

Mobile Payments



Trend Focus: Issue 1

M-Payments: Tech Giants Rubbing Shoulders

with Major Banks

As an interconnected nation, Canada has embraced technology in every facet of life, from communications to shopping and up to banking. Where Canadians go, so do their mobile phones and digital devices. This changing landscape is also transforming traditional industries such as retail banking, which is constantly trying to keep pace with evolving consumer demands. One such demand is mobile payments (or m-payments), which is reshaping Canada's multi-billion dollar small payments market.

M-payments – the process of sending money or paying for goods and services electronically using mobile phones – is creating new opportunities not just for retail banks, but for global technology companies looking to tap into the highly lucrative payments market. Canada's small payments market – transactions that are less \$20 – is valued at \$90 billion annually. Tech giants like Apple have already entered the payments arena in the United States and are looking spread their wings north of the border. This could have a profoundly transformative impact on Canada's retail banking industry. With four out of every five Canadian smartphone users connected to Apple or Google devices, traditional banks are potentially at a major competitive disadvantage in the mobile payments arena.

While Canada's payment landscape has been described as more conservative compared to the US, there is perhaps no other country more prepared to embrace m-payments, given Canada's extremely high adoption rates of mobile technology among consumers and businesses. It is therefore no surprise to learn that Canada is ranked second in the world in mobile payments readiness, behind only Singapore, according to the MasterCard Mobile Payments Readiness Index.

| Country | MasterCard Mobile Payments Readiness Index (Rank) |
|---------------|---|
| Singapore | 1 |
| Canada | 2 |
| United States | 3 |
| Kenya | 4 |
| South Korea | 5 |

With the federal government recently extending its payments code of conduct to mobile payments, banks and merchants are already adjusting to manage the anticipated m-payments revolution. Concerns about cyber security, transaction fees and market share dominate the current discussion, with the federal government taking steps to establish regulatory certainty in this uncharted market.

Market Forces Drive M-Payments Revolution

Information and communications technology is the major driving force behind Canada's evolving payments landscape. There are three interconnected market forces driving mobile payments demand in Canada: (1) consumer sentiment, (2) high Near Field Communication (NFC) penetration at point of sales (POS) and (3) very high mobile device adoption.

(1) Consumer Sentiment: Canadians are widespread consumers of mobile technologies and related payments platforms. According to MasterCard, one-quarter (27 percent) of Canadians profess familiarity with using mobile technology to buy goods and services and 15 percent profess willingness to pay with their mobile devices.

(2) High NFC Penetration at POS: Each of Canada's leading banks have integrated NFC or contactless payments, allowing consumers to make cashless, contactless payments through cloud technology and encrypted SIM cards.

(3) Mobile Device Adoption: More than half (55 percent) of Canadians own a smartphone ; this figure is as high as 64 percent for Canadians aged 18-34, according to ICTC. Canada's mobile device penetration rate is 100 percent.

- 1) Rita Trichur (12 June 2014). "The next gold rush? Mobile payments." The Globe and Mail.
- 2) Jason Field (6 March 2015). "How Apple Pay Will Impact Canada's Banking Industry." Tech Vibes.
- 3) MasterCard. Mobile Payments Readiness Index.
- 4) Ibid.

Tech Giants Enter Payments Arena

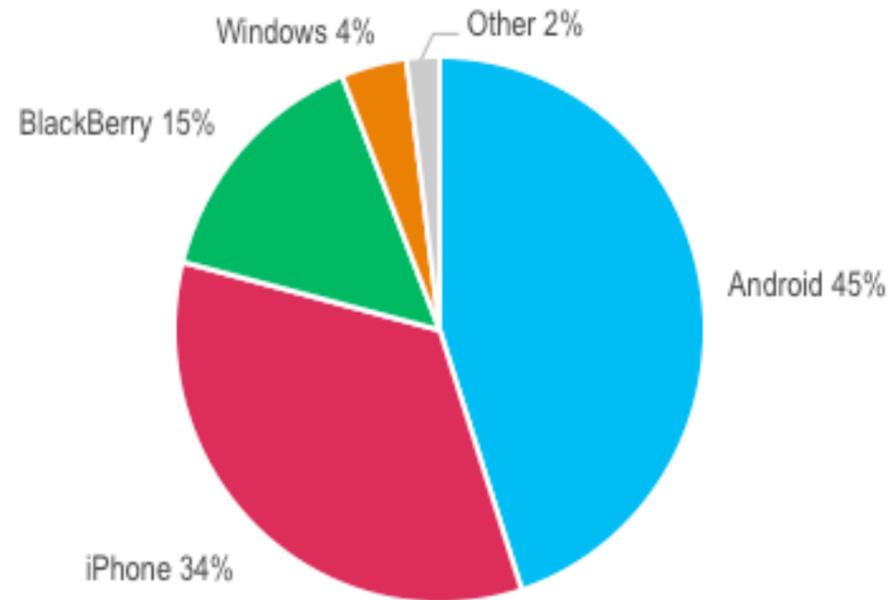
With Apple expected to introduce its momentous Apple Pay to Canadians in November 2015, the race to give consumers the coveted card-less mobile wallet has intensified. Apple Pay gives consumers the option to pay for goods and services using credit and debit cards stored on their Apple devices.

Google has also struck a mobile payments agreement with wireless providers in the United States. The agreement will enable users to access and pay with the innovative Google Wallet payments app already pre-installed on their phones.

With iPhone and Android devices dominating the Canadian smartphone market, Apple and Google have the opportunity to make significant inroads into the payments arena. Over 55 percent of Canadians own a smartphone, with four in every five users (79 percent) adopting either Android or iPhone devices.

The advent of Apple Pay can set the stage for a massive shift in the Canadian payments market by facilitating a bigger push toward m-payments. Consumer trends in the payments market clearly indicate a preference for cashless, electronic payments. On the consumer side, electronic payments accounted for 89 percent of small payments processed through Canada's automated clearing settlement system (ACSS) in 2014.

Share of Canadian Smartphone Market (Catalyst, 2015)



Government, Banks Respond

With Apple Pay expected to enter the Canadian market this year, the federal government recently extended the 2010 Code of Conduct for the Credit and Debit Card Industry. The update ensures that the same stipulations applied to debit and credit cards also apply to m-payments. The update reduces the transaction processing fees paid by merchants and provides more regulatory certainty to foster the m-payments landscape.

Canada's major banks have also formed a consortium to manage the m-payments transition in Canada. The Big-6 Canadian banks are in negotiations with Apple over cyber security concerns and transaction fees, the latter of which is expected to rise with Apple in the fold. The broader concern for banks, however, is losing their direct relationship with consumers, who already use Apple and Google services for communications, entertainment and information.

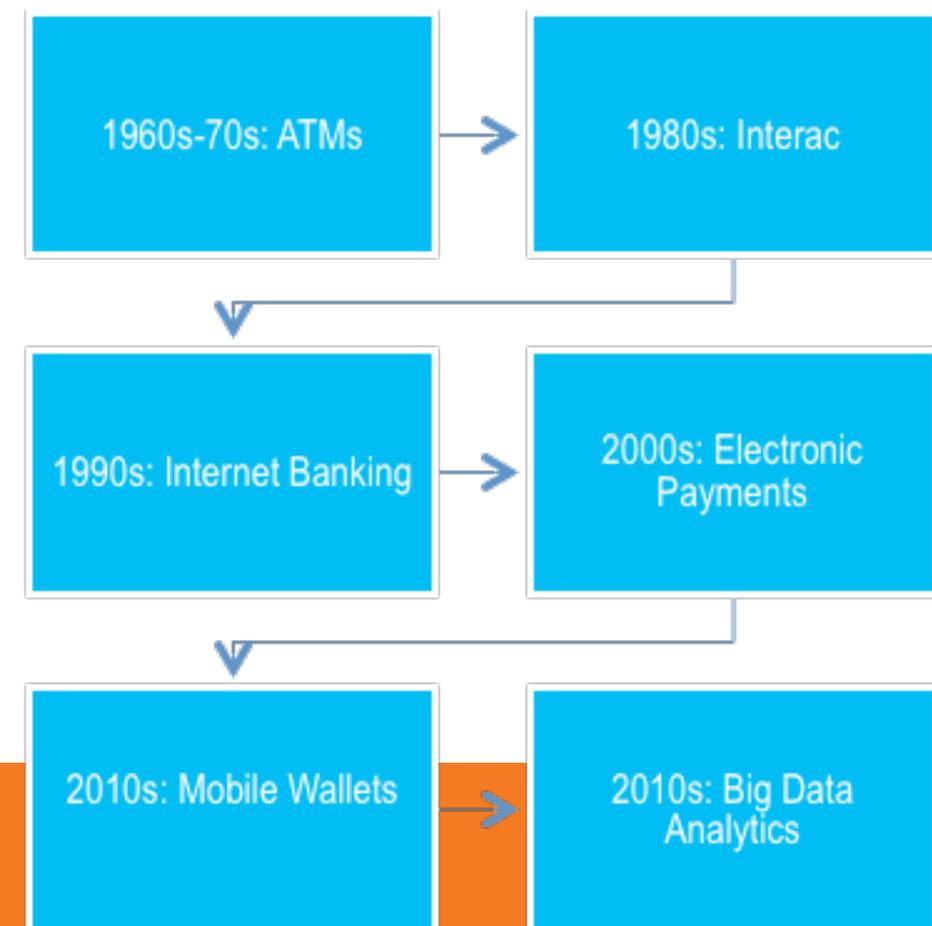
Capitalizing on Consumer Choice

"As long as companies are dependent on the credit card ecosystem, they are doomed to lose roughly 2 percent of every transaction to the Visa-MasterCard-tel."

The advent of m-payments means banks risk being squeezed out as middleman between consumers and their purchases. To avoid reducing their direct relationship with consumers, banks will have to provide customers access to a third-party service like Apple Pay that lives outside their platform. The fine balance for banks is providing the technology consumers are demanding without losing their relevance in a rapidly expanding market.

Analysts have speculated that Apple is poised to lead the mobile payments market, having only recently added Discover to its Apple Pay Passbook. This move gives consumers four credit cards to store on their phones in addition to their debit card numbers. With Visa, MasterCard, American Express and now Discover included in Apple Pay, the iPhone maker is poised to compete not just in North America, but internationally as well.

Big companies like Wal-Mart may also choose to create their own mobile wallets to win back the 2 percent transaction fee paid out to payment processors. This "rebranding of finance" seeks to eat into the banking sector's traditional grip on payments. While this is a welcome sign for consumers, it is creating a "breakdown of trust" between small businesses and payment providers, with the former having to pay more in the way of service charges. While the updated code of conduct gives merchants more discretion in the mobile payments arena, consumer behaviour will likely have the final say.



5) Catalyst.ca. Infographic: The 2014 Canadian Smartphone Market.

6) MasterCard. Mobile Payments Readiness Index.

7) Michael Lewis (17 April 2015). "Apple Pay to launch in Canada in November: report." The Toronto Star.

8) Jason Del Rey (23 February 2015). "Google Strikes Mobile Payments Deal With Wireless Carriers."

9) CNBC.

10) Catalyst (2015). Infographic: The 2014 Canadian Smartphone Market.

11) Canadian Payments Association (2015). Flow of payment items through the Automated Clearing Settlement System (ACSS).

On the technology side, mobile payments are creating greater demand for big data analytics, another major technology trend driving business intelligence. Big data analytics become more important in the mobile payments environment, where real-time transactions must be monitored to safeguard against fraud and identity theft. The push to accommodate quicker, contactless payments and real-time transfers requires the sort of real-time, predictive analytics made possible only through big data. As competition intensifies, it is imperative that we monitor further disruption in the mobile payments market. It remains unclear how m-payments will impact banking intermediation, cyber security, small businesses and market share. Regulations are constantly evolving to protect merchants without slowing the relentless pace of consumer demand.

Trends in consumer behaviour clearly show that mobile payments represent the next stage of the payments revolution. The introduction of Apple Pay later this year could serve as a case study in how mobile payments will play out in Canada.



- 11) Robin Arnfield (21 April 2015). "Canadian government extends code of conduct to mobile payments." Mobile Payments Today.
- 12) David Berman (17 April 2015). "Canada's banks form consortium to deal with Apple Pay: reports." The Globe and Mail.
- 13) Ralph Dangelmaier (18 April 2015). "Wallet Wars: The fight to dominate payments is just beginning." Venture Beat.
- 14) Jason Field (6 March 2015). "How Apple Pay Will Impact Canada's Banking Industry." Tech Vibes.
- 15) Michael Fitzsimmons (28 April 2015). "Apple Pay's quest for payment domination just got a major boost." Tech Radar.
- 16) Rita Trichur (20 March 2013). "Merchants wary of mobile-payment costs." The Globe and Mail.
- 17) Mike Urban (26 August 2014). The Role of Big Data in Monitoring Real-Time Payments Fraud." Bank Systems and Technology.



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