CAPCO

COVID-19:
WINNERS AND LOSERS IN PAYMENTS

INTRODUCTION

The coronavirus pandemic has demonstrated just how vulnerable our business and financial services landscape is, with the world now preparing for its first recession triggered solely by a pandemic since 1870.[1] We know that business recovery will be slow and could continue to be painful for many, and so financial institutions must make payments as seamless as possible to facilitate circulation – and remain relevant. This will be a war, and in every war, there is always something to gain and something to lose.

SUMMARY

As banks give consideration to segment propositions and product features, they should take into account the winners and losers in payments. The consumer is increasingly comfortable with formless, tokenized, contactless transactions, as bricks and mortar and travel have lost out to online and stay at home. Speed remains important as does the current account, so faster payment systems (FPS) and BACS are still strong. We believe that cash has become less popular as a result of Covid-friendlier alternatives. Credit cards and facilities should also be concerned about the adoption and penetration of point of sale credit and BNPL into the mainstream financial behavior of the online shopper. Ultimately, any sharp customer proposition should bear in mind that the consumer and merchant have changed, or at the very least have adopted new ways of paying tactically and quickly.

LOSERS

1. Bad news might travel fast, but FX, leisure, hospitality and travel-related card businesses won't

The impact of lockdown has had a detrimental effect on personal and business travel, with the airlines and tourism industry particularly bearing the brunt. The outlook for recovery doesn't look positive; with many airlines now fighting bankruptcy[2] and the International Air Transport Association having forecasted that 2019 passenger demand levels will not be exceeded until 2023.[3]

It is no surprise that COVID-19 pressures have had severe repercussions for foreign exchange (FX) transactions, and revenues and profits for card and payments providers, and those that focus on the travel industry therein. Back in March, WEX Inc. announced it had cut its Q1 revenue outlook[4], and then in May backed out of a $1.7 billion acquisition of two UK-based travel payment businesses.[5]

So, what should these companies do? Just as we've seen airlines such as Ryan Air providing credit vouchers rather refunds (a move we're also seeing by London restaurants)[6], perhaps struggling financial providers in this space can look to similar incentives.

2. Cash comes with a health warning …. Literally!

The cash supply chain has slowed down dramatically since the coronavirus crisis took hold, with reports of cash going without the green for an average of 44 days.[7] While cash is not proven to carry coronavirus, financial and retail industry bodies certainly encouraged contactless use by increasing the limit on contactless spending from £30 to £45, just in case. It certainly helped, because at the end of April cash use had reportedly declined by 60 percent in the UK.[8] Last month, Barclays then reported that 90 per cent of face-to-face transactions were now made using contactless payments.[9]

Although cash has not lost its value, there is a close relationship between micro and SME businesses and the velocity and liquidity of cash. There have also been concerns about vulnerable people in society, such as the disabled and elderly, who may struggle with digital payment methods[10] and could also become more susceptible to fraud if pushed to use them. In addition, The World Bank is now expecting remittances to drop by 20 percent, which would signal the largest single-year decline in remittances in the past century.[11]

3. Businesses aren't so cash friendly either

Businesses heavily reliant on cash such as the food, hospitality and trade industries are likely to be getting their revenue through a higher proportion of card transactions as a result of COVID-19 cash phobia. Indeed, at the start of the UK lockdown, ATM transaction volumes fell as much as 62 per cent year on year, according to data from Link, the UK's cash machine network.[12] As a knock-on effect of contactless payments, these businesses are probably incurring fees and some delay in accessing funds.

Meanwhile, for those businesses already reliant on card and contactless payments, such as online businesses, the increased credit risk may push up capital and collateral requirements from acquirers.

Also not so cash friendly, are fraudsters. With new security checks such as strong customer authentication (SCA) being delayed until March 2021, and Confirmation of Payee (CoP) until the 30th June 2020, fraud is being touted as the 'hidden cost of coronavirus.'[13] From the end of February to the end of March, financial crime rose by 667 percent;[14] and in the past two months, more than 2,200 people have fallen victim to coronavirus-related scams.[15]

4. Plastic is not fantastic

There was already a perception that credit cards were not as popular with younger generations as they used to be. For millennials and Gen Z, debit, digital wallets[16] and buy now pay later (BNPL) schemes like Klarna are gaining prominence. Since the COVID-19 lockdown took hold, almost a quarter of 18 to 24-year-olds (23 percent) have been using BNPL to fund purchases.[17]

For those who do hold a credit card however, April's lockdown was an opportune time to pay off debts and loans, with the news that consumers collectively reduced UK credit card debt by £5 billion, more than double the previous record net repayment of £2.4 billion set a month earlier.[18] It seems that 'transactors' will form a larger percentage total of credit spend in 2020 as a result of these consumers refocusing and reducing their spending habits.

Although it is fair to expect less credit card use for the remainder of 2020 given the long-term impacts of COVID-19 and payment holidays on loans and mortgages, we might see a higher number of account holders with revolving balances, persistent debt and eventual defaults. Banks, loan providers and credit card companies may have to devise more flexible and affordable repayment plans to get customers back on track.

WINNERS

1. E-commerce is booming (unsurprisingly)

For card networks, acquirers and banks, there has been a significant increase in online spending which has helped to offset the impact of the decline in lucrative FX. However, there have been sharp falls in point of sale transactions and therefore a net reduction in payment volumes.

A report by Visa has found that nine in ten consumers (89 percent) have used online shopping since the UK's lockdown restrictions came into force, that 31 percent have used e-commerce to purchase something for the first time, and a whopping 74 percent will make it a permanent habit after lockdown lifts.[19] Further bad news for UK high streets.

2. … As is contactless (obviously)

Like online transactions, contactless payments have also had a good spell, with a 44 percent increase in tap-and-pay transactions since the week of 23 March.[20] Sixty-two percent of consumers over the age of 65 are now using contactless methods (as well as record numbers moving to online banking).[21] This will have been partly driven by contactless spending limits being increased on 1st April, and aforementioned fears of virus spreading from banknotes.

The tokenized 'Pays' have also been positioned to do well. The customer experience is straightforward, the qualities of contactless are augmented by additional features, and the position of the phone as man's new best friend is unchallenged.

We expect the strength of contactless to continue as lockdown eases, taking transactions away from cash and traditional chip and pin payments. As time goes on, it will be harder for businesses to justify not accepting card payments or upholding a minimum payment threshold. 7.4 million people are already living cashless in the UK already, just another 59.2 million to go![22]

3. Digital wallets, in-app purchases and tokenized payment services could be in their heyday

In a health crisis where convenience, safety and speed are of utmost importance, is it any surprise that digital payments providers and services such as 'click to pay' and tokenized card payments are having a successful time of it? Food delivery businesses with in-app purchase systems such as Uber Eats and Deliveroo have not only been able to continue through lockdown but thrived off their commissions.[23] Meanwhile, Visa Token has been gaining significant traction in the US, and reduced fraud rates by 26 percent.[24]

Crypto payment providers are also having their moment. Wirex, a UK crypto-mobile payments platform, reportedly gained 60,000 new customers at the start of the COVID-19 outbreak;[25] and down under, Centrapay, a digital asset integrator, signed agreements with Coca-Cola Amatil to help facilitate cryptocurrency payments from vending machines using QR-scanning.[26]

Although not crypto-friendly yet, Paypal are similarly going down the QR-route to drive transactions during COVID-19.[27] In April, the fintech reportedly saw a 22 percent increase in processed payments year-over-year and then on May 1st alone broke Black Friday and Cyber Monday records.[28] It's clear that it pays to have good UX!

4. A rise in point-of-sale credit and BNPL

What's not to like about a card-free, 'interest-free', smooth point-of-sale credit purchase? Well, 7.85 million US Klarna users seem to agree with the principle; and retailer signups have risen by 20 percent in the UK over the last two months.[29] BNPL schemes like Klarna and ClearPay are reportedly growing at 39 percent a year and are set to double their market share by 2023; growing twice as quickly as bank transfers and more than three times the rate of annual growth of digital wallets.[30]

5. Faster payments and BACS

As speed of payment has become more important, the volume of government disbursements increased, and more consumers and businesses chose to settle bills online, the average daily value of Faster Payments transactions in the UK rose by over 10 percent from Q4 2019 to the end of Q1 2020.[31] With BACS, which is slower and often less expensive than FPS, daily transaction values have marginally increased in the same period.

6. Cheques are not dead yet

While cheques are considered an old-fashioned payment method (well, over 361 years, to be exact) some banks have seen a resurgence in the number of cheques being digitally deposited during lockdown. Back in April, HSBC UK reported an increase of 30 percent.[32] Their days might still be numbered (the Bank of England reported a steady decline in cheque daily transaction values from 2019 to the end of Q1 2020)[33], consumers appear to still appreciate a variety of payment methods.

WHAT NEXT?

In 1932, Austrian economist Joseph Schumpeter defined innovation as the sum of invention and adoption.[34] Fast forward to 2020, it certainly seems like the coronavirus pandemic has accelerated the adoption of established payment solutions to enable further innovation in financial services. Although we can't say for certain, it has also driven cash use further towards obsolescence a lot faster than expected; so much so we believe it could accelerate UK Finance's initial forecasts about a diminishing cash society in 2027 (such as the assumption that 36 per cent of all payments across the UK will be contactless)[35]. We might very well see an increase in cash-use again after the pandemic, but we expect this to be short-lived along with cheques, as their demise is clearly part of an existing trend towards more seamless alternatives.

Now we have seen customers' acceptance of digital payment methods, providers should capitalize on this accelerating multi-generational shift, and continue plugging away at the gaps to ensure a safe, secure and frictionless customer experience. For example, the success of Paypal during COVID-19 has shown just how much it pays to put a good UX layer over the top of clunky card and bank payments mechanisms (thus removing the need for a 16-digit card number, a CV2 code, expiry date, billing address, then a 3D Secure authentication from a bank). Similarly, it will be interesting to see how WhatsApp's new in-chat payment services fair in Brazil[36], along with FacebookPay in the US[37]. While there have been no concrete plans shared about a UK launch, these peer-to-peer payment mechanisms could have come in handy during lockdown!

While COVID-19 has demonstrated some clear winners and losers, there are still elements of the landscape where success or failure remains to be seen. These include request to pay (R2P) services, which is expected to boost uptake of instant payments, and has made some progress during lockdown months with testing and use cases, but has ultimately been delayed due to COVID-19[38] (as has ISO20022 for cross border payments)[39]; billion dollar cost-saving distributed ledger technology for FX and B2B such as R3; cloud and outsourced payments as a service; and the long awaited use case for Open Banking perhaps in account funding transfers, personal finance management systems and embedded payments.

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Contact us to find out how we can help your organization define pandemic-proof customer propositions and payment products and features.

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