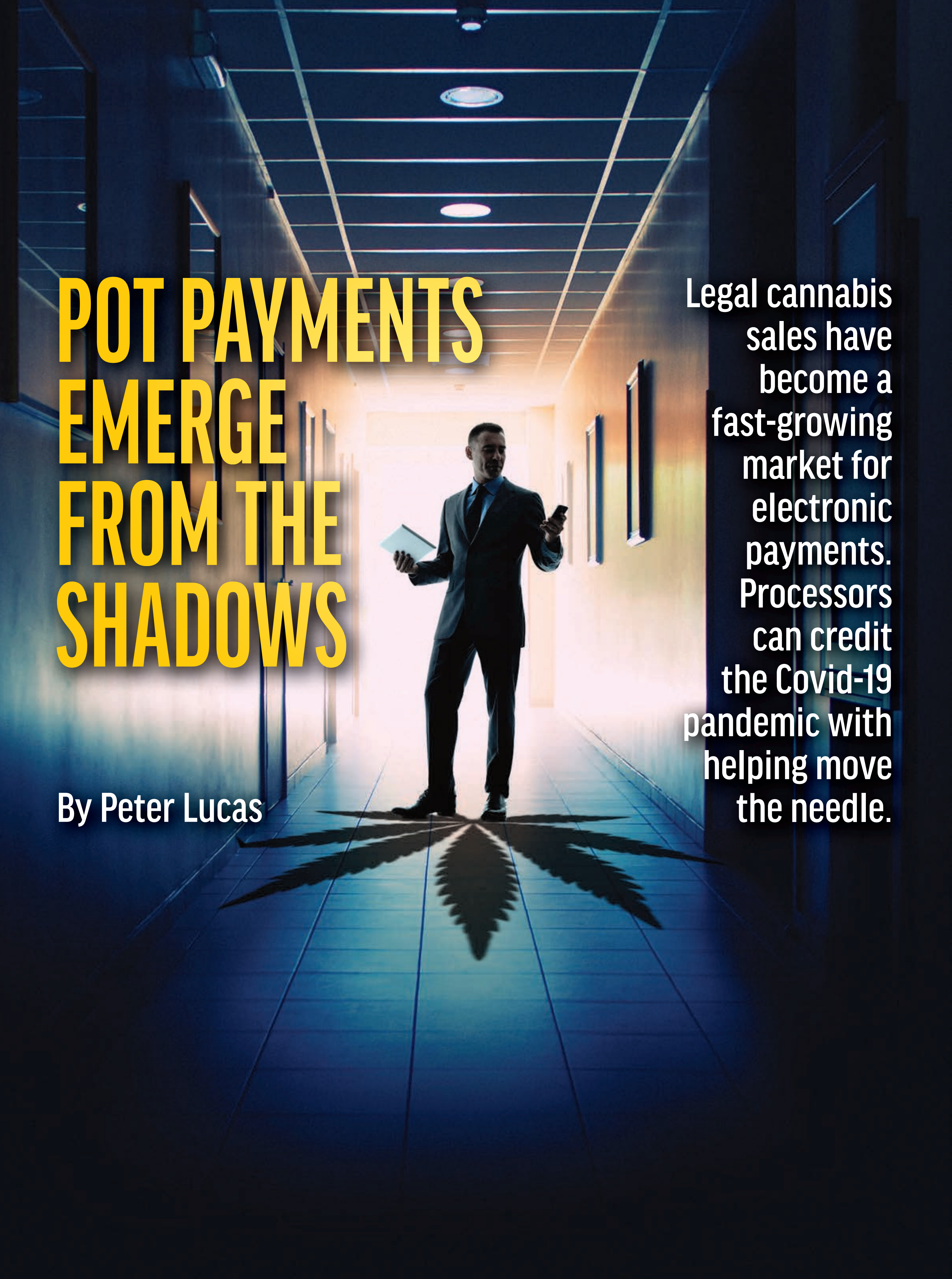
And, in financial transactions, some level of face-to-face interactions will be prevalent. "But the efficiencies we created during this process, like how quickly we can onboard, will continue to enhance that," says Yazdian. "I do see face-to-face coming back to the market. The process will be faster, cleaner, and more succinct."

That mirrors Drieling's position. "It won't ever go away completely," he says. Large enterprise merchants in particular value these type of interactions. They have large, complex payment systems and some merchant categories, like petroleum or the airline industry, are extremely complex he says.

But for less complex merchant segments, more focus on online sales and advertising may be here to stay. "Social media in itself, not only for the advertising, but direct selling, is becoming extremely popular," Jakobe says. "They will continue to be a large sales channel."

That can include third-party social media sites or a company's own Web site, among others, he says. Because so much data can be collected online, highly targeted advertising can be used to potentially reach merchants.

Whatever the size of the merchant, acquirers of all sizes have faced significant changes in how they find them. Some were already in the works prior to the pandemic, but other changes got a boost. "Covid caused us to move a little bit faster on doing things," Yazdian says. DT



POT PAYMENTS EMERGE FROM THE SHADOWS

By Peter Lucas

Legal cannabis sales have become a fast-growing market for electronic payments. Processors can credit the Covid-19 pandemic with helping move the needle.

JUST LIKE THEIR COUNTERPARTS in other merchant segments, legal cannabis merchants found themselves scrambling to embrace contactless payments options in the wake of Covid-19.

Over the past 16 months, and in increasing numbers, these sellers have been turning to electronic payment options, including account-to-account transfers over the automated clearing house, that do not run afoul of federal banking laws.

The latest rush stands in stark contrast to prior practice. Pot merchants have been primarily cash-only businesses because the federal prohibition on cannabis has kept financial institutions from offering them card-acceptance services,

But the pandemic led many of the states that have legalized the drug to declare these sellers essential businesses. At the same time, consumers wanted a contactless payment option that enables them to pay online from home for a delivery or curbside pick-up or to pay in-store through a mobile app.

Now, many cannabis-payments experts view the addition of electronic payments to dispensaries' online-ordering platforms as a logical next step for the industry to grow sales.

"Consumers have shown during Covid they are receptive to trying new payment options," says Dan Roda, chief executive for Abaca, a North Little Rock, Ark.-based provider of payments and financial services to cannabis merchants.

"The cannabis industry lacks conventional card-based payments," Roda adds, "so it makes sense for merchants to try alternatives because electronic payments can increase consumer spending power and improve operational security by reducing the amount of cash they handle."

If anything, increased customer spending power is a potent business case by itself. In June 2020, Abaca gathered data from about 15,000 transactions at one of its medical-cannabis merchants that had installed its AbacaPay app.

Abaca—which in addition to its own payment app supports cashless ATM and other well-established electronic payment options for cannabis merchants, such as CanPay—found the average ticket for non-cash transactions was $136.35, compared to $109.06 for cash, or 25% higher.

Overall, adding non-cash payments increased the merchant's total revenues during the test period by nearly $135,000, or 8.3%.

"When customers pay in cash, most of them make their spending decision at the ATM and not the point of sale," Abaca cofounder and chief strategy officer Brian Bauer said in a blog detailing the study.

"When presented with the option, about one-third of this dispensary's customers opted for cashless payments—just shy of 10,000 transactions were cash and almost 5,000 were cashless. [T]he surprising finding is how much more money the cashless customers laid out," the blog continues.

In 2021, total cannabis sales in the U.S. are expected to hit $19.6 billion, up from $16.3 billion in 2020, according to The Arcview Group, a San Francisco-based cannabis industry investment and research firm. In 2025, those numbers are projected to reach $33.9 billion. Just seven years ago, cannabis sales totaled a mere $3.3 billion.

THE AMAZON EXPERIENCE

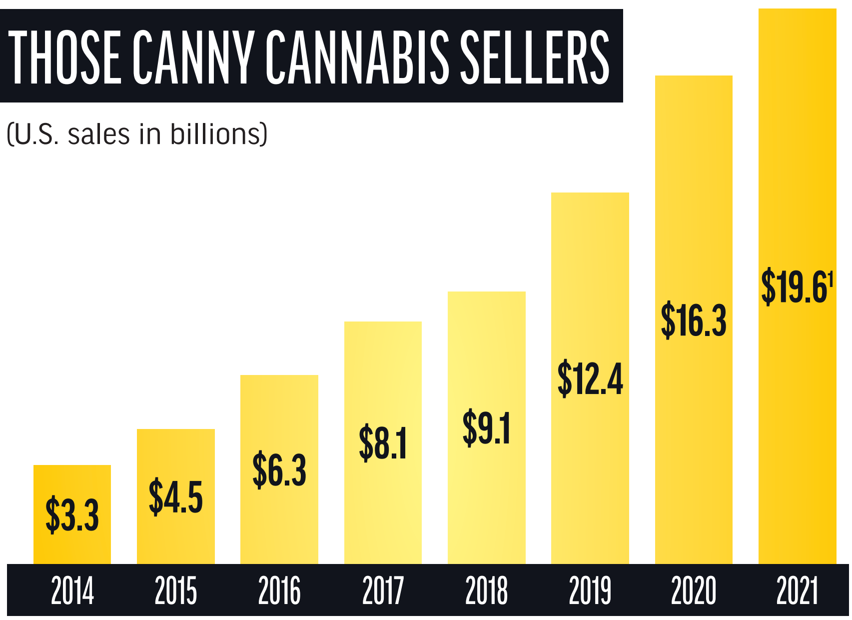
Given the rapid growth in legal cannabis sales in the United States and consumers' preference for non-cash payment options, it's not surprising payments providers are expanding their reach in this market.

Their approach includes deals involving online-ordering systems, mobile apps, and delivery services. Many of these deals were announced through press releases—quite a change from the pre-Covid era, when financial-services providers preferred not to draw attention to themselves because of the stigma attached to legal cannabis.

"Digital payment adoption by cannabis merchants accelerated during Covid, especially as many states

THOSE CANNY CANNABIS SELLERS

(U.S. sales in billions)



1. Projected Source: Arcview

mandated curbside pickup," says Tyler Beurlein, chief revenue officer for Hypur Inc., a Scottsdale, Ariz.-based provider of payment and banking technology. "E-commerce is also here to stay and is the future of this merchant segment because mainstream consumers that buy cannabis want the same kind of e-commerce experience they get from Amazon."

In February, Hypur partnered with mobile-app provider Strain to integrate Hypur Pay in Strain's app. The Strain app, a white-label solution for cannabis merchants used by 355,000 consumers and 250 dispensaries, allows consumers to shop online.

With the addition of Hypur Pay, Strain users can pay for their purchases through the app either in-store or prior to pick-up. Hypur Pay facilitates payments by directly debiting a consumer's account and sending the funds straight to the merchant account.

Cannabis merchants can also use the Strain app to enroll customers in rewards programs, send promotional offers, and push SMS marketing messages to app users when they are near a dispensary.

"The ability to pay through the app adds value for dispensaries," says Strain chief executive Manuel Ramirez. "As we gained more customers, we saw the need to close the gap between online ordering and payments. With our app, cannabis merchants can accept orders and payment, market to their customers, and provide customer service through a single point of integration, which shortens their technology stack."

Strain's app also captures consumer-behavior data, such as products viewed during a session, purchase frequency, and average spend. Merchants can also conduct customer surveys through the app to receive feedback on customer satisfaction and create customer profiles for marketing purposes.

About 70% of a dispensary's customers that shop online will move to Strain's app for ordering, says Ramirez. Strain is also developing a customer relationship-management application for cannabis merchants that it expects to release later this year.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'THE NEXT WAVE'

Other fintechs striking deals this year with cannabis-related technology providers include Kirkland, Wash.-based POSaBIT Systems Corp. and Chicago-based AeroPay.

POSaBIT's linkup is with online-ordering platform provider I Heart Jane to add payments. For cannabis merchants, POSaBIT offers several payment options, including POSaBIT ACH. That option allows customers to log in and store their banking information within POSaBIT's payments portal for in-store and online payments.

'We want to be ready to offer cannabis merchants a business model that includes multiple payment options.'

—RONNY YAKOV, CEO, OLB

POSaBit, which declined to comment for this story, also offers a debit point-of-banking option that acts as a cashless ATM at the point of sale. Point-of-banking solutions allow customers to purchase goods or services by inserting a debit card in a POS terminal, then entering the amount of the transaction and their PIN.

Instead of dispensing cash, a point-of-banking application generates a receipt for the transaction as funds move from the consumer's deposit account linked to her debit card to the merchant's account.

In January, AeroPay, which also refused to comment, partnered with Blackbird, a cannabis-software and -delivery company, and in February linked with Olla, an e-commerce platform built specifically for cannabis merchants. The connections enable payments through both platforms via bank-to-bank transfers.

Consumers using Blackbird will be able to prepay online at the time of checkout using AeroPay for curbside pickup or delivery orders in states where legal cannabis delivery is allowed, such as Nevada and Florida.

Blackbird provides a white-label online-shopping application for cannabis merchants, It also operates an online marketplace called BlackbirdGo in select markets for consumers who want to place orders for delivery or curbside pickup.

Olla's platform supports online pre-ordering, curbside pickup, home delivery, and in-store ordering. In 2020, more than $250 million in online cannabis orders were placed through Olla's platform.

"E-commerce is seen as the next wave in the legal cannabis industry," says Abaca's Roda. "Practically all cannabis merchants are developing an e-commerce strategy to make it easier for customers to pay and market to them."

GETTING BANKS' ATTENTION

Another fintech announcing payment options for cannabis merchants this year is OLB Group, Inc., which has partnered with a marketing firm that offers a white-label rewards programs to more than 500 cannabis merchants.

"They came to us looking to add a payment option," says OLB chief executive Ronny Yakov, who adds OLB plans to offer cannabis merchants a prepaid card at a future date. "The sense we are getting is the market for legal cannabis is opening up more and we want to be ready to offer cannabis merchants a business model that includes multiple payment options. We already provide payment processing to CBD merchants."

CBD, or cannabidiol, is a chemical in the cannabis sativa plant that is not psychoactive, and therefore does not get the user high. Fourteen states have legalized CBD products.

Besides credit and debit card acceptance, OLB's SecurePay payment gateway supports QR codes, mobile-app solutions such as Apple Pay and Google Pay, ACH account-to-account transfers, and cryptocurrency.

In all, 36 states have legalized cannabis for medical use, and 16 plus the District of Columbia have legalized it for adult recreational use. The trend is not unlike how alcohol prohibition fell in the United States almost a century ago.

"The biggest driver in overall sales is new states legalizing," says David Abernathy, principal for Arcview's management-consulting division. "Legal cannabis sales are also eating away at the illegal market, which represents between $60 [billion] and $80 billion in annual sales. We don't expect a plateauing of legal sales in the next five years, and would be surprised if we saw it in 10 years."

Ultimately, Abernathy predicts legal cannabis sales will eventually displace the bulk of illegal sales. If enough illegal sales are converted, legal cannabis could easily become a $100 billion industry within a decade.

"Once that happens, it will be a large enough market to catch big banks' attention," Abernathy adds. "The reason cashless-payment providers are gaining traction is the difficulty cannabis merchants have getting payment services from banks."

COMPLIANCE ISSUES

Indeed, the financial institutions that are working with fintechs to provide banking services to cannabis merchants are typically small banks and credit unions. These institutions are less averse to servicing high-risk merchants than are large banks, cannabis-industry experts say.

The compliance issues that surround financial institutions servicing the legal cannabis market are strict and cumbersome. For example, they are required to file a suspicious-activity report for every cannabis-related transaction they handle. As a result, the compliance issues are not worth the cost and operational headaches for big banks given the size of the current market.

'The big banks don't see legal cannabis as large enough to move the dial because they can make more money in credit cards.'
—**BOB CRAIG**, CHIEF EXECUTIVE, PAYQWICK INC.

"The big banks don't see legal cannabis as large enough to move the dial because they can make more money in credit cards, for which they already have the supporting infrastructure in place. With cannabis merchants, they'd have to build that infrastructure," says Bob Craig, chief executive for PayQwick Inc., a Los Angeles-based provider of treasury-management services to cannabis merchants.

PayQwick, which launched in 2014 and serves more than 400 cannabis merchants, initially offered a cashless-payment option, only to drop it after several years because of wavering support for the product among processors.

PayQwick works with multiple financial institutions around the country to provide treasury management and banking solutions to cannabis merchants and their suppliers.

"We didn't get a lot of assurances that our merchant accounts wouldn't be suddenly shut down, even though they were compliant, so we began moving away from consumer payment options to focus on treasury management," Craig adds. "Our focus now is to help cannabis merchants digitize cash to pay their bills."

'GETTING MORE TRACTION'

Despite the inroads fintechs are making with non-cash payment options in the cannabis market, there are still providers looking to mislead the card networks by veiling the true identity of their cannabis merchants, some observers say. That, cannabis-payments experts say, not only gives the industry a black eye, but invites tighter regulation.

"There is a lot of money that can be made short-term by processors gaming the system, but we still live by the rule that dispensaries shouldn't have to hide their identity for payment processing," says Dustin Eide, chief executive at CanPay, which provides a mobile-payment app to more than 700 merchants in states where cannabis has been legalized.

"Cannabis merchants are definitely seeing the value in digital payments and e-commerce now," he adds. "That's why they are getting more traction." DT

THE DOUBLE PAYOFF IN CONTACTLESS PLASTIC

The transition to contactless payments offers a rare opportunity to meet another priority by ushering in sustainable payment cards.

BY **GUY DIMAGGIO**

Guy DiMaggio is senior vice president and general manager of Secure Card and Sustainability Solutions at CPI Card Group.

THROUGH THE COVID-19 PANDEMIC, business operations and consumer interactions with their finances have fundamentally changed. The past year has seen a major acceleration in the shift away from cash, with the pandemic driving industries and consumers alike to ramp up the use of contactless options for a touch-free payment experience.

Periods of drastic change like these present potent opportunities to drive other evolutions that create an emotional response. One such opportunity is to prioritize a move to more sustainable products, such as more eco-focused cards.

The challenging scenarios fueled by the pandemic have many major brands and organizations re-assessing where their values line up. Over the past year, sustainability and environmental justice have seen major commitments from top business leaders, from the use of green energy to a concerted focus on ESGs (environmental, social, and governance priorities). Initiatives like community development, pollution and waste management, and the mitigation of carbon emissions are all examples of ESG considerations.

Major consumer-product companies like Unilever and P&G have led sustainability efforts like creating goals for net-zero emissions for their products from cradle to shelf, committing billions to climate-friendly initiatives, and moving away from PVC in their packaging.

Companies like Dell, Ikea, and HP, as part of the NextWave initiative, have also committed themselves to keeping plastics in the economy, and out of the ocean, by establishing the first global network of ocean-bound plastic supply chains.

Companies across the financial-services industry have also committed to sustainability. Emerging digital banks like Unifimoney have embraced eco-focused initiatives, including the adoption of payment cards and products that use upcycled materials.

Other major financial institutions and global banks have committed to sustainable finance, allotting billions to investing, financing, and advisory activities to help customers accelerate the adoption of clean energy, sustainable transport, and responsible waste management, among other initiatives.

CALL TO ACTION

Over the past year, there's been a call to action from consumers hoping to see aggressive action from both public and private institutions on the environmental front. In a recent Boston Consulting Group report, 87% of consumers surveyed said companies should integrate environmental considerations into their products, services, and operations to a greater extent than they have in the past.

By doing what consumers demand, even when it is more difficult, businesses are viewed as innovators that are working for the greater good. The tide is turning as companies realize the massive impact and public support that comes from investing in environmental initiatives in an effort to become more sustainable.

In a time of major disruption, it's an encouraging sign that companies are continuing to take a stand to prioritize sustainability and create frameworks for others to follow in their footsteps.

The increased prevalence of contactless-payment options is another good example of responding to consumer demand and innovating for the greater good. Contactless payments were already on the rise prior to Covid-19. But as concerns over the safety of touching card readers or point-of-sale terminals rose, so did the desire for cards that you can use to wave and pay. According to a recent survey from the National Retail Federation and Forrester, the acceptance of contactless cards rose to 58% of respondents in 2020, up from 40% in 2019. Of the retailers that accept contactless payments, 94% expect the increase to continue over the next 18 months.

As we continue to settle into our new normal, consumers may come to expect contactless cards as a standard offering from their financial institution. Visa's "Back to Business" study noted that nearly two-thirds of consumers globally would switch to a business that installed contactless payment capability over an existing relationship (with the assumption that factors like price, selection, and location are equal).

A SUSTAINABLE OPTION

While contactless payments have steadily become a higher priority for financial institutions, the pandemic has heightened the necessity to create contactless options for payments. As institutions capitalize on this need, there's an opportunity to make sustainability a part of transitioning card portfolios to contactless cards. This will need to be a priority for financial institutions that want to retain and grow their customer base.

The push to create payment products in a more sustainable manner has been coming to a head in recent years. The United Nations, for example, created the Principles for Responsible Banking, where over 200 banks have joined the movement to start a new future for banking.

One of the ways that financial institutions can demonstrate a commitment to sustainable practices is through the use of payment cards made with recycled or reclaimed materials, like ocean-bound plastic and recycled PVC. CPI Card Group commissioned a survey, conducted by an independent research firm, that found that 94% of consumers say they are concerned about the amount of plastic waste in the oceans.

Earthwise cards from CPI Card Group are manufactured using at least 85% upcycled plastic.

Further, some 87% of respondents find the idea of an ocean-plastic card appealing, and 53% are willing to switch to another financial institution offering cards with the same features and benefits.

If consumers are willing to switch institutions for contactless card options, adding cards made with eco-focused materials to the mix could offer a competitive differentiator.

Financial institutions have an opening to introduce products and services that resonate with environmentally conscious consumers. It's an opportunity to simultaneously embrace payment card options that are contactless and reduce first-use plastic. Now, it's clear that there's no better time to drive the convergence of two trends that have risen in prominence over the past year—and meet growing consumer demand and help create a healthier planet in the process.

Historically, in times of crisis, companies need to invest to "recover better," as opposed to just trying to get back to business as usual. By leading the way for others in the industry to follow, we'll be able to expand our capabilities and show true progress, despite the hurdles caused by the pandemic.

And, by doubling down and investing in more sustainable payment products, the financial-services industry can serve as a pioneer in welcoming a new age of eco-focused change and innovation. DT

DiMaggio

'There's an opportunity to make sustainability a part of transitioning card portfolios to contactless cards.'

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What if two became four?

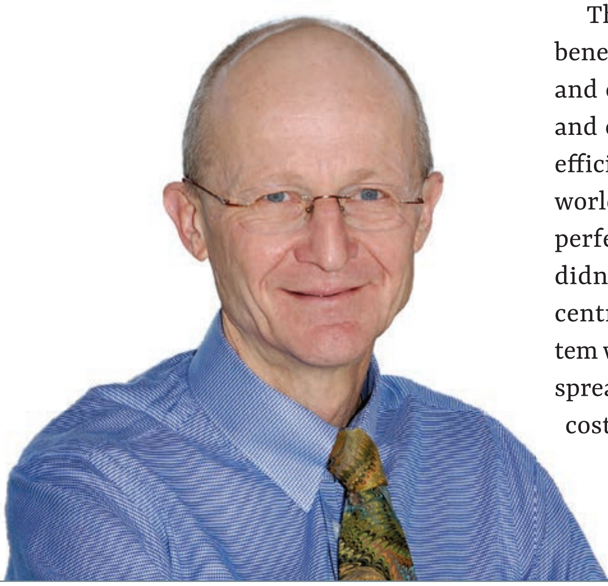
endpoint

BE CAREFUL WHAT YOU WISH FOR

A brief thought experiment illustrates the benefits—and risks—of breaking up the dominant network duo.

BY **ERIC GROVER**

Eric Grover is principal at Intrepid Ventures, Minden, Nev.



BANK CARD NETWORKS Mastercard and Visa were the 20th century's greatest payments innovation. Today, there's a worldwide competitive patchwork of hundreds of "card" networks and alternative payment systems. But Mastercard and Visa are the only two genuinely global retail-payment networks.

They've been subjected to what is now a decades-long barrage of antitrust investigations, regulation, and lawsuits stemming from concerns that payment-network markets are insufficiently competitive and the two giants enjoy too much market power.

Nabanco's 1982 antitrust suit against Visa was the opening salvo. Years later, a fusillade of suits alleging that interchange fees violated the Sherman Antitrust Act caused the banks that owned Mastercard to spin it off in a watershed 2006 IPO.

There are tradeoffs between the benefits of more payment networks and competition, on the one hand, and consolidation and greater cost efficiencies, on the other. In a static world, where management enjoyed perfect knowledge and monopolies didn't abuse their power, a single, centrally engineered payment system would arguably be ideal. It would spread one set of substantially fixed costs across all payments.

However, the world isn't static. No management, however bright, can match the market's vast, distributed knowledge and dynamism. Also, men aren't beneficent angels. Unchecked by competitors, monopolies are less attentive to customers, costs, and service enhancements, and they often charge more.

Free-market competition is the most vigorous and ruthless regulator of value, continuously re-allocating resources from underperforming enterprises to those maximizing value. Hence, more cross-border and national payment-network competition would increase value and innovation worldwide.

COMPETITIVE JUICES

Let's engage in a thought experiment. Suppose that, to end antitrust risks, Mastercard and Visa each split in two, creating four global payment networks. While each would process fewer transactions, they'd have substantially the same assets, excepting brands.

Critically, all four newborn networks could inherit the same global-acceptance network. Cardholder counts and spend could be split in half, with each network retaining a critical mass of issuer licensees planetwide. Each clone could inherit a copy of all delivery systems, software, and intellectual property. Personnel would be divvied up to ensure each clone started with comparable talent.

KEEP YOUR CARDHOLDERS: COMPETE WITH BUY NOW, PAY LATER POPULARITY

By Anita Lemaire, Product Executive, Global Cards and Payments, FIS

The buy now, pay later (BNPL) market is expected to grow 181% by 2024, and will account for 13% of all global e-commerce payments that same year, according to the 2021 Global Payments Report by Worldpay from FIS.

These post-purchase installment programs aren't a new concept, but the ease of use, flexibility and mutual benefit they bring to various phases of the value chain have made them one of the fastest growing segments in payments. To compete with alternative point of sale (POS) installment loan providers like Affirm, Klarna and Afterpay, and direct competitors like Chase, Citi and American Express which all offer flexible repayment plans, credit and debit issuers must respond. Here's a closer look at what's driving BNPL popularity.

CARDHOLDERS WANT TO CONTROL THEIR FINANCES

When FIS surveyed 15,000 consumers around the globe in June 2020, respondents between the ages of 18 to 39 were particularly receptive to the idea of paying with installments over time, for a few reasons:

- Value of having control over their money
- Want to track spending
- Desire to avoid going into unmanageable debt

Nearly half of consumers across all generations said they were comfortable taking on debt they could pay off over the short term, and Gen Y and Gen X (consumers between the ages of 24 and 54) were the most likely to agree with the statement.

Price point also matters when it comes to the likelihood of using BNPL options. Half the consumers surveyed would likely use BNPL for a purchase under $250, but the figure dropped to 41% for a purchase between $250 and $999. For purchases of more than $1,000, just 31% of respondents would use a post-purchase installment plan or BNPL option.

Despite research conducted by The Ascent revealing 31% of respondents had incurred some type of late fee associated with a BNPL offering, the illusion of control is overriding the actual cost of using such a program when repayment terms are not followed.

CREDIT CARD OWNERSHIP HAS DECLINED WITH THE PANDEMIC

Except for senior millennials (ages 29 to 39), credit card ownership dropped in every age group between April 2020 and February 2021, according to FIS research of 1,000 Americans conducted in February 2021. Non-card ownership was particularly prevalent among Gen Z consumers (ages 18 to 23). In April 2020, 31% of Gen Z respondents did not own a credit card. By February 2021, the number jumped to 51%.

Reasons for this fall off might include an increased use of digital payment methods that eliminate the need for credit cards. Other reasons to blame could be declined credit card applications, or suspensions of credit card use due to worsening financial conditions. In fact, The Ascent's research showed BNPL usage jumped 62% between July 2020 and March 2021 among GenZ users.

BUY NOW, PAY LATER OFFERS ALSO APPEAL TO DEBIT USERS

There's debate on the need to regulate BNPL providers, so they do not become yet another form of predatory lending for consumers who may not understand the terms they're agreeing to. Yet these offerings do provide borrowing options for those who may have none. For example, when Capital One said it would no longer approve point of sale lending transactions on its credit cards due to excessive risk, Afterpay CEO Nick Molnar told Pymnts.com the decision wouldn't impact his business. Why? According to Molnar, 90% of Afterpay's transactions are paid for with debit cards.

LET'S REIMAGINE CARD PAYMENTS

Issuers cannot disregard BNPL as a passing trend or fail to address consumers' overall response to them. With FIS BNPL, you can give cardholders the option to convert their credit and debit purchases into installment plans, for flexibility when making large purchases.

FIS

Brands would be the thorniest issue. Significant pieces of Mastercard's and Visa's $378-billion and $489-billion enterprise values, respectively, consist of brand equity. Their powerful brands convey the payment networks' promise to consumers, merchants, and banks worldwide. They couldn't be easily divided.

Two of the four networks, therefore, would have to craft new brands while finding a way to leverage, and yet distinguish themselves from, the existing brands—a huge undertaking fraught with risk. And, they'd have to be compensated.

While the new global networks' marginal payment costs, like those of the old, would still be zero, average transaction costs would initially increase.

The offsetting benefit would be greater payment-network competition and innovation. History has shown us that, after being unshackled by their IPOs from bank-association governance, Mastercard and Visa became more enterprising.

Splitting them up would further fire their competitive juices. Visa, Visa's clone, Mastercard, and Mastercard's clone would compete more fiercely planetwide for cross-border and national payments and would likely take different approaches. They'd be each other's most formidable rivals in many markets.

One or several of the new global payment networks might focus more on mobile network operators, tech platforms, penetration of national markets, digital currencies, or adjacent business-to-business and interbank payments. Several might become less (or more) woke. To gain share, several might get more aggressive on price; others might focus on boosting issuer value.

PERSISTENT PROTECTIONISM

Still, while creating four competing global payment networks would put to bed most genuine antitrust concerns, protectionist sentiments wouldn't be assuaged. EU regulators would still stew in their euro-mercantilist juices because the four pan-European payment networks would be American.

Chinese regulators would remain keen to bar American payment networks, including PayPal, American Express, and Discover, from penetrating their domestic market.

To be sure, US-domiciled payment systems have been used as instruments of American foreign policy. To differentiate itself, one of the new networks might move to a more neutral jurisdiction, like Switzerland.

U.S. antitrust cases against the payment networks would become difficult, if not impossible, to make. When payment systems are viewed holistically, it has always been difficult to argue that Mastercard and Visa harmed consumers. With six national credit card networks and a dozen-plus national debit networks, the contention that the market wasn't sufficiently competitive would fail on its face.

There'd be two additional U.S. debit networks with signature-, signatureless-, PIN-, and PINless-authentication. There'd also be two more suppliers of tokens and EMV application identifiers. Debit-routing competition, consequently, would intensify.

Payment network competition in the United Kingdom, where Mastercard and Visa currently enjoy a 98% combined share, would become fiercer.

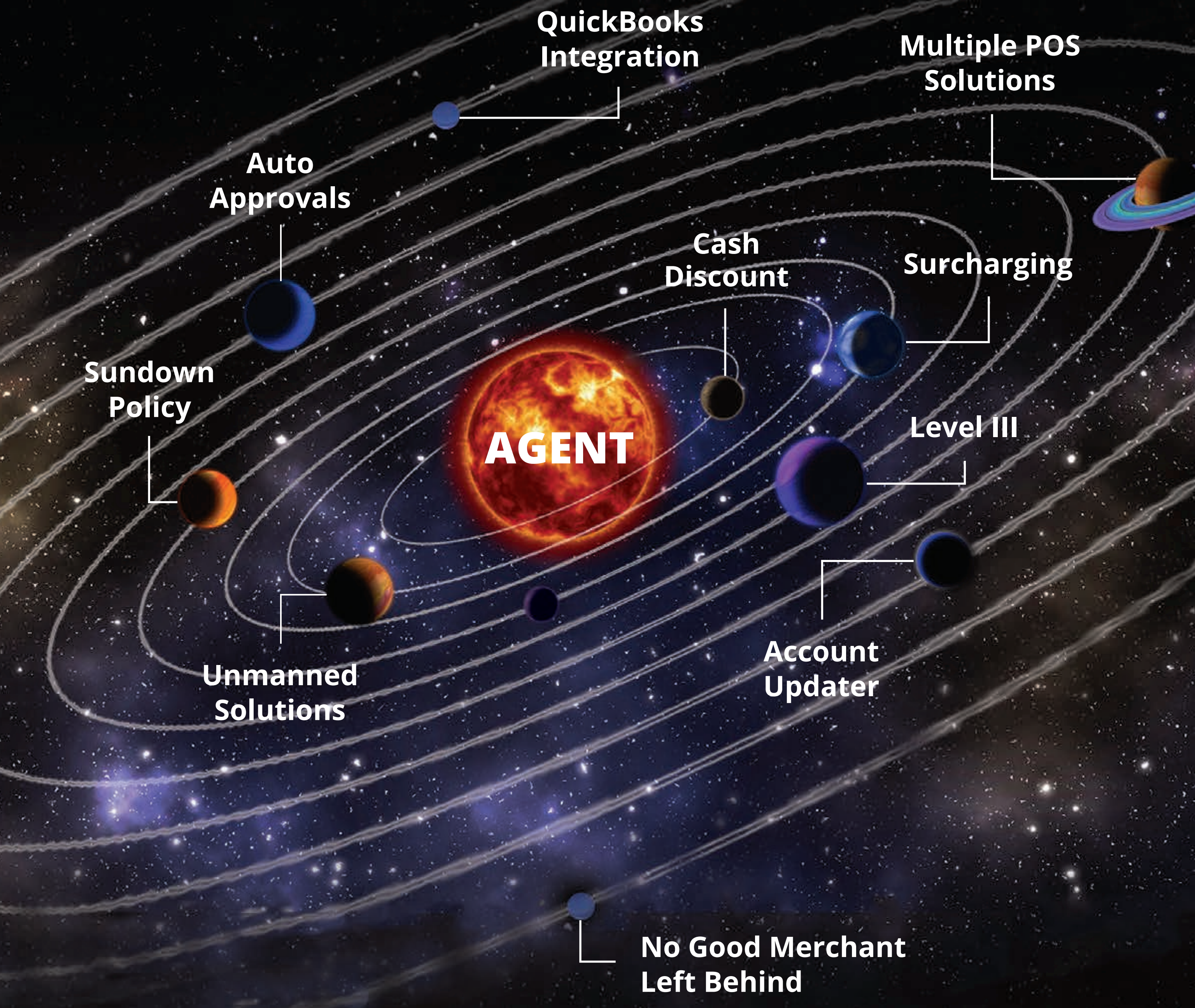
FIRE IN THE BELLY

While competing payment networks might welcome Mastercard's and Visa's breakups and the short-term benefit, long-term they'd rue the day. Each 50%-revenue-diminished network would have more competitive fire in the belly.

Intensified competition for cross-border and national payments worldwide would spur electronic payments growth and innovation. That would spur value creation and economic growth for consumers, merchants, and banks.

However, with Mastercard's and Visa's stellar post-IPO performance, the chances are slim shareholders would seriously entertain, much less execute, cleaving these systems in two. DT

DOES YOUR PROVIDER PUT YOU IN THE CENTER OF THEIR UNIVERSE?



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