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Payment: will Smartphones kill big POS?

We call them “swipers,” although some show the label “Chip&Pin”. Their security has stirred debates and some changes for the better: they are now PCI-DSS and PCI-PTS compliant. These “light” card readers associated with current smartphones are spoiling the party. They are not just opening up new markets but they are actively taking part in the renewal of the traditional payment culture, by directly threatening the status of the classic POS.

Mobiles, mobiles, always mobiles... It has become rather commonplace to describe the device as the Swiss-Army knife of the digital era. It's much more than that, thanks to the explosion of applications and physical “prostheses”: flash memory sticks, stickers, cradles, miscellaneous cases and now mini-card readers that can be plugged into the serial port, the audio jack or connected via Bluetooth – which is providing the stellar base (a future black hole?) of an unprecedented force field, paving the way for convergence between technologies and uses and imposing new rules that are undermining established models.

“We are indisputably witnessing the formation a new deal,” declared Angelo Caci, VP of French consulting firm ADN' Co., which hosted a round table in June dedicated to the “New Payment Landscape” during the unveiling of the 2012 edition of the CARTES expo.¹ “A new deal whose highly varied components combine in a complicated alchemy the results of which we don't yet know,” he further explained. Even if we are

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already seeing this new landscape traced out across the multiplication of payment instruments and methods, the arrival of new actors across the value chain and the boom in “interconnected” trade (O-to-O, for Offline-to-Offline, which includes E-commerce, M-commerce, S-commerce (for social) and even T-commerce (for interactive TV), a number of uncertainties remain. Uncertainties on the role of the new actors, on the effects of U.S. regulatory measures (the Durbin amendment, but also terms arising from recent settlements between Visa, MasterCard and retail outlets in the U.S.) and European regulations, all aimed at reducing interbank fees on card and wire transactions. Also and above all uncertainties about the reception and adoption by merchants and consumers of new technologies and new uses, closely linked to mobiles. The revolution is total. It affects issuing, acquiring, and processing, the technologies, the economic models and user experiences. The emerging, booming mini-card reader market (actually, ecosystem) is one illustration. Its success is due to very simple reasons: an expanded offer of payment methods and enhanced wallet features. The card is not only a payment instrument. And studies have already shown that an expanded offering grows the purchase conversion rate by 14%. The potential for using the mobile phone’s camera to cash checks or pay using QR codes, the native communications abilities also allow for payment by SMS. What’s more, all these payment methods are accessible via a wallet interface

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that offers resources for managing purchases and payment. Reason number two: the cost of the reader and the transaction are less than those for a classic card transaction. The Square reader, along with PayPal's (PayPal Here) are free, for example, with transaction fees at 2.75% and 2.70% respectively. Without subscriber fees and with very quick registration and activation procedures.

Square, the start-up created by Jack Dorsey, one of the founders of Twitter, is today valued at around a billion dollars. That represents just under half the value of Ingenico (€2.08 billion), and nearly a fourth of that of VeriFone (\$3.74 billion), a huge amount for a company that handles only 11 million transactions daily, whereas Ingenico and VeriFone with an installed base of POS terminals handle roughly 30 to 40 billion per day. But this figure also gives an indication of what's at stake in the mobile payment market. The model for this market is no longer the classic POS, highly secure, offline, primarily centered on the dominant use of bank cards, bound to a system of fees that was always the cause of discord between banks and retailers, and that we now see quietly undermined. The new system is an online, Cloud-based model where scoring transactions is the preferred method at the level of security. In this "Chip-to-Cloud" model, the chip is not a secure element, but rather an anchor to weekly affirm the identity of its user via a classic log-on/password, or a simple phone number. The lively debate on security questions which

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accompanied the launching of the first Square reader, opposing internet innovator Dorsey with the mighty CEO of might Verifone revealed this fissure. Since then, it's been attenuated. Square, which received capital investments from Visa Inc., now encrypts transmitted cardholder data end-to-end to its scoring back-office. That's become the rule for all card readers. A large number of them are now Chip&PIN and display PCI-DSS and PCI-PTS (for Pin Transaction Security) labels.² Square, which recently announced its goal to expand internationally, will no doubt have to undertake EMV migration sooner rather than later to do so. This is also the case for PayPal.

By becoming the heart of the new ecosystem, the smartphone offers a "ready-to-use" economic model, accessible to start-ups such as Square, iZettle or ex-start-ups such as PayPal – the original incarnation of the disruptive payment model – and processors such as mPowa, Elavon and Charge Anywhere, and of which the major POS manufacturers had long dreamed and anticipated. The first "mixed" payment terminal deployments (Unicapt/Windows CE for Ingenico, for example, in the 90s), or the launch of iPA, again by Ingenico (a PDA linked to a mobile payment terminal) and finally all the more recent initiatives launched by Ingenico and VeriFone to "offer" the POS at no charge, in exchange for a transaction processing contract³ were in some respects the forerunners of today's developments. As Christopher Cooner, EVP, Global Solutions,

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sales and marketing, Ingenico has pointed out, these new “SmartPOS” open up new markets, and won’t cannibalize classic POS market except marginally, a market that also has evolved in terms of functionality, no doubt to more closely resemble that of smartphones and tablets.

Big POS had a good run. The last demonstration to date was given by the Commonwealth Bank of Australia, which just announced the joint launching during the first quarter of next year of a POS in the form of a 7’-screen Android-based platform with secure EMV PIN interface, printer and merchant terminal functionality, as well as a platform called Pi enabling application developers and businesses to create applications for business use and distribute them through CommBank Pi’s AppBank to merchants. Basically the Appstore model applied to payment. The bank, which is setting several worldwide “firsts”, will also launch next month a mini-reader of iPads and iPhones, known as Leo, based in Ingenico’s iSMP technology. “Both Leo and Albert represent the future of merchant terminals and open a new innovation ecosystem to developers and businesses alike,” declared a bank representative.

¹The reference mark in terms of the smart security industry will be held from November 6-8, 2012 at the Paris-Nord Villepinte expo center.

²To our knowledge, no PA-DSS (Payment Application) label has been given to a mobile payment application.

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³VeriFone developed this “fee-free” model for London and New York cabs.