Merchant Acquirers: How to achieve long-lasting success

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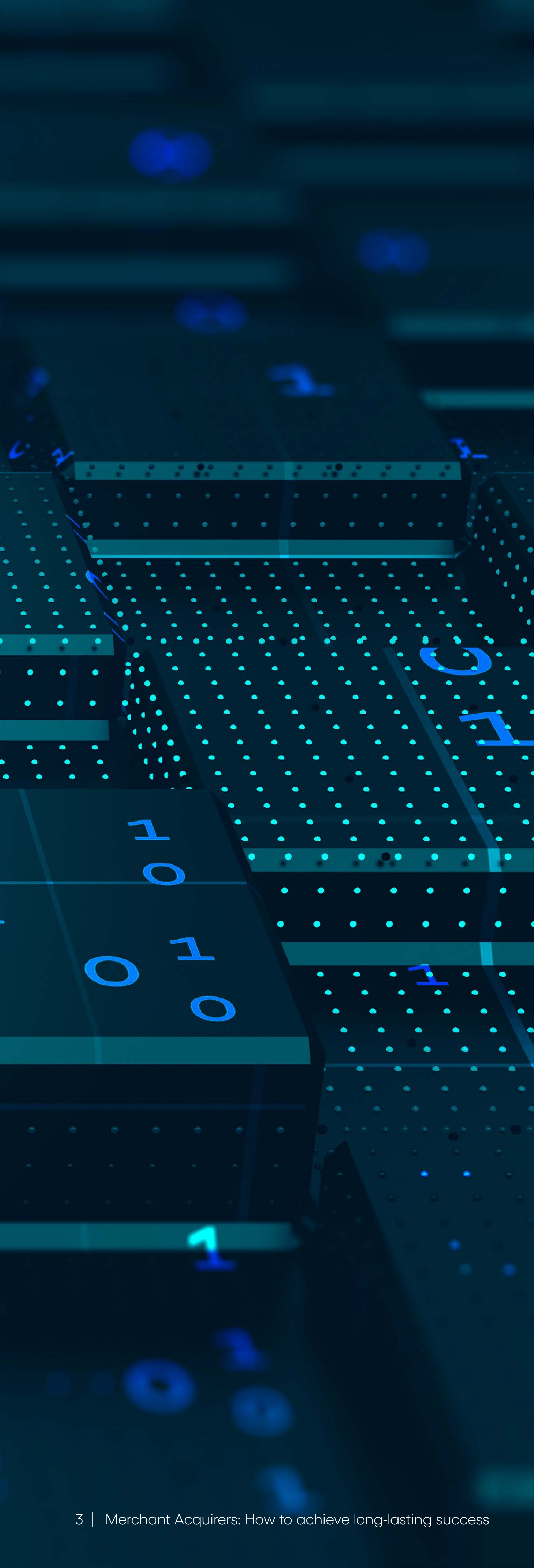

In his book The Infinite Game: How Great Businesses Achieve Long-Lasting Success, Simon Sinek argues the best way to win is not to focus on beating the competition, but on creating a sustainable business that can adapt and thrive over time. This is a valuable lesson for merchant acquirers, who are facing a rapidly changing landscape.

The merchant acquiring industry is being reshaped by number of trends, including the meteoric rise of digital commerce, increasing M&A activity, and the rapid proliferation of technologies. To stay ahead of the curve, acquirers need to adopt a long-term view and focus on building a strong foundation while making strategic bets for long-term success of the business.

This report identifies some of the key focus areas for merchant acquirers in the years to come.

Focus area 1

Become a one-stop-solution provider for clients

While offering payment-only solutions for clients may have worked for merchant acquirers in the past, it's not a viable solution going forward. Today's acquiring landscape is crowded with modern solutions providers offering more holistic propositions at competitive price points. Because of this, merchants are now expecting more from their incumbent acquirers. Additionally, the rapid growth of independent software vendors (ISV's) market has also prompted acquirers to invest in building strategic partnerships to drive value-added-services and integrated payment offerings.

The good news is that an increase in such value-added products is likely to result in an increase in revenue. According to a 2022 US survey conducted by Mckinsey[1], small businesses indicated they are willing to spend a total of $10,000 annually on such value-added-services.

Merchant acquirers will need to anticipate this trend in other markets and evolve from being a payments-only provider to become a full-services merchant solution provider by offering a well-rounded proposition to not only solve for the merchant payment requirements but also for the broader merchant business needs for e.g., banking, loyalty, marketing, payroll, financing and more. This will be vital in creating a more entrenched relation with the merchant in the long term.

The shift in strategy will require acquirers to quickly re-organise their business and operating models. Additionally, the commercialization strategy needs to be reshaped and investments need to be made in training and up-skilling the sales force to sell holistic merchant solutions instead of payment-only solutions. The success of this approach will also depend to a great extent on acquirers' ability to recalibrate their seller targets and incentivization models.

“Acquirers who are building a relational model will benefit from these advances in payments technologies and models. Merchants are looking to move from a transactional relationship to a holistic one where merchants can not only get their acquiring but also other services to help with their business especially in the SME segment – banking, FX, lending, working Capital, analytics, payment methods, and new solutions that help drive a merchant's business.”

Tribh Grewal

Head of AltPay, FinTech and Commercial Solutions,
EMEA, Discover Global Network

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Focus area 2

Simplifying product propositions to save cost, reduce customer confusion and improve sales

The M&A activities of the last decade have left merchant acquirers with a jumbled set of solutions and sowed confusion in the minds of merchants. The time is right for merchant acquirers to simplify the chaos and provide the clear solutions their clients crave.

To start, acquirers need a clear product strategy to focus on simplifying their market-facing proposition, making it simple for both the merchants and their own sales force. Next, acquirers need to invest in platform rationalization and simplification initiatives. For example, many acquirers still use multiple payment gateways that have been developed in-house, licensed from a third-party platform provider, or have come by the way of M&A activity. In those situations, acquirers need to retire or consolidate those gateways.

Such consolidation can be done—by creating an overarching payments orchestration layer that will simplify product presentment, pricing, onboarding, transaction processing, reconciliation and settlement.

Payment orchestration will enable merchants to have greater flexibility, effectively providing an integration layer enabling acquirers and other payment solutions to easily plug into their systems. This could assist in multi-acquiring options and simpler integration of new services and streamlining business.

Acquirers should use this as an opportunity to simplify pricing wherever possible while looking for creative ways to price the product. In the next few years, we expect acquirers to evolve to more matured pricing models such as value-based pricing.

> “If the payment company is delivering value in terms of enabling customer journeys, achieving highest authorisation rates, reducing fraud and chargebacks the pricing discussion becomes less important. That being said, it is paramount that pricing should be transparent, simple in nature, and based on the value that the solution provides.”

Angus Blest

Commercial Director, Adyen UK

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Focus area 3

Be aware of, but don't fear, the pay-by-bank disruption

From the merchant's perspective it may be beneficial to use the pay-by-bank (aka open banking payments) method in high value cases because it eliminates the high interchange cost and offers real-time settlement options. This is especially true for categories that include B2B payments, tax payments, credit card payments, and brokerage payments.

While the use case for e-commerce is known and well appreciated, the pay-by-bank solution for in-store purchase introduces friction in the payment journey. Since the launch of contactless products, the consumers in the UK for instance are used to making payments with minimal friction for in-store purchases, so the pay-by-bank providers will have to offer the same level of convenience and frictionless experience to really compete with contactless product. Variable recurring payments (VRP) for non-sweeping use cases looks like a promising solution as it would eliminate the need to authenticate every transaction once the customer sets up a mandate for a merchant.

Also, from a pricing standpoint an open banking payment in the UK is priced close to a debit card. For the product to be beneficial to the merchants, the pricing needs to be more competitive. Equally, to make it more appealing to the buyers, merchants would need to consider incentivising the buyers by passing part of the cost saves as discounts or finding other innovative ways to reward buyers for their choice.

Some merchants have found a clever way to promote pay-by-bank and are making it harder for the buyers to pay by other methods. So, while incentivization is a good approach, but so is promotion throughout the website before the customer reaches checkout, as well as high prominence on checkout screen.

In certain markets such as the UK, another important consideration is the difference in consumer protection on open banking transactions vis-à-vis a card transaction such as Section 75 of the Consumer Credit Act 1974 and scheme chargebacks which do not apply to pay-by-bank payments. This has proven to be one of the key deterrents for consumers wanting to use pay-by-bank solution. In the UK, Joint Regulatory Oversight Committee (JROC) is trying to make open banking safer, scalable, and economically sustainable. And one of the key JROC recommendations is to conduct a gap analysis to ensure effective consumer protection if something goes wrong.

Also, for open banking payments, there is a minor chance of transactions not being instantly confirmed and, in some cases, this would mean transactions could remain unconfirmed for several hours or days. This adds a bit of uncertainty, and as a result merchants that process a huge volume of transactions could be a little apprehensive in accepting this payment method. Therefore, some sort of guaranteed payment / settlement scheme would help address this and increase merchant's confidence in accepting open banking payments.

The future is bright for open banking payments and recent reports show the growth figures from the UK are very encouraging. However, in the shorter term, we expect it be more complementary to the other prevalent payment methods.

“Adoption will be driven by a clear statement of benefits like product, usage, convenience and security, for the consumer as well as the merchant. The card experience especially contactless is so familiar, trusted and easy and it will continue to remain relevant. However, there are plenty of use cases where the card experience is still lacking, especially in the areas of consumer visibility and control such as regular payments and online authentication journeys. This is where open banking processes can provide significant benefits.”

Tim Johnson

Head of Strategy, Payit and Tyl by NatWest

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Focus area 4

Commit investments to ensure superior and seamless customer experience

It's time for acquirers to learn what merchants have long known: when it comes to payments you must be present where the customer is. As several industry reports suggest[2], one of the top reasons a customer will abandon their shopping cart is due to a lack of preferred payment options.

To meet customer expectations, acquirers are rapidly adding more payment methods to their existing offerings. This trend is expected to continue in future. There are over 350 Alternative payment methods (APM's) in the market such as digital wallets, BNPL, loyalty points, cryptocurrencies, and NFTs. The checkout is becoming very competitive as every provider is eyeing for customer's wallet share.

> "Technological progress has always played a significant role in the customer experience—especially in the payments industry. Customers are developing new payment preferences, which vary around the world, leading to an ever more diverse set of payment methods. To expand global reach, businesses have to meet their customers' payment expectations. That could mean offering one-click checkout in some markets, local payment methods like iDEAL in others, or instalment plans in regions where buy now, pay later options are popular."

Amandeep Batra

Payments performance Strategist, Stripe

Re-imagining customer journey

As per Visa[3], the average checkout time in the EU is over 3 minutes and over 60% of the customers abandon their journey within the first 2 minutes. With the growing number of supported APMs, there is high likelihood that it could result in increased checkout time and higher abandonment rates. Also, an average of nine screens in the payment journey further increases friction in the process.

To compete in this space, one of the strategies for acquirers could be to look at ways to engage with the customers early in their shopping journey and shift-left in the buying process. This may mean providers will have to embed their propositions within the product discovery step to get the customer's attention early on. A good example is PayPal's acquisition of Honey - a browser extension that automatically finds and applies coupon codes at checkout with a single click.

Further, front-end payments orchestration will allow a merchant the ability to filter and sort payment methods offered to a customer at the checkout based on their region, preferences, or previous purchase behaviour to make it a seamless checkout experience.

"Acquirers are an important part of the equation, but it requires the whole payments ecosystem to come together to create a payments experience that results in a superior customer outcome. Alternative payment methods provide customers with more choices in how to pay, whether that's dividing the payment up in four even payments or paying through an app on their phone. But we're reaching a point of saturation in the market and having a payments partner who can help you surface the right payment option at the right time using AI/ML and make payments the foundation of the shopping experience by leveraging data is what will really set the winners a part."

Nitin Prabhu

Vice President,
Merchant Experience and Payment Solution, PayPal

There is also a need to re-imagine the checkout journey through a better UI/UX to improve customer experience. Initiatives like network tokenization, click-to-pay, digital identity will help greatly reduce the overall friction in the checkout process.

> "Merchant acquirers need to review their entire business model to be more merchant and shopper focused; thereby aligning their motives and goals to their customers. They must focus on optimisation, the customer journey and how they can support their merchant by improving the whole payment experience. Complexity is not necessarily a bad thing as long as it does not impact the customer journey or experience."

Angus Blest

Commercial Director, Adyen UK

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Investments in connected commerce capabilities are on the rise:

Another major trend that has drawn investments from the acquiring community in recent times is connected commerce or omni-channel payment solutions. Customers love the flexibility of purchasing across multiple channels, especially since the pandemic that saw a significant uptick in e-commerce volumes. Brick-and-mortar merchants have since then added e-commerce as one of their primary channels to do business, however many of these solutions still operate in silos making it more of a multi-channel proposition.

By connecting offline and online channels through an omni-channel token, acquirers will be able to offer a seamless channel-agnostic commerce experience, capture cross-channel insights, create loyalty programs to drive more sales and engagement and making reconciliation easier.

The channel landscape is evolving rapidly. ISV integrations and partnerships are driving newer channel possibilities; therefore, it is important for acquirers to prioritise these new and emerging channels as part of their overall omni-channel strategy to stay competitive and relevant. We also expect acquirers to develop sector specific omni-channel propositions aligned with their priority and top performing industry verticals.

> “Today, payments innovation is being driven by the needs of consumers, as well as merchants, who want to ensure the customer journey is seamless and friction-free. This has led to an evolution around connected commerce, which is focused on ensuring transactions can be completed anywhere, anytime. At the same time, these payments need to be connected to other services that allow merchants to better manage their business – from loyalty programs to making appointments/reservations online. One of the dominant models in the global commerce marketplace is the rise of the payment platform. Traditional acquirers are transforming into merchant service providers. These providers have made significant investments in technology innovation that offer a unified, connected solution that makes it possible to accept cards and digital transactions across currencies.”

Peter O’Halloran

Vice President, Head of Enterprise and Digital Commerce EMEA, Fiserv

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Improving in-store checkout experience

Contactless and digital wallets like Apple Pay and Google Pay have revolutionised in-store checkout experience to a great extent by reducing friction. The holy grail of in-store payment experience in the retail world is the Amazon's much talked about Just Walk-Out (JWO) technology which enables shoppers to simply enter a store, take what they want, and just walk out, enabling a seamless shopping experience. Businesses will need to identify the right use case, create a business case, and continuously evaluate ROI for such an implementation.

We have also seen alternative solutions where businesses like Waitrose allows shoppers to use their phone camera or use the retailer handset that allows shoppers to scan the product in-store and pay at the self-checkout area. We expect to see more innovations that will focus on improving the in-store experience and making it more frictionless. Retailers can further use technologies such as AI/ML to recommend products based on recipes and prompt the shopper for missing ingredients or promote hyper personalised offers[4].

Also, technologies like SoftPOS (aka tap to pay) has the potential to improve the traditional in-store payment experience for customers. Merchants can now offer inexpensive, and more points of acceptance on-the-go.

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Focus area 5

Take bold steps to progress from early trials to mass-rollout

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The technology landscape is evolving at breakneck speed. In the recent years several technologies like AI/ML, Biometrics, Web 3.0, IoT, digital ledger technology to name a few have got every industry excited and merchant acquiring is no exception.

Earlier this year, Worldline announced the launch of a new shopping mall in Metaverse (Decentraland). In the shopping mall, retailers, service providers and banks can build up their presence and engage with their community in the metaverse. Their starter package for newcomers contains many useful features including payments with or without cryptocurrencies.

Another technology that has taken the world by storm is Generative AI viz. OpenAI's Chat GPT. Payment providers such as Stripe and Klarna have forged partnership with ChatGPT. OpenAI plans to use Stripe to power payments for ChatGPT member access and DALL·E. Stripe in turn is incorporating OpenAI's new natural language technology, GPT-4, into its products and services. Klarna is planning to use OpenAI's protocol to build an integrated Plugin for ChatGPT to provide personalized shopping experience through product recommendations for Klarna users.

Also recently, Mercedes-Benz has introduced native in-car payments called Mercedes Pay+ for its customers in Germany, using Visa's 'delegated authentication' and Visa 'Cloud Token Framework' technology. The carmaker said the new technology turns the car "into a payment device". This innovation allows customers to pay for digital services and hardware upgrades in the Mercedes-Me-Store using a fingerprint sensor in their car.

"The fact is the process to implement new technology can be a long-term commitment. From ensuring there is the infrastructure in place to support the technology and implementation process, the adoption of new technologies can be a long-term proposition that is challenging and requires overcoming barriers to adoption. Contactless payments are a good example, the technology was available in 2005, and did not start to pick up adoption until 2013-14, and once the pandemic hit, we couldn't implement it fast enough. So, even though the technology may show potential, the market may take time to recognize the value and for business to adapt their processes and infrastructure to support it."

Tribh Grewal

Head of AltPay, FinTech and Commercial Solutions, EMEA, Discover Global Network

There is no doubt, technology is going to re-define the future of payments. Acquirers have experimented with one or more of these technologies with varying degrees of success. Given the speed of innovation acquirers will be nervous at leading the charge with new technology as historically they have taken the role of fast followers. Agility is key to success and parts of the market demand the latest solutions. By the time they are launched it is too late if they have not already started to consider the latest options. Greater partnering will help the slower organisations stay in touch, but many will need to change their risk profile.

Implementing any new technology requires time and commitment. So, depending on their strategy and risk-taking abilities, acquirers should be ready to take bold steps in moving from a pilot phase to production and be prepared to stay in it for the long haul.

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Focus area 6

Drive towards leaner, modernized cloud-native payments platforms

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The ever-growing digital payment volumes mean payments platforms need to be highly available, reliable and scale continuously to meet this growth. Downtimes and service disruptions not only prove to be a reputational risk but may also lead to revenue loss for acquirers.

As a result, we are witnessing acquirers transform their legacy monolithic payments platforms and transition to cloud-native microservices and event-driven architecture. Achieving payments technology modernization alongside enhancing existing product capabilities continues to be a challenge for acquirers, however modern technology stacks and architecture patterns are providing adequate options to address this. Additionally, reliability engineering has gained a lot of prominence with acquirers building proficiencies in observability, monitoring and overall automation for increased predictability and maintainability of core payments infrastructure and something that is being added in the architecture and engineering DNA.

We have seen acquirers adopting different strategies towards modernization, from hollowing the core and building orchestration layers, implementing strangler fig patterns, for leveraging both legacy and modern applications in tandem during the journey to completely overhauling and replacing the core processing platforms with API driven and learner cloud platforms. Either ways modernization is a continuous journey which brings in long-term benefits and should have complete business and product buy-in.

> “Acquirers that are flexible and have the technology stack in place prepared to take on new capabilities will stay ahead of new industry trends and be able to implement quickly and easily.
>
> With a modernized tech stack in place, the business foundation can respond to industry and consumer behavior changes quicker and scale more efficiently.”

Tribh Grewal

Head of AltPay, FinTech and Commercial Solutions, EMEA, Discover Global Network

As acquirers are also looking to expand and grow their footprint in newer geographies to attain more global market share, it is imperative that there is more focus on adopting models like “build once and deploy anywhere”, ensuring complexities like in-country data localization can be easily solved.

As stated above, Mergers and acquisitions has been a preferred path to attain efficiencies of scale, newer capabilities, geographical expansion and long-term growth for large acquirers. While there are many other upsides to consolidation through M&A, it often also leads to fragmented IT platforms and redundant applications which contribute significantly to the Opex and slows down roll-out of new products and capabilities to the market. Acquirers need to be more agile than ever to keep up with the market pace and adopt changes and extend capabilities with plug and play integration models.

The need for rationalizing and modernizing IT platforms and infrastructure is higher than ever and it is necessary for acquirers to introspect and take measures to carve out modern, leaner, and future-ready IT platforms.

Conclusion

The journey towards achieving long-lasting success for acquirers begins with having a long-term view and creating a continuous positive impact for consumers, merchants, and the overall payments ecosystem.

Sustenance and growth can only be gained with a holistic approach that combines - addressing customer needs with simplified products and propositions, taking bold steps to disrupt and innovate with new technologies, continuously staying relevant to the consumer with better experience, and ensuring flexibility with leaner platforms to course correct and adapt to dynamic external factors.

There are plenty of opportunities to pursue. But the fact is there is no one-size-fits-all when it comes to these opportunities. The pace of adoption will vary by market and as a result the tipping point. So, it is important for acquirers to place the right bets and commit to a longer time frame. The journey can be a long and uncertain one but in the end, if you have the infinite mindset you will sustain and thrive – So are you ready to play the “Infinite Game”?

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