Belgische Mededingingsautoriteit
BMA-ABC
Autorité belge de la Concurrence

Discussion of ‘‘Economics of Payment Cards”

28 November 2014
Pros and cons - Stockholm

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Summary of the presentation

- membership and usage externalities
  - the number of members of a network raises the attractiveness of the network for the other side
    - cardholders and merchants
  - interchange fee paid by merchants is based on usage
- number of transactions depends on the allocation of transaction fees
  - interchange fees help internalize the complementarity between services on both sides
  - but, theoretical arguments suggest that platforms will set higher interchange fees than socially optimal
  - difficult to identify optimal interchange fees in practice, even using simple models
    - average surplus and elasticity on both sides

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Summary of the presentation

- optimal IF
  - "optimal price structure and level of IF depend on hardly observable demand properties (no rationale for cost-based cap regulation)"
  - Tourist-test:
    - "a merchant discount passes the tourist test if and only if accepting the card does not increase the merchant's operating cost"
    - MIF such that card payments do not harm merchants
- "effect of NSRs on the social welfare is ambiguous"
  - Bourguignon, Gomes, and Tirole, 2014: "Banning surcharging increases welfare if the merchant fee is sufficiently high (above the tourist test level) and decreases welfare otherwise"
- MANY more relevant questions!

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Messages for policymakers?

- broad picture: card payment associated to significant welfare benefits
  - reduction of crime, fraud and… costs for all parties
  - environmentally friendly
- how does the literature on two-sided markets contribute to the choice of policy options?
  - e.g., ex post competition enforcement Vs ex ante regulation; EU-wide approach for cross-border and national payments?
  - increasingly complex literature
    - difficult to disentangle first-order effects from second-order effects… and third order effects
  - back to basics?
    - *interchange fees can help internalize the complementarity between services on both sides*
    - *but, platforms may introduce too high interchange fees*

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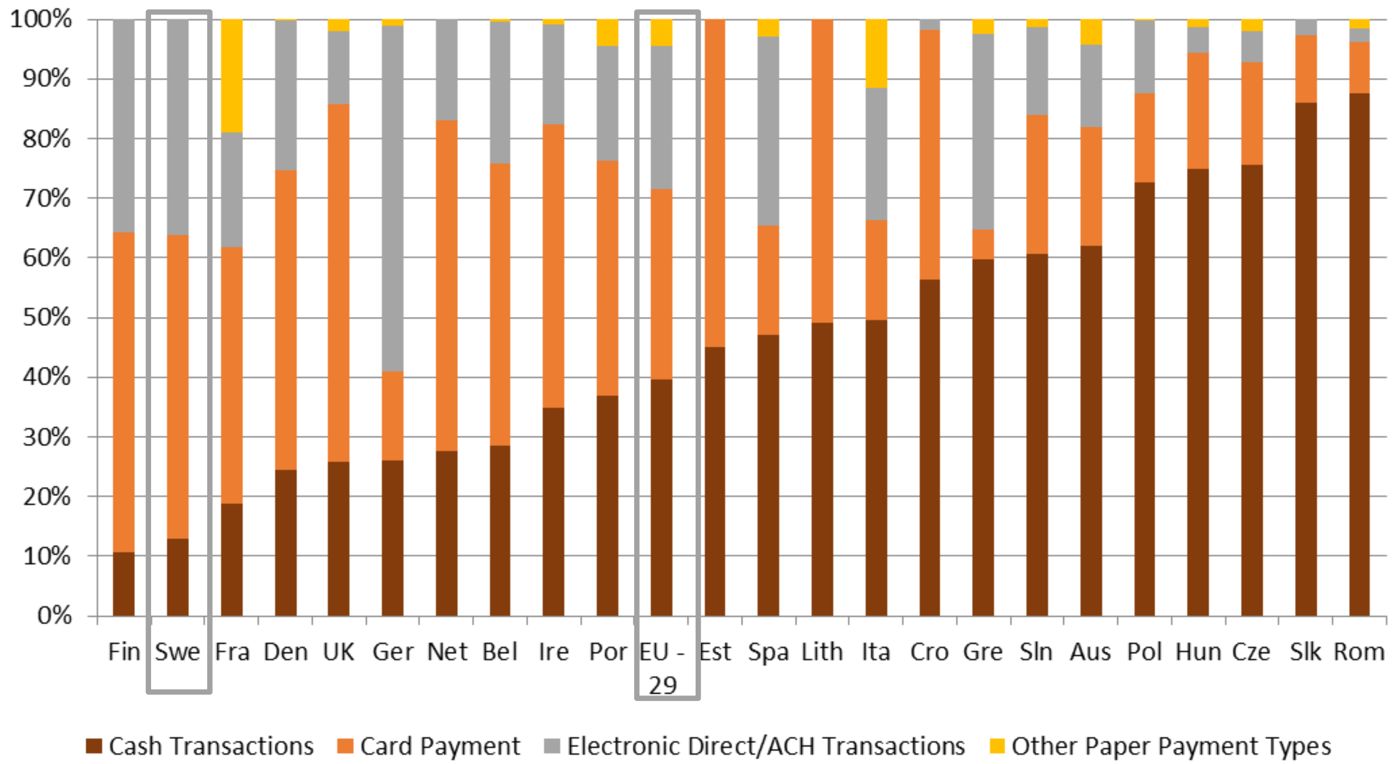
Law of one price (interchange)?

- the European Commission is not satisfied with significant interchange differences across Member States
  - “Visa's MIF levels show wide divergence between Member States. The weighted average MIF level ranges between 0.20% - 1.40% for consumer debit cards, and between 0.30% - 1.50% for consumer credit cards depending on the Member State.” [FAQ: Visa Europe decision 26/2/14]
- different policy objectives?
  - significant differences in cash vs card payments
  - shadow economy more prevalent in some Member States
    - should policies target consumers or merchants?
    - Rysman (2007) establishes a positive correlation between merchant acceptance and consumer usage
    - Carbó-Valverde and Liñares –Zegarra (2013): MIF scrutiny increases the number of transactions per card

Significant cross-country differences



Source: MasterCard; by transaction value (2013)

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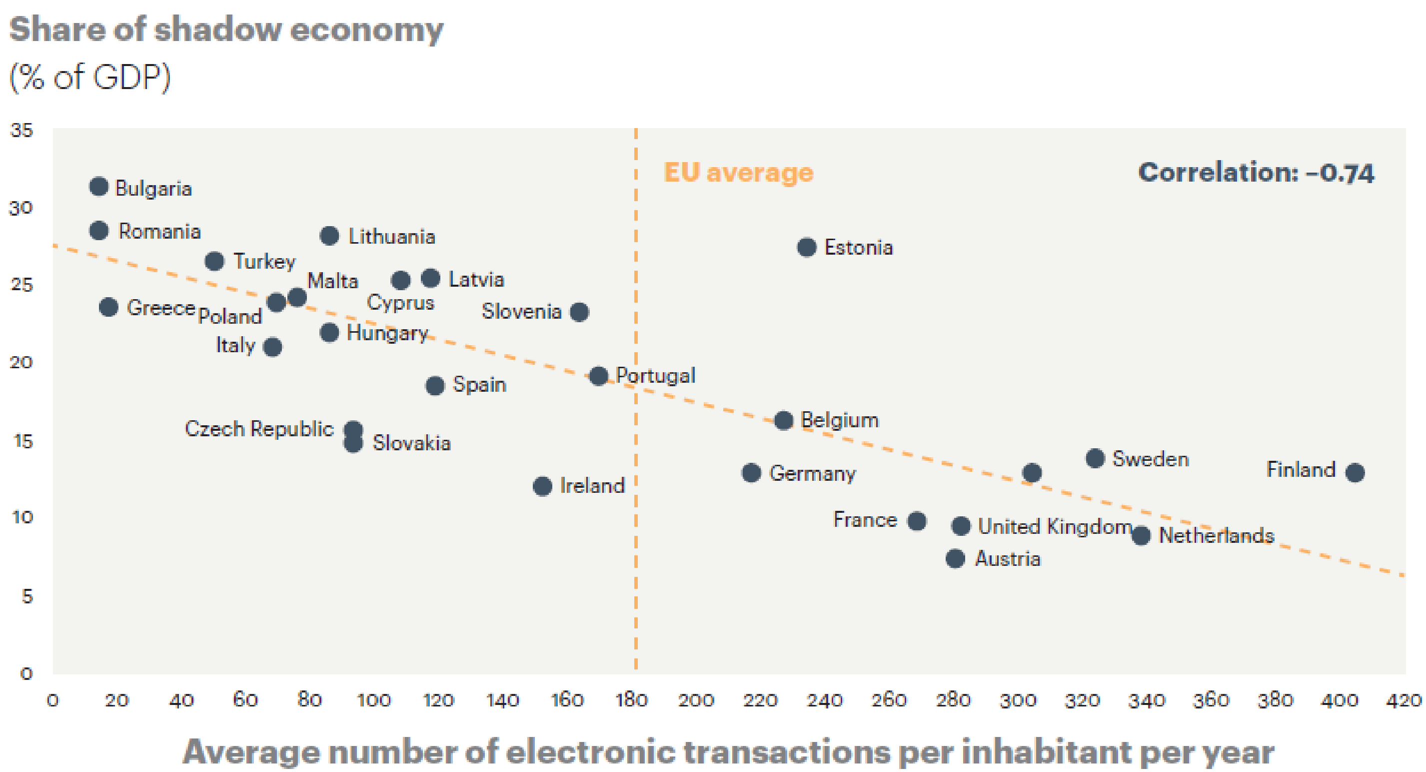

Source: AT Kearney and F. Schneider "The Shadow Economy in Europe, 2013"

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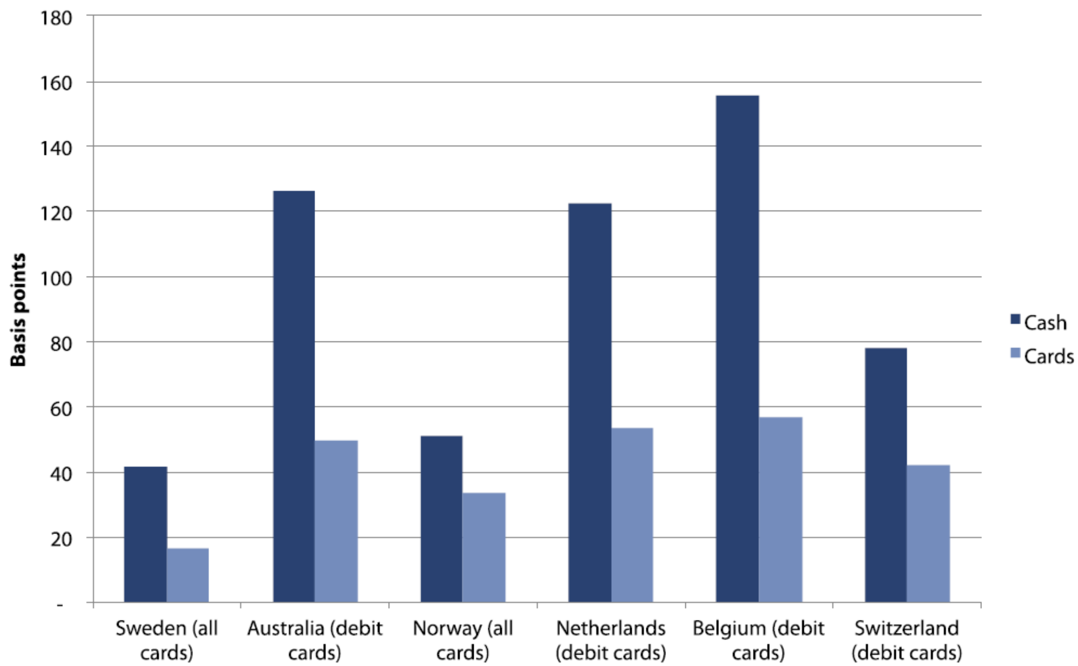
Law of one price (interchange)?

- what would the tourist test advise?
  - do benefits of merchants differ significantly across countries
  - answer when the Deloitte study will be published?
  - DotEcon (2011), “Costly cash”



Competition Vs Regulation

- a number of competition investigations
  - US, EU, Member States, Australia,…
  - EU-level
    - MasterCard (2007) upheld by the General Court (2012) and the European Court of Justice (2014): cross-border MIFs 0.2% (debit) and 0.3% (credit)
    - Visa (2010) and Visa (2014): cross-border and national transaction MIFs 0.2% (debit) and 0.3% (credit)
  - European Court of Justice (2014) in Groupement des cartes bancaires ruled in favour of restrictions *by effect*
- ex ante regulation of MIFs discussed with Member States and the European parliament
  - cross-border and national transaction MIFs 0.2% (debit) and 0.3% (credit)
  - + absolute limit for debit transaction €0.07?

Competition Vs Regulation

- regulation raises a number of questions
  - Tirole (2011) lists a number of potential unintended consequences of the regulatory approach
    - the tourist test is a conservative estimate of the socially desirable IF, because it does not reflect industry profit (total welfare) and the negative externalities of cash payment (tax evasion)
    - focus on open systems favours three-party systems and large issuers or large merchants, that are able to launch preferred merchant programs

Relevance for other markets: OTAs

- role of the no-surcharge-rule
  - "We know very little about how we should address vertical restraints in two-sided markets"
- investigation of most-favoured customer clauses in the online hotel booking industry
  - Germany, UK, but also Austria, Belgium, Denmark, France , Hungary, Ireland, Italy, Norway, Sweden
  - often pan-European pricing clauses