Payments in Latin America: Under Digital Transformation

A payments industry whitepaper by Americas Market Intelligence

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Latin America has seen better days. In 2015, growth in the region declined for the fifth year in a row, to less than 1%. Growth in Mexico, Colombia and Peru hovered around 2%, while Brazil and Venezuela floundered in deep economic crisis, contracting 3% and 10%, respectively¹. Unfortunately, 2016 has brought much of the same, as governments grapple with the effects of slack Chinese commodity demand, devaluing currencies and rising inflation.

One bright spot in the region, however, is payments. Although the rate of increase is smaller than in the past, credit card spend is still growing. E-commerce is robust, with projected double-digit growth for the next several years. Local fintech startups are disrupting age-old financial systems like lending and scores of mobile wallet launches demonstrate investor determination to usher in the next wave of payment technology. And with ~75,000 users in its first month, BIM, a new mobile money platform in Peru may be changing the nature of financial inclusion.

Certainly, the payments space looks very different than it did just five years ago. Banks and acquirers—highly consolidated, powerful legacy players—are seeing their dominion over financial services threatened by local and international tech companies who offer everything from cross-border remittances to cash-based e-commerce payments to consumer loans. In response, banks, card networks and processors are investing in technology to 1) make banking cheaper; 2) win over new customers; and 3) engage with customers in new, exciting ways.

To do this, banks are shifting their investment dollars away from credit cards in sharp contrast to their retail strategy over the past 20 years. Few of the region’s largest markets saw the launch of personal credit cards in 2015. Instead, banks and acquirers are investing in everything digital, including online banking platforms, mobile apps, digital wallets, mPOS and support for e-commerce. BBVA in Mexico reports that improvements to its online offering, including online lending and a digital wallet, have resulted in attracting two million users to the online channel in just 18 months compared to the 1.5 million users it attracted over the previous 10 years. The digital channel is here to stay and will only become more entrenched. Credit cards still lie at the center of retail banking—issuers are simply implementing technology to help consumers use them in new ways. This is smart.

Consumer credit is plateauing in Brazil, and card issuing is actually declining in Mexico as consumers avoid over-indebtedness. Cardholders’ interest in the credit instrument is waning. Banks now need to teach their customers to employ cards for everyday needs like groceries and gas as opposed to expensive goods bought with credit. To do this, issuers are embracing emerging payments and channels, hoping that new technology is sexy enough to keep Latin Americans tied to their cards and away from cash.

The mobile phone is at the center of payment innovation for the unbanked as well. Payment companies continue to look for ways to convert paper money into digital currency, namely in the form of stored value on cell phones. Telcos have been trying to achieve this for years without great success, but market players are not giving up. A trend toward interoperability, led by the Peruvians, may provide best practices for success. PayPal recently announced partnerships with Telcel and Claro to support mobile money; TransferTo, a mobile money hub for telcos, announced an alliance with Tigo, to help scale Tigo Money. Last year, Huawei expressed interest in mobile money in Colombia. No one has learned how to turn a profit on financial services for the unbanked, so the continued interest in such products is puzzling. Everyone is optimistically betting on capturing a piece of a pie that does not yet exist.

2016 is seeing a wave of digital disruption not previously witnessed in Latin America—and the trend is clear: digital is in. However, much of these technological developments require a change in consumer behavior, which is notoriously inflexible. We must remember that 70% of Latin Americans do not have a bank account, 60% of transactions made by SMEs are in cash and 47% of employees work in the informal economy. E-commerce accommodates a minority population, and digital wallets cater to an impossibly small market. These products are sure to grow but are far from certain to become profitable in the short term. Most likely, it will be generational change that brings these products to scale, meaning robust revenue is potentially decades away. Latin American payments are changing rapidly, but a long road of digital transformation is still ahead.

¹ International Monetary Fund data.
Trends in digital payment technologies for the affluent

Chapter 1: Investment in mobile payments ignites a fight for the digital wallet space

Despite concerted efforts, profitably serving the unbanked remains a quagmire. Banks are re-strategizing to focus on digital wallets for smartphone users

In recent years, banks, card networks and telcos have demonstrated great optimism regarding mobile financial services for the unbanked. But after 8+ years in operation, such initiatives remain woefully unprofitable, triggering a move away from the unbanked by some market players. In a recent interview with Electronic Payments International, the Miami-based technology provider YellowPepper noted that “providing banking services to the unbanked wasn’t paying enough for us to survive, so for the time being we’ve left that market.” 2015 saw the fruits of an alternate strategy: the development of mobile financial services for affluent consumers.

Smartphone penetration in the region is roughly 45% in 2016, totaling 175 million, and is forecasted to grow by 12% annually through 2019. In four years’ time, 73% of Chileans and 70% of Mexicans will have smartphones. So banks have refocused on smartphone-based financial solutions—namely, contactless mobile payments and digital wallets for e-commerce.

New technologies emerged in 2015/2016

2015 saw the launch of at least six mobile wallets for contactless payments at brick-and-mortar merchants, involving big players such as MasterCard, Bancolombia, and BBVA Bancomer. This year, PROSA, and Grupo Aval threw their hats in the ring and SamsungPay launched in Brazil. BBVA plans to launch the first mobile wallet in Peru in 2017. Despite a lack of evidence that such technologies will gain traction, investment in digital payments is going full steam ahead. Developing merchant networks and providing consumer incentives for mobile payments will be crucial for their success.

Many newly launched contactless wallets do not require NFC technology, including the much anticipated SamsungPay, but rather build on existing POS infrastructure.

Apart from Brazil, NFC POS penetration in Latin America is low (e.g. 5% in Colombia) and NFC-enabled smartphones (such as the iPhone 6) are very few in number compared to Android-based handsets. Undeniably, the solutions most likely to succeed are those that are cheap and easy to roll out and not dependent on the installation of new hardware. With such low NFC infrastructure and the dominance of Android in the region, the launch of ApplePay in Latin America is likely far off, giving local solutions and SamsungPay the chance to battle for leader status.

Also notable in 2015/2016 were developments in digital wallets to enable e-commerce. LatAm markets experienced a late onset of e-commerce thanks to customer misgivings about security, clumsy online stores and limited credit card penetration. Nevertheless, a maturing market and robust growth projections (approximately 15% through 2019) have led payment companies to take e-commerce more seriously. Now, payment players are in the throes of competition for e-commerce spend via wallets.

PayPal and Visa are leading the charge in streamlining e-commerce transactions. Visa launched its digital wallet Visa Checkout in Mexico, Colombia and Brazil last year, in an effort to increase conversion rates. Although the Visa Checkout launches were highly publicized events, the momentum in signing up additional merchants seems to have waned in 2016. PayPal launched is OneTouch feature globally in Q2 2016, enabling customers to make one-click purchases. Banks, historically overzealous in refusing e-commerce transactions for fear of fraud, are recognizing this missed opportunity: In 2016 they have sought to enhance the consumer e-commerce experience through improved anti-fraud and authentication tools.

As market players align around e-commerce growth, new opportunities will emerge for processors, gateways, merchants and technology companies alike.
Bringing digital wallets to scale will be no easy task

During banks’ romantic pursuit of the underbanked, they took their sights off the needs and wants of their most valuable customer base. Latin America’s wealthy have long been weary of conventional credit products and reward programs that do not reflect who they are. Today, affluent Latin Americans are hungry consumers of international goods, services, and content: They pine after the technologies available in the developed world. Banks must honor these aspirations if they want to capture the loyalty of the big spenders of today (middle-aged professionals) and tomorrow (technology driven 20-somethings). To do this, they must enable technology-based payments and consumption.

Contactless payments and e-commerce wallets are a start, but formidable hurdles remain for these products to exhibit high consumer adoption. Without investment in continual merchant training, contactless payments will be dead on arrival. Moreover, consumers need constant reminders and incentives to tap on their phone instead of swiping their card at a POS. Banks, processors and payment gateways must collaborate to convince consumers it is safe to buy online, and merchants need assistance building clean, professional online stores. Finally, once new payment technologies are accepted by the region’s upper-crust users, market players must pursue strategies to target the traditional and emerging middle classes, especially by expanding access to electronic payment methods.

While banks distance themselves from the unbanked, it appears that the digital age of payments has arrived in Latin America. Competition to capture payments in both the physical and online realms will grow fiercer. While the digital wallet space for physical transactions is still nascent, banks and payment companies are already in the throes of battle for e-commerce market share. As product offering becomes more sophisticated and consumers climb the online shopping learning curve, lame ducks will fail. There is a long road ahead for full digital payment adoption, but with so much investment in the space and competition whittling away bad providers, digital adoption will continue to accelerate.

Recent and upcoming contactless mobile payment launches

<table>
<thead>
<tr>
<th>Product</th>
<th>Country</th>
<th>Launch date</th>
<th>Involved entities</th>
<th>How it works</th>
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<td>Billetera Móvil</td>
<td>Q3 2015</td>
<td>Bancolombia, MasterCard</td>
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<td>Aval Pay</td>
<td>Q3 2015</td>
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<td>Smart Wallet</td>
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<td>Yepex Wallet</td>
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<td>NFC, BLE, QR codes, six digit one-time passcodes</td>
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<td>BBVA Wallet</td>
<td>Q2 2015</td>
<td>BBVA Bancomer</td>
<td>NFC, Host Card Simulation</td>
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<td>PayClub</td>
<td>Q2 2015</td>
<td>Diners Club of Ecuador, Banco Pichincha, YellowPepper</td>
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<td>White label digital wallet for banks</td>
<td>Q2 2016</td>
<td>Partnership between PROSA and Gemalto</td>
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As e-commerce in Latin America becomes more sophisticated, e-commerce enablers must up their game

E-commerce retail sales in Latin America will exceed USD $50 billion in 2016, according to eMarketer. Compare this to US retail e-commerce, clocking in at USD $341 billion in 2015, and Latin American e-commerce looks decidedly underdeveloped. The reasons for this are well known: bank rates hover at around 30% and fear of fraud deters even affluent credit card holders from shopping online. A lesser-understood reason is that local e-commerce payment enablers and banks lack some technological expertise, resulting in too many authentic transactions being declined. In Mexico, this number is 14%. In Peru, it can reach 60%.

The good news is that e-commerce in Latin America is expected to grow by 15% annually through 2019—by as much as 11% in Brazil and 40% in Peru. Organic growth is part of the reason but so is a concerted effort by payment enablers to improve the customer experience—an opportunity that is inviting ever more competition.

E-commerce enablement in Latin America remains a fragmented industry. In Brazil there are at least 20 e-commerce payment gateways—technology companies that enable online payments for merchants. In Colombia, which represents just 9% of Brazil’s e-commerce market, there are 10. Peru, smaller still, has at least eight. Going forward, competition will ramp up in three distinct ways: 1) existing leaders will expand into new markets and improve their product offering; 2) local startups will enter the market; and 3) new international gateways will arrive in Latin America for the first time.

Market leaders

Regionally, market leaders include PayPal, PayU and MercadoPago. PayPal established local presence in Brazil and Mexico in 2010 and 2012 respectively and has since expanded local service to Chile, Peru and Colombia. PayPal has excelled at gaining consumer trust of its brand thanks to its enhanced security and value-added services, such as free return shipping for remorseful buyers. PayU has the largest footprint in e-commerce enablement in the region with presence in seven markets; growth is in the triple digits for newly launched markets such as Peru. As a Colombian company, PayU has positioned itself as the Latin American e-commerce expert. In 2015, MercadoPago partnered with Alipay to enable payments in Mexico for AliExpress (Alibaba), the largest marketplace in the world.

But where PayPal, PayU and MercadoPago have achieved regional recognition, other gateways have faltered. The region is littered with less sophisticated companies that have unstable and insecure platforms, which can result in dismal conversion rates of under 50%. As consumers climb the e-commerce learning curve, their user experience expectations increase and merchants become less tolerant of shoddy service.

Emerging local competition

New local players want to capitalize on the mediocre service of incumbents. Conekta, established in Mexico in 2012, enables advanced features less commonly found in Latin America, including recurring payments, card-on-file and anti-fraud tools that negate the need for authorization via 3D Secure. Similar launches include AstroPay, which specializes in enabling local payment methods for cross-border e-commerce, and Peru’s Culqui, catering to the m-commerce market. As these companies consolidate in their home countries, we can expect regional expansion, with a focus on small and medium businesses that need excellent customer service and intuitive tools.

Additionally, local payment gateways and merchants are capitalizing on cash payments for e-commerce. The boleto bancario, a cash-based invoice used religiously in Brazil, actually gained share in e-commerce in 2015, ticking up from 18% of transactions to 19%. This is due in part to Brazilians rejecting credit in a more economically challenging climate. But another factor is the increasing number of e-merchants who are accepting boletos for the first time. SafetyPay, a Miami-based cash payment enabler, has expanded throughout the region to 14 markets and is actively integrating operations with local gateways.

PagoEfectivo, a Peruvian competitor to SafetyPay, launched the country’s first prepaid card specifically for e-commerce in October 2015. By enabling these alternative payments, merchants tap into two severely underserved segments: card holders who are afraid to use a credit card online, and uncarded customers who are otherwise shut out of the e-commerce channel.

Traditionally, many merchants have preferred international gateways because of their technological superiority, better authorization rates and lower fees. But as the local gateway offering improves, merchants region-wide are switching...
to local providers. Emerging local competition is trouble for international gateways, including 2Checkout, Adyen, and Global Collect, which face the disadvantage of not being plugged into local processors in all markets. As such, transactions are charged in foreign currencies and consumers are assessed FX fees. Merchant earnings are stored abroad, necessitating costly wire transfers to the local market.

**International players**

This does not stop new international players from being attracted to Latin America in the belief that they can outwit or outmuscle the region’s local solutions. The most prominent example is Stripe, which is in pursuit of the burgeoning m-commerce segment. Stripe wants to launch its own product in beta phases in Brazil and Mexico to serve the underpenetrated segment of in-app payments and payments via social media. It faces little or no competition in this endeavor.

As the e-commerce market matures, international payment companies are launching ever more sophisticated products into Latin America, encroaching on the turf of legacy players. Visa launched Visa Checkout—a card-on-file wallet—in Mexico, Colombia, and Brazil in 2015 and PayPal’s OneTouch feature makes e-commerce more seamless. E-commerce giant AliExpress has made significant strides with its proprietary gateway, AliPay, and YellowPepper is powering multiple digital wallets in Colombia, Mexico, and Ecuador.

**Heyday for merchants and consumers—a test of cunning for payment companies**

A turbulent competitive landscape is a win for merchants and consumers. With increased competition, consumers enjoy an improved e-commerce experience, enhanced convenience and a lower risk of fraud. Merchants benefit from declining fees and can offer better customer service as greater competition pushes slack providers out of the market.

One downside for international merchants, however, is the complexity of the e-commerce enablement landscape from a regional perspective. There is no one provider to enable e-commerce for all of Latin America, a disappointment for merchants expecting an easy LatAm solution. Gateways that 1) have presence in multiple markets and 2) enable local payment solutions, such as PayU and AstroPay, have the best shot at international merchants and their lucrative cross-border sales. But international merchants unfamiliar with these lesser-known brands are often gun-shy when it comes to using a local solution. Regardless, a multi-faceted approach to Latin American e-commerce is required.

Payment gateways, both big and small, are under fire from all sides. Large players need to measure the competitive dynamic and identify acquisition targets or weaknesses that they can exploit with their own service launch. Start-ups, armed with superior technology, need quick wins and the right partners to scale up their operations. New players in search of funding must prove to investors that their offering is superior to what is found in the market. In short, competition is growing fiercer—and to compete, companies must understand both the context and competition.

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4 3D Secure is technology offered by Visa and MasterCard for card-not-present transactions, which requires the user to authenticate his/her identity, thereby enhancing security. However, authentication adds an additional step to any e-commerce transaction and results in significantly lower authorization rates. Gateways are attempting to bypass the process using their own security features.

Chapter 3: Homegrown solutions are capitalizing on m-commerce opportunities

M-commerce opportunities vary widely by country and require understanding of the local context

M-commerce has been slow to launch in Latin America, with a number of structural factors inhibiting its scale. Both merchants and consumers have yet to navigate the m-commerce learning curve. Estimates are that in Brazil, for instance—by far the region’s most mature market—fewer than 5% of merchants have an m-commerce site, forcing mobile customers through a clumsy, non-optimized shopping experience. Card-on-file features are scarce, requiring users to enter their 16-digit card number for each individual purchase. High-speed internet has expanded impressively in recent years but is still limited: 50% of mobile connections are still covered by 2G⁶ 7. As a result, m-commerce represents less than 10% of total e-commerce sales region-wide.

But the ground is being laid for swift m-commerce growth, due to the rapid expansion of smartphone penetration and 4G coverage. Currently, roughly 40% of Latin Americans have smartphones. By 2019, this number will exceed 70% in Mexico, Colombia and Chile and reach 57% region-wide. Additionally, by 2020 the GSMA expects 75% of all mobile connections to be covered by 4G and many Latin Americans will come online for the first time via a mobile device. As a result, in 2016 mobile commerce sales is growing by 40%-60%, depending on the market.

M-commerce growth driven by homegrown solutions

Certain segments will champion this growth much more than others. Transportation has been one of the first segments to excel in m-commerce, led by Brazil’s Easy Taxi and followed by Uber. In Latin America’s traffic-choked cities, the on-demand economy is a major driver of m-commerce for other types of products as well. The region already has a strong culture of cheap, same day delivery—much more so than the US—for virtually any type of product, from medication to hard liquor to fresh steaks. The digitization of delivery services is low-hanging fruit for m-commerce, especially among the young, rich, and urban, and local companies are experiencing the greatest success.

Take iFood, Brazil’s largest online marketplace for restaurant delivery services. Founded in 2011, iFood allows consumers to browse nearby takeout options and make orders online. With 200,000+ delivery orders per month—75% of them placed via mobile—iFood estimates it is capturing 80% of the online takeout market valued at USD $1.5 billion⁸. A large part of its success comes from enabling small, informal restaurants to utilize the service, even if they do not have a broadband connection. This is done using a special iFood POS device, connected via 3G, that receives and prints orders—crucial in regions where broadband penetration is limited and doubly so among local mom-and-pop establishments.

Digital retail sales*, 2015, USD billions

Sources: eMarketer, E-bit Internet Retailer, interviews, AMI analysis
*Excludes travel and event tickets

⁸ Ruvolo, J. 2015. “iFood Raises USD $50 Million From Movie And Just Eat For Food Delivery.” Tech Crunch.
Restaurant food is only a small slice of the enormous delivery market being disrupted by m-commerce. Rapiddo is an Uber-style service providing on-demand package delivery via motorbike, bicycle or van. In São Paulo, where traversing the city can take longer than an international flight, such services are embraced wholeheartedly.

Local companies are transforming other segments as well, including retail. In Latin America, 90-95% of mobile users are on a prepaid plan, purchasing data in bundles to be used on social media and messaging. Customers are reluctant to deplete their limited data by visiting websites and online shopping suffers for it.

MUV, a Brazilian mobile marketing firm, is finding ways around this. It has developed a product enabling consumers to surf merchant sites on their cell phones for free without consuming any data. A pilot launched in November 2015 with Netshoes, a popular sporting goods e-retailer, yielded astounding results. In the month of November, mobile surpassed desktops in visits for the first time ever and 3G visits experienced higher conversion rates than Wi-Fi visits. App downloads grew by 150% and the mobile channel now accounts for 40% of all NetShoes’ online traffic.

M-commerce will undoubtedly grow in coming years, even in Brazil, which is going through its second year of recession. But m-merchants must understand the particularities of Latin America when attempting market entry. Internet access is dodgy, local logistics are a nightmare and social media dominates mobile activity. Merchants must invest in mobile channels and devise new ways to encourage mobile purchasing in order to stay relevant as the on-demand app space inevitably grows more competitive. Most importantly, Brazilian companies understand their own reality and cater to Brazilians’ needs. Multinationals attempting to penetrate m-commerce must follow their example to compete.

**M-commerce payments**

Overcoming deficient connectivity is only one part of the equation, however. In Brazil, where payment card penetration is relatively high at 59%⁹, m-commerce companies have a huge addressable market among carded consumers only. While cash-based boletos bancarios are a mainstay of Brazilian e-commerce, on-the-go goods and services consumed in the mobile channel are not typically compatible with this payment method.

But in other, more underdeveloped markets, the preference for cash remains a huge barrier to m-commerce. Mexico is a prime example. According to a study conducted by BuzzCity, a mobile advertising company, Mexican m-commerce is heavily concentrated in two product categories: mobile airtime top-ups and mobile content. Less than 10% of mobile users have purchased a physical good using a phone and 56% of users report never having made an m-commerce purchase¹⁰. The most often-cited reason for hesitancy is fear that mobile transactions are not secure; the runner-up is a strong preference to pay in cash. Of Mexican m-commerce customers, only 5% report that a credit card is their preferred payment option—trailing behind carrier billing, cash payments at authorized agents and cash on delivery.

In Peru, the m-commerce environment is even more stunted. Overall m-commerce amounts to less than 5% of all e-commerce sales and is heavily dominated by taxi apps such as Uber and Cabify. Moreover, airtime top-ups were not even available for purchase via mobile apps until July 2015, when MNO Entel partnered with VisaNet to develop a card-on-file app. Using the app, customers can now top up their mobile accounts and pay monthly bills after registering a Visa card. Entel represents only 7% share of mobile users, however. Telecom giants Movistar and Claro have not yet developed these capabilities. In Argentina, with a robust, tech-savvy middle class, demand for digital goods and services is severely repressed for lack of electronic payment methods; cash still represents 40% of all online spend.

So m-commerce has a long road ahead outside of Brazil, and both merchants and payment companies must coordinate to promote its adoption. There is a clear opportunity to develop and promote card-on-file capabilities in mobile apps and sites. Visa is leading in this space with last year’s launch of Visa Checkout, but there is ample room for competing products from gateways, banks, networks and other tech players.

Additionally, markets outside of Brazil are just as ripe for disruption in terms of m-commerce delivery services, but for the strong preference of paying with cash. Credit card penetration goes as low as 21% in Peru, precluding access to card-only m-merchants to a huge percentage of the population. Although costly to merchants, enabling cash-on-delivery attracts first-time users to m-commerce, especially those with no other device through which to place orders. While mobile will grow, organic growth can only take merchants and payment providers so far; smart innovation around local problems is essential to win.

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¹⁰ BuzzCity. 2015. “Mexico: M-Commerce Profile”
Chapter 4: As mobile money in LatAm gains ground, feasibility and utility are still questionable

Latin America leads the world in mobile money growth but success remains highly speculative.

Having first experienced success in Africa, mobile money attempts to provide financial services to the unbanked by converting the mobile phone into a digital wallet. In Latin America, where 70% of people do not have a bank account, investment in mobile money has gained ground steadily in the region since 2007. At the end of 2014, there were 37 live services deployed in Latin America and the region is leading the world in mobile money user growth (50% in 2014). There were five new mobile money launches in 2015 and two regional giants, PayPal and America Móvil, partnered to create a mobile money wallet in 2016.

However, mobile money fanfare must be accompanied by a heavy dose of reality. Today, mobile money has reached only 3% integration, insignificant in a region of nearly 480 million adults. Very few services have reached scale; only two mobile money platforms in LatAm exceed 10% of all mobile subscriptions—Tcho Tcho (Haiti) and Tigo Money (Paraguay)—and profitability in the region fares just as poorly.

According to the GSMA, the road toward profitability is a long one and it usually takes between 36 and 48 months to achieve just 2-5% profit margins. To do so, operators must invest in the development of a robust digital payments ecosystem. Interestingly enough, it is the region’s newest deployments that are doing this through investments in interoperability.

Two new launches are setting precedent for interoperability

2015 and 2016 have been milestone years for Latin America, as they saw unprecedented progress in mobile money. This progress was characterized by the launch of the world’s first mobile money service operated by a Central Bank in Ecuador and the development of a fully interoperable platform in Peru.

Ecuador

Ecuador made global headlines for its Dinero Electrónico, a government-run mobile money service launched in Q1 2015. Ecuador’s Central Bank, the world’s first to issue electronic money, created interoperability by striking deals with both Claro and Movistar.

Currently, 11 banks and 40+ credit unions had joined up, though not without controversy. Initially, Banco Pichincha, Ecuador’s largest bank, declined to participate. Analysis speculated that this was in order to oppose left-leaning President Correa, acting out of concern that Dinero Electrónico was actually a state attempt to muster control over the issuing of currency—as a dollarized economy, Ecuador cannot dictate monetary policy. While the law requires all mobile money to be backed by a physical dollar bill, critics worry that with exclusive control over electronic money the government will eventually use the platform to compensate public employees and pay off public debt—or the beneficiaries of unsavory dealings.

All speculation aside, the truth is that Ecuador’s Dinero Electrónico is so far just scraping by, managing to round up only 140,000 users in its first 18 months (the government’s goal was one million in the first year.) Significant obstacles abound: since banks were not originally included in the platform, neither were their correspondent agents. Also, since Dinero Electrónico is run as a public service, low government-set fees do not encourage banks to push the service out to consumers. After a year in operation, USD $760,000 were in circulation in the Dinero Electrónico platform. Compare this to the government’s goal of USD $80 million in five years, and it is evident that Dinero Electrónico is not living up to expectations.

Despite widespread skepticism, Ecuador’s mobile platform is the region’s premiere money service and the first to be truly low-cost to both consumers and merchants. There is no doubt that Ecuador, one of the poorest countries in South America, needs expanded access to financial services, and some believe Dinero Electrónico is the first step in this direction. Others believe it is doomed to fail.
Peru

In contrast to Ecuador’s publicly run mobile money platform, Peru’s BIM is the result of a four-year collaborative effort coordinated by Peru’s Bankers Association. Launched in February 2016, BIM is interoperable among three telcos and 30+ financial institutions—a significant feat that is unprecedented globally. The platform is supported by Peru’s robust network of bank and non-bank correspondent agents (60,000 in total), although these are concentrated in Lima and other metropolitan centers. BIM initially enabled peer-to-peer payments, cash-in/cash-out and mobile top-ups and merchant payments and in the process of being rolled out. Because they are priced at USD $0.15 per transaction, the hope is that fees will not deter Peru’s poor and unbanked, the service’s prime target. In its first four months of operation, BIM accumulated 120,000 users.

BIM is a long-term investment for banks and reflects their attempt to support financial inclusion. It will take at least five years to grow to scale (five million users). For now, all fee revenue will flow to Pagos Digitales Peruanos, the company established to oversee BIM, and banks will only see a return on their investment when cross-selling opportunities become available. This hope is pinned on two uncertain developments: 1) that the service achieves scale; and 2) that the platform proves an efficient way to deliver additional banking products, such as savings accounts, loans and insurance to Peru’s underbanked. Those involved are optimistic but success is still highly speculative. Either way, Peru has achieved something truly unique in the region: a fully interoperable, privately run system based on voluntary participation. Time will tell if users are as keen on the system as the operators.

Mobile money and utility: Is mobile money really practical for users?

Despite these developments, mobile money in Latin America is not yet of great utility to users, as demonstrated by low uptake rates. Latin America is overwhelmingly a cash economy, and consumers are not yet swapping their beloved cash for digital currency. Promotional videos for both BIM and Dinero Electrónico showcase excited users typing into a mobile phone to buy a one-dollar cup of coffee from a street vendor. This scenario is far from reality. Fear of fraud, mistrust of banks, technological illiteracy and the simplicity of cash are all deterrents to mobile money’s widespread adoption. To prosper, mobile money must solve daily problems and increase convenience. So far, with the exceptions of Haiti, Paraguay, and select cases in Central America, it does not.

Facilitating utility bill payment may be the best strategy toward this end. Across Latin America, consumers experience the inconvenience of shockingly long lines to pay for utilities such as water and electricity. Peer-to-peer payments offer a practical solution but well-entrenched money wiring firms are already top-of-mind among remittance senders. For either BIM or Dinero Electrónico to flourish, they must 1) make the lives of their customers more convenient; and 2) displace models that already attempt to do this. If they succeed at these two tasks, consumers may be convinced that mobile money is worth the trouble after all.

¹¹ Almazán, M. and Jennifer Frydrych. 2015. “Mobile Financial Services in Latin America and the Caribbean: State of play, commercial models and regulatory approaches” GSMA.
Chapter 5: Why financial inclusion efforts in Latin America may be missing the mark

The poor are adopting smartphones much faster than bank accounts, yet mobile money platforms are directed almost exclusively at feature phone users

In Latin America, where 70% of people do not have bank accounts, both the public and private sectors have homed in on financial inclusion as a strategic objective for growth. Mobile financial services for the unbanked have flourished in the region since 2007—there are nearly 40 live mobile money platforms, with five new launches in 2015. However, while mobile money efforts have been successful in Africa, uptake is minimal in Latin America despite concerted efforts by every major telecom and bank to promote such services. Of 480 million adults in Latin America, there are a mere 15 million registered mobile money users (3% penetration), of which only six million were active, defined as using the service in the past 90 days. Deficient agent networks, technological illiteracy, a lack of interoperability and the plain old convenience of cash can all be cited as reasons for poor mobile money penetration.

Very few mobile money services in LAC have reached profitability. As a result, some providers have migrated away from the unbanked. Banks and card networks are dedicating significant resources to launch services for their banked customers, including m-commerce mobile wallets and contactless merchant payments.

Yet providers may be missing out on an intriguing opportunity. Almost all mobile money platforms worldwide are developed for feature phones under the assumption that the unbanked cannot afford smartphones. But smartphone penetration in the region is at 45% in 2016 and forecasted to grow by 12% annually through 2019. This is much faster than the rate of bank product adoption by the unbanked. The World Bank reports that in Colombia, bank penetration grew only 2% annually from 2011-2015. By 2019, 60% of Latin Americans will have smartphones; the number of unbanked (70%) will not have noticeably budged. This means that the ranks of unbanked Latin Americans using a smartphone versus a feature phone is growing—and quickly.

So mobile money operators who are focused on low-tech interfaces for feature phones may be developing the wrong types of products. Unbanked smartphone users are an entire demographic for which financial inclusion products have not been developed. Indeed, one self-admitted flaw of Peru’s mobile money service, BIM, launched in Q1 2016, is that it is clumsy and slow for smartphone users who are used to switching seamlessly between apps. Considering the projected rapid growth of smartphone penetration, mobile money services may become obsolete before they even become mainstream.

Growth of smartphone usage aside, there may be another reason to target more high-tech consumers. Mobile money uptake has been so low in part because its main users are marginalized, poorly educated and highly suspicious of banks and technology. But the unbanked population is diverse and includes young, lower middle-class urban dwellers who, in many cases, have smartphones. These users are more tech-savvy and adaptive than feature phone users, and thus are more likely to trade in old behaviors for new ones. With regard to mobile money, smartphone users would be more inclined to trust that their cash is stored safely in their phone and to be more excited about sending money to friends electronically than their feature phone counterparts.

Nowadays, the smartphone is the mechanism by which behaviors change and old patterns are disrupted. It has transformed how we communicate, shop, bank and even hail taxis. Theoretically, if unbanked smartphone users—who are richer and better educated than feature phone users—adopt mobile money, they will want to use this technology to transact with their feature phone user friends, encouraging them to also use the service. Instead of working from bottom up with the most financially excluded, mobile money providers would be wise to let smartphone users push the service to the bottom of the pyramid for them.

¹³ La República. 2015. “Tecnología y mayor cobertura impulsan el crecimiento de la bancarización.”
Chapter 6: Traditional remittances are under attack by online competitors

Remittance providers seek to digitize the remittance journey by playing to convenience, but cash’s stronghold on money sending remains

Remittances to Latin America totaled USD $68 billion in 2015—a historical high—finally surpassing pre-financial crisis levels. The recovery of the US economy in 2013 and 2014 resulted in resumed growth of remittances to the region, particularly to Mexico, which achieved 5% in remittance growth in 2015. Increased migration largely from Central America, climbing wages of remitters and declining wire fees all contributed to this positive growth. The US-Mexico corridor is the most active in the remittance landscape. It alone represents 40%-+ of all remittance money sent to Latin America.

The remittance space in this corridor is competitive, with 15+ providers serving consumers. Most providers have vast brick-and-mortar infrastructure across the Americas to enable cash-in and cash-out transactions. Western Union, for example, has 45,000 agent locations in the US and 31,000 in Latin America. Arguably the number-two provider, Wells Fargo, is follows close behind with 9,000 stores in the US and 40,000+ cash-out agents in LatAm. Extensive retail networks are necessary, as most migrant remitters prefer cash to online transactions that call for using a computer or mobile device linked to a bank account or payment card. There are several reasons for this. Migrants in the US often have limited access to the Internet and even fewer have the resources, documentation and wherewithal to open a bank account. Since banking crises are commonplace in Latin America—the 1990s banking crisis in Mexico being just one of several examples—many are wary of banks. Fear of deportation motivates protecting anonymity and the trust generated between remitters and in-person agents promotes customer loyalty. For these reasons, retail remittances are well-entrenched. Yet despite decades of success, market incumbents are now coming under threat by online providers.

Today, the online channel represents less than 10% of total volume sent to Latin America, but it is encroaching on space traditionally owned by brick-and-mortar operators at an estimated pace of 10% annually. The much-celebrated success of low-cost money sender Xoom, present in the region since 2005, has sparked three trends: 1) market incumbents are forced to develop an online option to remain competitive; 2) additional online-only providers have come to market; and 3) prices have dropped. Today, nearly all MTOs with service in Latin America have a digital offering. Wells Fargo’s ExpressSend launched in 2007, and Western Union premiered its online option in 2011. Other online-only providers, Remitly and Transferwise, began offering service in Latin America in 2014.

Although still a relatively new phenomenon, online remittances are posing a significant threat to traditional players. By 2011, Western Union’s fees had dropped by over 50% since 2001 and margins fell below 1% in 2013. Faced with a fierce price war, MTO no longer counts on fees as a principal source of profit. Now, income comes from managing its foreign exchange spread. With more competition, cost pressure will increase and retail MTOs will migrate an increasing number of customers to the digital channel as they shrink their agent network. The 2015 acquisition of Xoom by PayPal indicates big payment companies’ interest in this growing business and the opportunity to capitalize on the trend toward digitalization.

While cash holds its ground, remittances for services may be another disruptor

Yet this trend has limits. The big appeal of online money transfer is convenience. As remitters inch up into the middle class, gain access to technology and become more pressed for time, their preferences trend toward online channels. This may be especially true for remitters from South America who are overall better—educated and wealthier than Mexican and Central American migrants. However, this ascent into the middle class takes time—and during the process migrants tend to become settled, have children, lose ties with their homelands and eventually cease to be remittance customers. New migrants who take

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Remittances to Latin America and the Caribbean, 2015, USD bn

Source: International Development Bank
their place are poor, often undocumented and have the same barriers to online remittances as the generation of migrants before them. Remittances as a product necessarily targets low-income demographics with low technological literacy: cash-in therefore remains a mainstay of the industry.

An additional draw toward the online space, however, is remittances as a service, in which remitters directly pay for the cell phone top-ups and utility bills of their relatives abroad. This segment is rapidly trending toward online and—more significantly—mobile, which now accounts for 60% of all online cross-border mobile top-ups to Latin America. Xoom, using technology furnished by white label provider TransferTo, enables mobile top-ups in 15 Latin American markets. Some users prefer this option since the funds go directly to pay for services chosen by the remitter, guaranteeing that the funds go to good use. Bill payments save friends and families in Latin America lengthy trips to the bank to pay for utilities—a serious time constraint for people living in rural areas or underserved urban neighborhoods. Growing at an estimated 10% annually, airtime remittances capitalize on the major opportunity to capture small value transfers cost-effectively. Most such transfers are for values less than USD $20.

TransferTo estimates the airtime top-up market from the US to Latin America to be about USD $1.5 bn, a small share of all money transfers to the region. But operators believe airtime remittances effectively attract new customers to money sending services. By enabling secure, low-value transactions, remittances as a service help generate trust among new users who may eventually migrate to a money-sending platform. And these transactions have an ever-increasing online presence. To plan accordingly, traditional players must forge partnerships with local service providers, namely telcos and utility companies. The most forward-looking providers will look at cross-border e-commerce and delivery services—buying goods from abroad and having them shipped directly to the recipients’ door. Progress in this realm will be slow, as recipients still prefer cash, but more diverse options become available, a trend toward digital will continue to consolidate.
 grace borrowers have long struggled to obtain credit. Mexico's credit market is strikingly small: $37 billion compared to the US's $225 billion. Mexico's per capita mortgage is $376, whereas the US's is $8,314. The story is the same for personal loans: Mexico's per capita non-revolving personal loan is $193, whereas the US's is $1,922.

The restrictions on mortgages and loans are more striking. As of December 2015, Mexico's total mortgage portfolio totaled $37 billion. To put this in context, in Q2 2015 alone, banks in the US issued USD $225 billion in new mortgages, dwarfing Mexico's entire portfolio. Per capita, Mexico's mortgage market comes out to just USD $376 per person; in the US, this number is USD $8,314. The story is the same for personal loans: the per capita non-revolving personal loan in Mexico is a total USD $193. In the US, it is USD $1,922. In addition to being scarce, capital in Mexico is also exponentially more expensive than in the US; credit card APRs commonly reach well above 50%. Interest rates on personal loans are usually upwards of 40%.

Mexico's small lending market is surprising, considering the country's sizable middle class, which is, in theory, creditworthy. According to Credit Suisse's 2015 Global Wealth Report, Mexico's middle class is the largest in Latin America, consisting of 13 million adults. Yet Mexico's population is 40% smaller than Brazil's, which has 11 million middle-class citizens. The 15 million pawn transactions taking place each year in Mexico highlight the mass market's need for cash.

Payday loans in Mexico did see a surge in 2015 of 18%, given a more formalized labor force, but only at the expense of the credit card market, which shrank by three million cards since 2014. Overall, banks remain hesitant to issue personal loans, restricting lending to the wealthy. The reasons are multifold: Underbanked customers are expensive to serve, are too risky and often do not have the required documentation to even apply for a loan. According to Luis Creel of Coheten, an online payday lender: "This is a highly underserved market—commercial banks are making no moves to extend their lending to a larger population." As a result, a slew of innovative players are entering the market to capitalize on this latent demand.

**Chapter 7: Online lending is shaking up Mexico's credit market**

**Online lending is shaking up Mexico’s credit market**

While still a tiny market, alternative lenders point to an emerging trend

Both consumers and businesses across Latin America have poor access to credit as a result of overly conservative banks, underdeveloped credit bureaus and high levels of informality. In Mexico, there are 33 million credit cards distributed among 18% of the adult population, roughly 16 million people. This is less than half of Mexico's total banked population: In other words, being banked does not equate to being financed.

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**Comparing access to credit in Mexico and the US**

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<th>Mexico</th>
<th>US</th>
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<tr>
<td>Credit card penetration, adult population</td>
<td>18%</td>
<td>71%</td>
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<td>Mortgage portfolio, per capita (USD)</td>
<td>$376</td>
<td>$8,314</td>
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<tr>
<td>Personal loan portfolio* (USD)</td>
<td>$193</td>
<td>$1,922</td>
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Sources: Comisión Nacional Bancaria y de Valores, World Bank, Federal Reserve, CID Gallup
*Non-revolving personal loans, excluding mortgages and auto loans

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**Alternative lending making a debut**

One example is Kubo Financiero. Founded in 2012, Kubo is a P2P lending platform akin to San Francisco's Lending Club. It serves simultaneously as a marketplace for Mexican investors and a source of financing for consumers. Using Kubo's platform, Mexicans with extra cash browse approved loans online and choose which to fund for a better-than-average return of 14%. Loans, called ‘projects,’ are filtered
into several categories including Small Business, Debt Consolidation, Home Improvement, Education, Health, Automotive, and Vacation, and investors select those that have the right balance of security and payoff. Not surprisingly, 75% of loans funded fall into the Small Business category, as investors are keen to reward enterprising borrowers, who tend to be safer bets.

Kubo’s business model depends on attracting investors and convincing them that the reward is worth the risk. Surprisingly, 35% of Kubo’s investors are millennials between the ages of 18 and 32. These budding investors make average deposits of USD $1,600 and are the company’s fastest-growing customer segment. Another 40% are Generation X-ers ranging from 32 to 55 years old, investing an average of USD $6,000. Kubo is capitalizing on an underserved market in Mexico’s investment space: the young, affluent, and tech-savvy who have faith in startups. So far, investors seem to be content with the Kubo experience—in 2015, 98% of Kubo investors reinvested their earnings, and 50% added additional funds after the first six months.

On the borrower side, most customers are semi-formal or informal business owners in need of working capital to expand their enterprises. This is where Kubo fulfills an unmet demand. These applicants would normally turn to pawnshops, microfinance institutions or loan sharks for cash flow. Additionally, Kubo’s model allows borrowers to apply for a loan conveniently on their own time. About 70% of Kubo’s loan applications are submitted online (as opposed to in—person with Kubo sales people) and 60% of transactions occur outside of normal banking hours.

The question: Is online lending by non-banks too much transactions occur outside of normal banking hours. Not surprisingly, 75% of loans funded fall into the Small Business category, as investors are keen to reward enterprising borrowers, who tend to be safer bets.

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The question: Is online lending by non-banks too much of a niche market to bring to scale? Kubo’s portfolio to date is tiny—USD $2.7 million in outstanding loans—and the total market for non-bank online lending is probably not more than USD $20 million, less than 1% of the total personal loan market. Growth is encouraging—in 2015, Kubo quadrupled its numbers in both number of loans issued and total portfolio—but whether this growth is sustainable is unknown. Kubo’s CEO Vicente Fenoll described the challenge ahead: “So far, we have been very successful with the early adopters. Our challenge now is to figure out how to bring Kubo to the mass market.”

Trend toward digitization

Lending of all types in Mexico is trending heavily toward the online channel. Technology companies use big data and complex algorithms to assess credit worthiness, enabling them to serve customers rejected by banks. Cohete provides 1,500 online loans monthly. Customers apply, and if approved, funds are deposited directly into their bank accounts. Kueski promises payment of 30-day micro loans (around USD $200) in under two hours. Prendanet is perhaps Latin America’s first online pawnshop. Mimoni and Yotepresto are still other online lenders competing in the space.

While these emergent lenders are still tiny, some traditional lenders are starting to feel the heat. In response to the appearance of alternative lenders in Mexico, BBVA Bancomer began issuing loans online in 2015. Using internal data, it pre-approves customers for personal loans and invites them to apply online, with no need to step foot in a branch. This strategy has seen spectacular results. Today, 30% of the bank’s personal loan portfolio is issued online, a startling jump from 2% at this time last year. Two-thirds of BBVA Bancomer’s loans sold online are short-term payday loans, in direct competition with the types of loans provided by Kubo, Cohete and others. According to Hugo Nájera, head of business development at BBVA Bancomer, the bank developed this strategy to mitigate the threat of these emerging players: “With the appearance of online marketplaces for lending in Mexico, we realized we needed to become more flexible and agile in order to compete. The world is changing. We have to interface with our clients digitally.”

So far, BBVA Bancomer is the leading commercial bank in this space. If others follow, it could mean trouble for lending tech companies. With access to millions of customers—and their data—banks have a direct channel into a much larger client base than Kubo, which has to scavenge to generate business. Nájera states that BBVA Bancomer has not eased its lending requirements—it has simply made it more convenient for eligible customers to take out a loan. Thus, commercial bank lending remains restricted to the affluent and alternative players have the chance to target a lower-income demographic. And commercial banks may actually help alternative lenders by promoting online loan applications to a wider market. Whoever comes out on top, consumer lending is trending sharply toward the online channel and growing in volume we as a result.
As the Latin American credit card market matures, banks are hustling to come up with better value propositions

Consumer credit cards have been wildly successful in Latin America, with the issuing of them growing 20%+ per annum for the past ten years. As avid consumers, Latin Americans delight in the credit afforded them through cards—credit that in large part has financed the region’s access to technology, international travel and luxury goods. Growth has been mostly organic and margins have been fat, making life easy for issuers. And although card issuing is restricted to the top 20% or so of consumers, banks have successfully pushed multiple cards into Latin American wallets, supported by retailer- and airline-backed loyalty programs.

Issuers are now facing an uphill battle, however. With slowed GDP growth, currency devaluation, high debt levels and a saturated market, the number of new credit cards has decelerated from upwards of 20% prior 2013 to <10% in 2015 across the region.

Card issuing in decline

In Mexico, the card market actually experienced negative growth in 2015, contracting by three million cards. BBVA, Mexico’s largest issuer, saw its card portfolio shrink by 11%²⁰ in 2015, while Banamex, the second-largest issuer, saw a drop of 9%²⁰. A 2014 tax reform that established better sales tax enforcement and introduced steps to verify that expenditures are congruent with income may have inadvertently caused a cannibalization of card payments by cash. Steeped in a culture of informality, many Mexicans are keen to avoid paying taxes—and cards create unwanted transparency.

Loan default rates in banks are on the wane thanks to an improved labor market and higher levels of labor formalization (4% growth since 2014²¹). Many banks now offer alternative financing options—particularly in the form of payday loans, which grew by a whopping 18% in 2015. Payday loans often carry lower interest rates and fees than cards do and are more suitable for the acquisition of durables, such as a refrigerator or television²². They are also less risky, because banks can recuperate funds directly from their borrowers’ paychecks. At the same time, there has been a surge in lending from non-traditional financial institutions that is putting added pressure on banks to find new ways to open up consumer lending.

A decrease in cards and an uptick in other sources of financing indicate two trends. First, for many Mexicans, a credit card’s appeal lies primarily in the access it gives them to credit—not in its convenience as a payment method. Second, current rewards programs are not sufficient to inspire loyalty among some cardholders. Issuers have lacked creativity in card incentive programs, relying on tired come-ons such as airline miles and travel insurance. These incentives are wholly uninteresting to newly middle-class families whose priorities lie in upgrading household durables, for instance.

Especially among elite cardholders, standard travel benefits are no longer cutting it. Competing for preferred cardholders requires better rewards, such as those offered by the Santander Aeroméxico Visa card launched in 2016. The card offers seriously exclusive benefits, including upgrades to first class tickets and private airport transportation. But issuers of these cards must battle for contracts with airlines and other co-branders. Santander won the 10-year co-branding contract with Aeroméxico in 2015 after the airline ended its longstanding relationship with Banamex. It’s expensive to migrate an entire card portfolio from one issuer to another, so Santander presumably

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<th>Credit cards in circulation (mn)</th>
<th>Carded population (mn)</th>
<th>Average cards per person</th>
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<tbody>
<tr>
<td>Brazil</td>
<td>162</td>
<td>50</td>
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<tr>
<td>Mexico</td>
<td>33</td>
<td>16</td>
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<tr>
<td>Colombia</td>
<td>14</td>
<td>4</td>
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Source: World Bank, ABECs, CNBV, Superintendencia Financiera de Colombia, AMI analysis

²⁰ PaymentMedia. 2015. “Disminuye en 3 millones el número de tarjetas bancarias en México”
accepted significantly lower margins to cut the deal. As cardholders demand more specialized benefits, issuers must sweeten the pot—and consequently cut margins—to win and maintain co-brander loyalty.

**Colombian banks diversify credit card offering**

In Colombia, credit card growth slowed in 2015 from 13%-12%\(^23\). In response, issuers have adopted a diversification mindset, providing niche products beyond their affluent customer base. Issuers launched nine new products in 2015, appealing to millennials and middle-class families among other demographics. Alliances with co-branders have been essential for this strategy and these are proving to be more creative than in other LatAm markets: For example, 2015 partnership launches include one with Linio, a large e-commerce marketplace, and one with the National Colombian soccer team. 2016 has seen scant personal card launches.

**Technology will drive credit card loyalty in Brazil**

Inflation and increasing default rates saw the average annual interest rate on cards in Brazil soar to 431% in December 2015, the highest in 20 years\(^24\). In part, rates have skyrocketed to help pay for Brazil’s famous parcelados—the hugely popular no-interest payment plans offered in conjunction with banks and merchants. In May 2015, 72% of the outstanding balance on Brazilian credit cards represented purchases made under a parcelado plan—and parcelado plans as a whole grew by 8% in 2015. By contrast, Brazil’s interest-bearing card portfolio has been in decline since 2008\(^8\).

It’s especially notable, though, that despite a recession, climbing interest rates and a severely devalued currency, credit card spend grew by 8% in Brazil last year when measured in Reais. (It contracted a staggering 24% when measured in dollars\(^9\)). Brazil in 2016 is experiencing its third year of economic crisis and the IMF expects the country’s economy to shrink by 1%. So even though credit card growth is still positive, it is likely to slow as consumer debt levels become unsustainable and inflation and unemployment increase. In this environment, Brazilians will use their cards less for high-ticket luxury goods and more for everyday purchases. Because expanded card issuing is unlikely in the current economy, banks are betting on technology to enlist consumer loyalty.

New and wide-ranging technological developments are having a rapid impact. In the past six months alone, Banco de Brasil has introduced a contactless payments app for its Ourocard, while a new MasterCard mobile app enables customers to use loyalty points for purchases at any merchant. As well, Visa launched its digital wallet, Visa Checkout, on FutebolCard, a popular e-ticketing platform. And according to market rumors, MasterCard and Apple will bring ApplePay to Brazil in 2016. For their part, Caixa Econômia and Bradesco will help launch Samsung Pay this year. The hope is that by engaging Brazilian consumers through technology, banks and payment companies can inspire Brazilians to use their cards for everyday purchases and not abandon them for cash.

**Cards have entered a phase of tough competition and lower revenue**

Latin America’s personal credit card market has reached maturity at an unfortunate period—an economic downturn. When times get tough, credit cards often meet their fate with a pair of scissors. Banks across the region must now act strategically to 1) form deliberate partnerships with co-branders; 2) deliver innovative and relevant rewards programs; and 3) employ technology. Revenue will not flow as easily as it has in recent years and banks may need to explore other products to drive growth, such as small business and corporate cards. One thing is certain: the halcyon days of sizeable revenue from credit cards are coming to an end. Issuer creativity and innovation will define the winners going forward.
## 2015 Colombian credit card launches

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<tr>
<th>Issuer</th>
<th>Network</th>
<th>Product</th>
<th>Target customer</th>
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<tr>
<td><strong>Premium/elite cards</strong></td>
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<tr>
<td>Citi</td>
<td>Visa</td>
<td>Premium/elite cards</td>
<td>Corporations with high T&amp;E spend</td>
<td>• Access to Visa Luxury Hotel Collection and Priority Pass</td>
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<td></td>
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<td>• Worldwide personal assistant service</td>
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<td>Bancolombia</td>
<td>Visa</td>
<td>Affluent</td>
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<td>• 10,000 bonus miles</td>
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<td>• 2 miles earned per dollar spent</td>
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<td>• Visa Luxury Hotel Collection and Priority Pass</td>
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<td><strong>Millennials</strong></td>
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<td>Banco AV Villas</td>
<td>MasterCard</td>
<td>Tarjeta “Talisman”</td>
<td>Millennials, Virgin Mobile customers</td>
<td>• Discounts and discounted interest rates for Virgin Mobile purchases</td>
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<td>Banco Colpatria</td>
<td>Visa</td>
<td>Frequent patrons of Linio, large eCommerce marketplace, i.e. middle class, e-commerce savvy</td>
<td>• 20% permanent discount on Linio.com</td>
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<td>• Purchase insurance</td>
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<td>Bancolombia</td>
<td>Visa</td>
<td>Mass market, young men</td>
<td></td>
<td>• Discounts on soccer-related apparel, accessories, tickets, etc.</td>
</tr>
<tr>
<td><strong>Middle class/families</strong></td>
<td></td>
<td></td>
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<tr>
<td>Banco AV Villas</td>
<td>MasterCard</td>
<td>Fondo de Empleados de Bimbo “FeBimbo”</td>
<td>Bimbo employees</td>
<td>• Preferential interest rates exclusive for Bimbo employees</td>
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</tr>
<tr>
<td>Tuya</td>
<td>MasterCard</td>
<td>Frequent patrons of Éxito and Carulla big box retailers, i.e. women, middle class families</td>
<td>• Triple points for every USD $100 spent at Éxito and Carulla</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>• 25% discount on select days</td>
</tr>
<tr>
<td>Tuya</td>
<td>MasterCard</td>
<td>Frequent patrons of Éxito and Carulla big box retailers, i.e. women, middle class families</td>
<td>• Triple points for every USD $100 spent at Éxito and Carulla</td>
<td>5% additional discount on groceries</td>
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<tr>
<td>Banco Colpatria</td>
<td>Visa</td>
<td>Frequent patrons of PriceSmart, membership-based discount big box store, i.e. middle class families</td>
<td>• 4% cash back on PriceSmart purchases; 1% cash back on all other purchases</td>
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Conclusion: What is to come in 2017?

The age of digital payments in Latin America has arrived. With a large unbanked population and much of the economy still operating informally, the trends outlined in this paper will continue to develop over the next several years. Competitors will scramble to gain their footing and find solutions that stick. Banks will fight to stay relevant in a rapidly decentralizing payments environment. And players of all persuasions will experiment with services to bring the underbanked into the digital age.

While all the trends outlined in this paper will continue to consolidate in 2017, one in particular will come to the forefront: the prominence of mobile commerce. Just as many consumers are accessing the Internet for the first time via a mobile device, the same can be said for merchants. Small merchants in Latin America see the power of e-commerce to boost sales, but too many do not have the resources or know-how to develop a full-blown mobile website or app. Thus emerges an opportunity to target merchants wishing to collect payment via email or messaging services, like Whatsapp. Whatsapp is increasingly becoming a tool for small businesses to communicate with their customers. Enabling payments and direct sales through the app and others like it represents an enormous opportunity and inevitable development.

The app economy is not showing any signs of slowing in Latin America and will continue to outpace e-commerce in the medium term. Technology companies Netflix, Spotify, Uber, Facebook, Airbnb, OpenTable, and Coursera are well entrenched among Latin America’s upper-middle class and are inspiring a host of local apps. As the sharing and on-demand economies advance in the region, payment mechanisms for the mobile channel will become increasingly essential to merchant success.

Yet as things stand, m-commerce is only available to Latin America’s credit-card holding upper-middle class. There is still a key underserved demographic: underbanked (and uncarded) smartphone holders. This group represents a huge opportunity. They are urban, tech-savvy, connected on social media, newly middle-class, and most importantly, aspirational, meaning they want copy consumption patterns of the affluent. They are eager to use Uber, stream online content and order food for delivery on their phones, but cannot for lack of a payment method. This will begin to change as banks enable more debit cards for e-commerce, but without a cash or prepaid option, most of these potential customers remained unserved. Ambitious merchants, like Uber, who recently enabled cash payments in Mexico, are likely to pave the way on this front, but they need local payment partners truly win.

Finally, in the medium term, Latin America will experience a trend toward consolidation in the payments industry. Currently, experimentation in digital payments is ubiquitous, but this will wane as leaders emerge. This is already occurring: banks are investing in fintech startups, Visa and MasterCard are expanding their service offering into other payment verticals including e-commerce and remittances, and PayPal’s stated ambition is to become a complete financial service provider. Facebook, owner of both Whatsapp and Instagram, has just launched a P2P payment service in the US, and with Brazil its number three market in the world and dozens of payment companies vying for partnership, bringing a payment facility to Latin American is not likely far off. Competing with these giants will be difficult; the ability to partner with them instead will spell success or failure for emerging payment players in the region.
About AMI

AMI is the leading independent Market Intelligence provider in Latin America

AMI is Latin America's leading Market Intelligence and Advisory group.

AMI has experience in every market in Latin America and the Caribbean.

AMI is a member of SCIP – Strategic and Competitive Intelligence Professionals.

AMI’s founding partners are pioneers in the field of Market Intelligence in Latin America, with over 20 of years experience in the region.

Experts in the Latin American payments industry

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About the Author

Lindsay Lehr  Senior Director, AMI payments practice co-leader

- Leadership of 70+ consulting engagements, 30 in financial services
- 10+ years experience working in Latin America
- Co-author of AMI payments whitepaper
- Frequent public speaker and thought leader in mobile money, mobile payments, e-commerce and m-commerce and financial inclusion in Latin America
- Fluent in English, Spanish and Portuguese