Rob Rubin, David Morris, and Jaime Toplin

The Banking & Payments Show: Payments trends 2023

Audio

On today's episode, we explore the evolution of the payments ecosystem and discuss the trends to look out for in 2023. In our "Headlines" segment, we discuss (among other things) buy now, pay later; credit card fees; and crypto. In "Story by Numbers," we examine payments at retail stores. And in "For Argument's Sake," we debate whether interest rate scrutiny by regulators will impact credit card rewards programs. Tune in to the lively conversation between our host Rob Rubin and analysts David Morris and Jaime Toplin.

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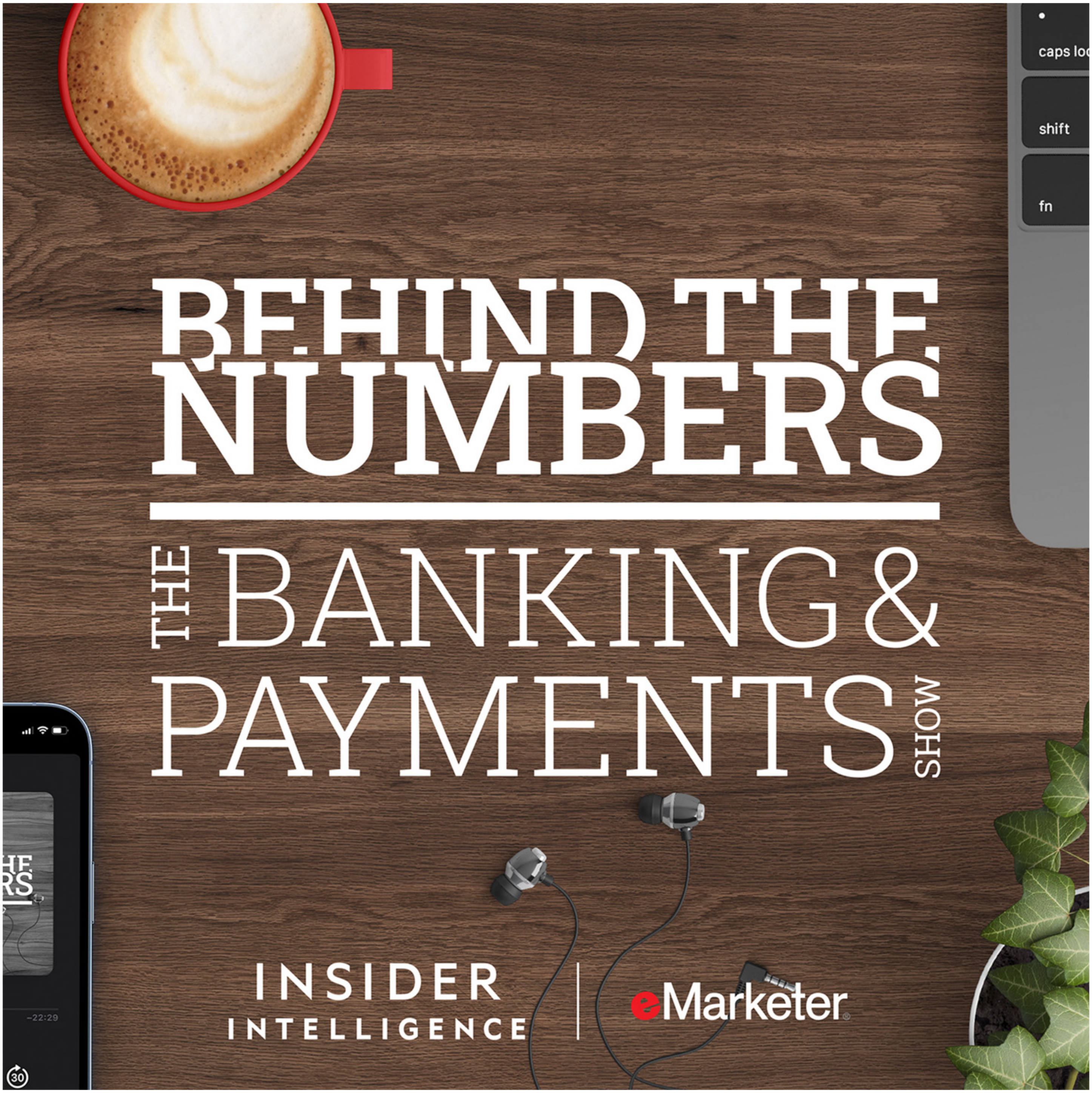

Episode Transcript:

Rob Rubin:

Hello and welcome to The Banking and Payments Show, a Behind the Numbers podcast from eMarketer. Today is March 21st. I'm Rob Rubin, GM of Financial Services here at Insider Intelligence and your host. If you enjoy this podcast, please give us a five star rating and subscribe. The title of today's episode is Payment Trends 2023, and I invited back Principal Analyst of Payments, David Morris, and Senior Analyst of Payments, Jamie Toplin, to join me to get their takes on the evolution of the payments ecosystem and what to look out for in the near future. But before we get into it, let's play a quick game of quick fire questions for fun. David, favorite rewards card?

David Morris:

American Express Blue Cash Preferred.

Rob Rubin:

All right. Jamie?

Jamie Toplin:

Capital One Venture.

Rob Rubin:

All right. David, true/ false, I plan out which credit cards to use to maximize rewards.

David Morris:

That's most definitely true.

Rob Rubin:

Jamie, true/false.

Jamie Toplin:

False most of the time, with some exceptions.

Rob Rubin:

All right. Jamie, what was the last thing you purchased using proximity payments?

Jamie Toplin:

I use proximity payments to pay for the subway almost every day. I'm based in New York, and it's really easy to just tap your phone and walk on in.

Rob Rubin:

Awesome. David, do you Venmo, Zelle, or Cash App?

David Morris:

This is a question for you. How old am I and how old is Jamie when we answer this question? I'm a PayPal guy. I use it for P2P, in a pinch, maybe a checkup.

Rob Rubin:

Jamie?

Jamie Toplin:

I use Venmo to pay my friends and family if we're splitting dinner or other purchases, but I actually pay my rent on Zelle.

Rob Rubin:

All right. I have to say that I have never really used PayPal. My wife does, but I use Venmo and Zelle.

David Morris:

You're really old, I'm old, and Jamie's younger.

Rob Rubin:

Maybe. I think that could be how it works out.

David Morris:

We're about the same age.

Rob Rubin:

I have to say, I've known you both for a while and I did learn something about each of you. We have a ton to cover, so let's get right to the headlines. In the headlines, we chat about a top story as it relates to our episode. For today's headline, I've selected an article we published a few weeks ago. CFPB adds more fuel to the push for BNPL regulation.

The article points to the fact that BNPL users have lower credit scores and are more financially strained compared to non-users. And that gives the CFPB a good reason to begin regulating BNPL. Jamie, is this actually a good rationale, or is the data more function of the audience? BNPL appeals most to our younger consumers who correlate with having lower credit scores and are more likely to be living paycheck to paycheck.

Jamie Toplin:

Unsurprisingly, the short answer is kind of both of the above.

Rob Rubin:

Okay.

Jamie Toplin:

If you zoom out a little bit, you can see BNPL's audience is really wide-ranging. People are going to spend nearly 95 billion using BNPL this year. That's a lot of money, and users will grow so fast, mostly from millennials and Gen Zers, but there's appeal across all age groups. And I think that's pretty important to take into consideration. But if you look at the reasons why people use BNPL, those tell an important story too. For most people, it's a budgetary tool.

But of the top nine reasons people use BNPL, five of them are related to avoiding credit cards and late payments and missed payments are growing, which is potentially problematic. On one hand, this might be because people just see BNPL as less serious than credit cards. They don't necessarily understand the penalties or the risks. There are fewer penalties and risks, which does make a case for regulation, especially because it could point to an issue with the product itself. Customers can overextend, double dip on debt, all that stuff.

Rob Rubin:

They don't want to have it put on their credit card limit.

Jamie Toplin:

Exactly. In some cases that might just be, like I said, because of budgeting, because they don't want to be levied penalties. But on the other hand, it can create some real financial risks that the CFPB, which is concerned with financial regulation, cares about.

Rob Rubin:

We had a whole episode on BNPL with Dan Van Dyke and one of the things that we talked about is that when the BNPL providers have to report to the reporting agencies, there's going to be a repricing reckoning with the credit card issuers who are now going to start looking at with some of their customers the amount of credit that they're extending and start to reprice them. Do you agree with that?

Jamie Toplin:

I do to some extent. I think it's still pretty hard to say, because I'm not entirely sure how much overlap there is between BNPL users and credit card users. Some of that avoidance might be because people don't want to or can't open a credit card in the first place, whereas others it might be because they're maxed out. But it's definitely something that I'm curious about to see when it happens. I also think there are already steps being taken to limit the amount people are extending themselves on BNPL.

Firms are already adding options like pay now to try to get people to cut down on how much they're borrowing, even if they still want to use the service for the perks that it offers. There might be some self-governance in the space too before we even see government step in.

Rob Rubin:

David, if we were to zoom out, I think that the BNPL industry needs regulations actually. What regulations do you think the payment industry in addition to BNPL is going to see this year?

David Morris:

Yeah, I agree with a number of things that Jamie said. I mean, just hitting buy now, pay later here briefly, I mean, you're looking at an industry that isn't regulated. Yes, it needs regulation. I mean, people need protections either against predatory behavior by companies or from themselves. I'd say briefly with buy now, pay later, they're definitely going to do something about increasing transparency. This is a no-brainer. It's something the credit card issuers have been doing for years.

They do have to do something at a regulatory level about loan reporting to credit agencies, so they can do exactly what Jamie has suggested, which is know exactly how much these folks have borrowed so that you're not contributing to overextending them into a debt hell hole. But I think beyond that, you have a lot of activity in the credit card space. There's everything from late fees to interest rates to credit card switching that regulators have on their minds. Late fees we've already called as something that's going to change this year.

The CFPB is going to attempt to lower those late fees significantly because it wants to be able to essentially take the profit out of the late fee, so to speak. That's what they intend to do from a regulatory perspective.

Rob Rubin:

How will the credit card issuers make up the money?

David Morris:

Well, that's a good question. You can stop one hole and the water will go elsewhere.

Rob Rubin:

It's a game of whack-a-mole

David Morris:

Game of whack-a-mole. I mean, that's an argument that yeah, the issuers themselves would even make, but they won't have this lever as much at their disposal. They are going to have to make up that ground in this capitalist economy that we find ourselves in. One of those things, actually, ironically, could be something that on its face could damage the standing of some of the credit card issuers, and that's requiring them to share customer data. This is an open banking phenomenon. This is all about APIs and some technical stuff here, but the bottom line here is that the regulators want to make it easier for customers to switch, go somewhere else.

Rob Rubin:

If you don't like your service, you're not tethered to it electronically. You can move.

David Morris:

Exactly. It's like HIPAA Portability except it's credit cards. You get to go somewhere else. You enhance competition, ultimately. That's the argument by bringing prices down.

Rob Rubin:

Is that what happened with HIPAA?

David Morris:

I don't think so. That's the thing. I mean, there's a hypothesis, and I think it's a very interesting one, is that your stimulating competition among a broader ambit of the banks. Because when you step back, you've got seven or eight banks that issue almost all the cards in the country. That's also where I think banks that are really smart are going to make money, to your point, which is utilizing open banking and customer data to their benefit.

Rob Rubin:

I think that I should ask narrower questions or have more time. I think we all agree that BNPL regulation will be a good thing for BNPL overall. And in fact, some new regulations will potentially increase competition and better services for consumers, we hope. But for our next segment, Story By Numbers, I want to focus on payment trends where most of the transactions occur. In Story By Numbers, we pick a number or two that helps us dig deeper into the episode's topic.

Today, for Story By Numbers, we're going to focus on payments at retail stores. At Insider Intelligence, we talk and write a lot about e-commerce. And as a percentage of all retail sales, e-commerce is growing and physical store sales are declining. But in 2026, we project physical stores will still account for 80% of all retail sales. The question is, how are retailers leveraging new payment technologies to improve in-store experiences?

Jamie Toplin:

It's a good question, and I think it's something that as we talk about this, a lot of our listeners will hear things that they have noticed in stores or see in stores or use in stores, which makes it fun to talk about. But what it really comes down to is the idea of how can retailers and payment providers use digital to make the store experience better the same way they're enhancing online. The biggest answer is probably new payment methods and specifically contactless payments and mobile wallets, which we were talking about a little bit earlier, but really come into play here as well.

Things like Apple Pay, Google Pay, even some P2P apps like Venmo and Cash App are moving in-store, and retailer wallets like Walmart Pay, looking at how as adoption of these wallets grows, how average spending grows. These wallets are approaching 20% of the retail dollars spent by every person who uses them, how they can incorporate accepting these, making it easier for customers to use them knowing they're available.

Rob Rubin:

Will we see account to account payments in-store?

Jamie Toplin:

Probably not yet. I would say that's more likely to be a focus online at the moment. Because if account to account was to move in-store, it would actually look a lot like a mobile wallet because customers would be paying through some sort of digital engine. Stores are probably going to focus on putting that on their website for now. What do you think, David?

David Morris:

Yeah, I think the account to account angle, it's very strong online. I mean, this is an open banking play. I think there's a clear natural fit online. It's a matter of being able to penetrate the digital wallet realm, and I don't think that's going to happen right away.

Rob Rubin:

What about retailers have to give the credit card companies a percentage of the transaction? Account to account potentially gives them a lower cost rail, right?

David Morris:

Well, yes and no. Jamie and I love talking about co-brand cards and private label cards. The big retailers, if you go to Best Buy, for instance, they have co-branded cards where they're actually making money with that card instead of giving it back all over to the issuers or the networks. It's one of the value propositions for them. Private label is even higher. Macy's, believe it or not, I think it was a billion dollars. This was maybe two years ago, over a billion dollars they made on their credit card revenue. Without it, they'd be bankrupt years ago.

Rob Rubin:

That's really interesting,

Jamie Toplin:

I think it's also a good time to think about if you back up a little bit, mobile wallets are not necessarily the payment method. They're more of the way that you pay. You pay with your phone versus you pay with plastic. You can feed almost anything that's not cash into a mobile wallet. Eventually we'll probably start to see all these methods being integrated. Buy now, pay later, for example, is showing up via mobile wallets in-store. That's partly why that's the area of focus because it really opens the doors to a lot of new stuff for years to come.

David Morris:

PayPal's a great example. I mean, PayPal has thrived for 20 years in the online world. Actually it has faltered entering in-store. It had the relationship with Discover. The time is now actually to be able to utilize all of the things that have gone on in the last two or three years with omnichannel and pivoting into digital, enforcing digital. These digital centric players have an opportunity, I think, to realistically start penetrating in-store, which is where they see the growth too.

Rob Rubin:

You think that even though we're saying that 80% of all sales is going to be in-store, in-store is still growing because retail overall is growing?

David Morris:

Well, what I mean is this, is that a buy now, pay later player like Klarna, which is seeing its own e-commerce reset, it wants that 80% pie too. How is it going to do that? Well, it can issue debit cards, for instance, so now that Klarna customer can walk into the store. Or if it's really smart, which Klarna is, people underestimate these buy now, pay later fintechs repeatedly, in my opinion, they partner with one of the biggest point of sale hardware players in the world so that they can start to place their buy now, pay later offering at more than 40 million points of sale. That sounds pretty smart.

Jamie Toplin:

We're seeing that with the P2P players too. Venmo, for example, which is...

Rob Rubin:

Has credit cards.

Jamie Toplin:

Yeah, it's super popular for P2P. They have credit cards. They're now also moving in-store with QR. You can go into CVS, for example, and you can pay by scanning a code on your Venmo app and that'll pull from your Venmo balance. If someone had sent you $100 for dinner the other day, you can then use that to go buy shampoo. That's still a pretty small segment for them, but it's something that they're putting a lot of attention into.

Rob Rubin:

It seems to me that especially physical retailers, they are leveraging new payment technologies and the options that consumers have to provide a better in-store experience overall and to continue to make the retail experience vibrant for consumers who shop in a digital realm as well. I think that this has been a really great discussion, and I want us to take a break so that we can hear about something that is very near and dear to both of you, the payments ecosystem. We have our payment ecosystems Reports just have been published, and I would like to tell everybody a little bit about them.

Economic uncertainty and rapid technological innovation are shifting industry dynamics for players across the payments ecosystem, including acquirers and processors, networks and issuers. Insider Intelligence just published our 2023 payment ecosystem collection of four reports. Throughout these reports, we analyze new types of payments taking hold, like account to account payments, new payment technologies on the horizon, and changing consumer behavior. Clients can log in to insiderintelligence.com today to access all four payment ecosystem reports. Future clients, please visit insiderintelligence.com to learn more.

Great. In our final segment, for argument's sake, we're going to argue nicely about whether interest rates scrutiny by regulators will impact credit card reward programs. Now, let me connect the dots. A consumer advocate could argue that the people paying over 20% interest on revolving credit lines are actually the ones who are funding the perks of people getting rewards because they're probably less likely to be revolving. That's a good place to start. I mean, isn't that how it works?

David Morris:

I would say yes, there's an argument to be made here. We can go back to how much money is made in the credit card industry. By our estimates, $145 billion in interest revenue off of consumer cards in 2022. That's part of the pie. The other part of the pie is interchange. That's another $90 billion.

Rob Rubin:

How much was late fees because that's going away?

David Morris:

Late fees was about $16 billion. Small part of the pie, but a huge chunk of money nonetheless. If you're taking a look at revolvers, they're definitely bringing in an amazing amount of money. That's interest income. You must have revolved at least somewhere.

Rob Rubin:

Probably late fee income, interest income, right? They're not just bringing in interest income. They were probably late on payments, in some cases. They're the ones that are accounting for those fees.

David Morris:

Well, if you're talking about maybe the ones that are more risky or irresponsible or whatever, underwater, sure.

Rob Rubin:

Well, late fees always come with an interest payment.

Jamie Toplin:

Yeah, but it doesn't necessarily go the other way, which I think is important to consider. There are people who pay even more than the minimum payment on time every month, but also revolve because they're trying to pay off a big purchase because they can't make ends meet, stuff like that.

David Morris:

I think that the question about rewards, I mean, is there an argument that the revolvers are contributing a great deal to the cost of rewards? Yes. I mean, it's $145 billion. The other side of that coin is, and this is something that American Express always makes clear in its spend centric model, is it when you have more highly affluent folks that it is courting, these people don't revolve. I mean, half of American Express is still charge and you can't revolve on charge. They make the money off the interchange because you have a higher priced card, a Platinum

American Express Card, that carries a higher discount rate and you're going to get that money back in the merchant fees.

Jamie Toplin:

Yeah, there's certainly funding for rewards that comes from these other pools, but issuers are always arguing that spending and income from interchange and from people using these cards are a lot of what funds the rewards too. It's almost like a virtuous cycle in that regard, because you use rewards to get people to spend. The people spend, you have more money for rewards, and so on and so forth.

Rob Rubin:

But you can argue that interchange is under threat because of alternate payment rails, providing cheaper platforms, giving consumers a choice with regulation about which payment rail a payment might get put on. It could potentially create a threat for interchange fees. But at the same time, if they really had pressure to lower their interest rates spread from the amount that they can borrow the money to the amount that they can lend the money, the spread, wouldn't they change the rewards programs that they're actually offering?

David Morris:

My way into that, there's a lot of levers here that you've brought up, Rob. I mean, I might back up and say our credit card's going to maintain their primacy here in the United States. I see some writing on the wall globally and now here that would say not necessarily. I would call it the golden age of credit cards. I think it's actually over because-

Rob Rubin:

All right. Called it here.

David Morris:

-you have global pressure here. There's global pressure on the interchange. This isn't just the US. There is global pressure to be able to adapt to technology. Account to account, that's European. They're way ahead. I imagine Visa and MasterCard three years didn't go, "I can't wait for that to come over this way." They don't have a choice. I mean, there's a global movement. And actually I should caveat that, because if you wonder who owns ACH in England, it's actually MasterCard. They own Vocalink.

Rob Rubin:

Oh really?

David Morris:

Oh yeah. They've been adapting to this. I think that's part of the writing on the wall argument that I would make is that they are going to look for newer flows, and that could be an alternative payment or it could be just ensuring that they're broadening this electronic payment opportunity as wide as they possibly can, and then they make up any kind of margin shortfall on volume.

Jamie Toplin:

I'll take David on though, because I think a lot of times, even though maybe the golden age of rewards, as we currently know it, might be changing, rewards are more popular than ever, so the demand for them isn't going away. Issuers are going to have to just find new ways to afford the rewards that people want. We're already starting to see some experimentation. U.S. Bank has a new card where there's a 6% category and you can choose two retailers that it applies to. It's a much slimmer margin of what your rewards are for, but you get to choose. It's equally helpful to you while potentially being less expensive for them.

We will probably see more co-brands on high growth areas like MasterCard and Chase's new DoorDash card where they're splitting the cost of those rewards with another partner, but they're still really beneficial cards. I think that's where a lot of the change is going to come from, where it's not that rewards are going away or that credit cards are going away, it's just that issuers are going to find new ways to make them lower cost while still delivering the benefits, because people really care about the benefits. These newer methods like BNPL, they're exploring them. Klarna has a rewards program, but it's not the same and it's not even close to the same.

Rob Rubin:

Maybe the generic rewards program where you can get a hedgehog coffee mug, that stuff will go away.

David Morris:

That's certainly a rewards program that I can't wait to sign up for.

Jamie Toplin:

Or you can't get toasters anymore at the bank.

David Morris:

Where's my toaster for signing up? I mean, I agree with a lot of what Jamie's saying, and I think maybe the difference is if and when this is going to happen, I do think that there's pressure that is going to come down the pike here to bear on this market. I think that there's a very good argument here about rewards. I mean, you opened today's talk asking us about reward cards. I love rewards. I mean, I make a nice little bonus every year on my rewards. But if buy now, pay later is able to continue to innovate and continue to push merchant rewards and A2A will have that same capacity, I'll take my three or 4% rewards from someone else. We consumers have very short memories.

Rob Rubin:

You're not loyal to the rail.

David Morris:

Consumers aren't loyal to anything other than getting a deal. I mean, that's one of the problems with branding these days.

Jamie Toplin:

It's actually funny, because this is a good example of how everything in payments is connected, because it goes back to the in-store checkout too of like whoever's giving this to you, customers don't care. As long as they're going into a store, getting an easy experience, getting a fast experience, getting benefits, they're going to take it and they're going to run with it.

Rob Rubin:

That's all the time we have, unfortunately. This has been a lot of fun. I think that we all agree that the credit card industry itself is really under a transition right now. What it will become, we will see. But clearly there's competitive threats and regulatory threats and all sorts of other threats that they need to respond to. This has been a really fun conversation. Thank you, guys. Well, that is all the time that we have for today. I want to first say thank you, Jamie. Thank you, David. This was amazing.

David Morris:

Great to be here. I actually was hoping I could bash the consumer a little. We weren't able to do that.

Rob Rubin:

We would never bash consumers on this show.

Jamie Toplin:

Yeah, I had a lot of fun. Thanks, Rob.

Rob Rubin:

Yeah, I really appreciate it. I want to thank everybody for listening to The Banking and Payments Show, an eMarketer podcast. I especially want to thank our editor, Todd. In today's episode, we referenced data from our payments ecosystem report collection and our payments trends in 2003 report. Our next episode is on April 4th, and you'll not want to miss it. See you then. Thanks, everybody.