Insights into Payment Market Trends within National Economies

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In recent years, the differences between the players within the global economy, more specifically between the collective of the United States and Europe and the countries that fall under the emerging markets umbrella, have actively increased. As these emerging markets grow their economic and political independence, the most pressing issues have become the regulation of national payments and the creation of an internal payment infrastructure; and these new payment infrastructures must be flexible enough to respond to external challenges quickly and effectively.

The global hegemony of Visa and MasterCard, which lasted throughout the first decade of the early 21st century, is becoming increasingly restrictive and, as such, has been subject to more active attacks from national regulators in different countries. The reasons behind this are primarily the economic interests of the players in national payment markets and political issues dictated by the dependency of international payment systems, that aren't in actuality, state-owned, on the foreign policy of the country in which they are registered. In this instance, it is clear that we are mainly talking about American companies, often dominant in many sectors of the world economy and therefore wielding significant influence over national markets in different sectors. By conducting foreign economic activity, these companies are required to execute the decisions of the US public authorities including any restrictions and sanctions imposed by the United States on individual states.

The most recent and prominent example that made the headlines is the sanctions imposed by the United States and the European Union against a number of Russian public and private companies, mainly within the financial sector. The outcome of upholding these restrictions, without any notification, led Visa and MasterCard to stop processing the bank cards of some of the largest Russian banks. This directly affected the banks' customers rather than the owners on whom the sanctions were imposed. As a result, more than two million cardholders were left stranded without access to their own money, and in excess of 5,500 retail outlets processed by these banks were unable to accept card payments from their customers. It is pertinent to mention that Russia quickly managed to minimize the negative influence on the cardholders who fell under the sanctions imposed on the banks. The use of local processing centers connecting various banking groups, as well as the establishment of direct interfaces between the largest Russian banks enabled transactions by the blocked cards to be processed in the internal terminal network, ensuring their normal use, at least within the Russian Federation.

There are a host of other examples of restrictions imposed by the international payment systems on certain countries where banks have fallen under the sanctions enforced by the public authorities, predominantly those of the United States: the entire financial system of Iran, Sudan, Syria, certain banks in Azerbaijan, Jordan, Cyprus, etc. A number of European and even American players faced huge penalties for cooperation with the countries and organizations under sanctions. The American JPMorgan Chase & Co had to pay an $88.3 million fine for violating several US sanctions related to transactions in Cuba, Iran, Sudan and Liberia. The Dutch ING Bank incurred even more losses with a $619 million penalty for similar actions; during the summer of 2014, the French bank, BNP Paribas was ordered to pay more than $8 billion to the Ministry of Justice as compensation for processing transactions in countries blacklisted by Washington. Despite the fact that not all international payment systems display such a serious dependence on their national jurisdictions in terms of foreign economic activity, the approach of the international companies that do significantly blackens the reputation of international payment systems as a whole.

As a natural reaction, many national economies as well as direct participants in the market have made efforts to set up their own infrastructure which, at minimum, regulates and monitors payments utilizing the international payment systems' tools, and, at maximum, fully localizes payment processing within the country, with a view to building their own payment system, which ideally would become international. The first step is to build direct host-to-host connections between different banks, enabling them to provide settlement for bank card transactions without the participation of the international payment systems; the organization of banks into associations that use a single processing and clearing center and, ultimately, growing to become nationwide, fully addressing the settlement and transaction processing issues between the market players for the international payment systems within their jurisdiction. There are numerous examples of such projects across the world: Algeria, Indonesia, Qatar, the Congo, Malaysia, Nigeria, Saudi Arabia, Singapore, Sudan, Tunisia, Ethiopia, South Korea and Japan amongst others; where processing local transactions abroad is prohibited. A number of European countries, including Latvia, have also closed their internal market to international payment systems and now process local transactions performed by international cards themselves.

Undoubtedly these measures will increase the stability of the national economy and payments market against external influences, caused mainly by political factors, as well as enabling the regulation of foreign exchange flows and settlement payments. Additionally, these measures have a rather significant effect on the economy, as all the fees for these transactions will be regulated locally and distributed between the local market players. Even if it is not quite on topic, it is important to touch upon another issue: who should be the beneficiary of this local infrastructure? Of course, the political benefits and those of being able to control the payments market nationally are obvious, but, amongst other things, there are huge financial flows passing through the new system, usually a commercial entity. If the owner of this commercial entity is a national regulator, the issue of monopoly and lobbyism becomes very acute and is ultimately detrimental for market participants. Maintaining the share of public participation, the owners of the consortium are usually comprised of the local commercial banks, but regardless, ownership is always a delicate matter that cannot be discounted lightly.

The final stage of creating a localized infrastructure is the emergence of various market specific products and even the move to become international payment systems built on their own infrastructure using their own tools. On occasion, the local system will offer co-branded cards that run on the technology platforms from international payment systems, but utilize different principles of transaction processing both inside and outside the country. In addition to financial and other local applications, these cards incorporate a variety of uses, relying on the concept of a single token for public services (as an ID, for using public transport, accessing medical records, etc.). For example, the concept of the Universal Electronic Card in Russia, the National Identity Management Commission in Nigeria, the EZLink transport card in Singapore and the Malaysian MYKAD. Some countries have managed to build fully functional international payment systems built on their own technology platforms and processing principles. Worth noting are China's UnionPay and Japan's JCB, which provide strong competition to the Visa and MasterCard giants not only in Asia, but also across the globe.

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The process of building both local and international payment systems brings with it complications, not only technological challenges, but fundamentally the issues around ensuring the regulatory framework and establishing the pre-trial settlement of claims between the participants. In addition, issues arise when replicating their own technical requirements and implementing them on existing devices and platforms used by other market players. However, experience has shown that even in the face of intense competition and within the current economic relations, nothing is impossible. When commencing projects to build a local payment system, payments technology trends need to be taken into account, including the move away from the plastic card to virtual money (including electronic wallets) and mobile technology that threatens to completely replace traditional tokens such as the magstripe or chip-based plastic card. A good example of this is the recent news that Apple has introduced its own payment system, Apple Pay, which exploded onto the scene and has created a lot of controversy.

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It is not farfetched to assume that we will soon see a rise in the number of projects primarily based around popular social networks; with a huge customer base on the one side and turnkey products built on a proprietary technology platform on the other side. This will enable the social networks to control the execution of payments on their sites using the tools already available and implementing their own payment tools and solutions, for use not only within their own infrastructure, but also for other well-known market participants, such as various retail chains. Advances, particularly in the field of mobile technology, significantly promote this process. Today, most smart phones, whose market continues to skyrocket, already support the contactless payment technology, NFC. With the majority of these smartphones, it is possible to implement alternative payment technology built on the applications that offer interaction between the merchant and customer phones. These types of technological advances support the idea that the physical payment card might disappear in the near future and be replaced by alternative payment tools that will simplify the development of local and international payment systems, unifying technology platforms.

From my point of view, active development of local payment systems and services, as well as the widespread use of mobile devices and technology in the financial sector are the most dominant trends in the market at present. In addition to the mandatory development of classic payment tools and services, banks and national regulators need to make sure they pay attention to these new trends today to ensure that they don't end up being left behind tomorrow.