Think there’s no more room for innovation in online payments? Think again. Why 2021 will see advancements like never before

On the face of it, online payments appear to be a pretty well-solved problem. Payment pioneers such as Paypal, Adyen & Stripe have come to prominence over the past 15 years, and are so ubiquitous that they now have a combined market cap of $440B.

Temps de lecture : minute

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Yet scratch the surface and you’ll discover a somewhat different picture.

Legacy card networks have remained remarkably fragmented across different geographies. The biggest regulatory shift for a generation – Open Banking – is coming to fruition, allowing a radical rethinking of how financial data is used and online payments are made. And as consumers in emerging markets come online, they’re bypassing card payments altogether for e-wallets. Each requires new infrastructure and approaches. That’s before we even touch on the acceleration of e-commerce adoption caused by COVID-19 or the huge opportunities on the B2B side.

At the same time, we’re reaching a level of maturation among e-commerce businesses, where they’re starting to outgrow their initial payment providers. They need to evolve their payment strategies in order to improve conversion rates (particularly as they expand internationally) while trying to reduce fees.

We’ve been investing into payments businesses as a team for the past decade, partnering with companies like Transferwise, Riskified, Melio, Rayd, Yapily, Libeo, Payaut & Compa. We see exciting opportunities to take the advances made by the early pioneers into 2021 and beyond. Here are the opportunities we believe will be big this year.

A payments tipping point

When we talk about maturing businesses needing to optimise conversion rates, we're referring to two types – customer conversions (i.e conversion on-site), and acceptance rate on the back-end by their payment partners, known as their "auth" rate.

The key to improving customer conversions is to reduce checkout friction. A recent study found that seven out of 10 customers abandon their online checkout because of complicated login processes, or inadequate payment options. This is even higher on mobile. In addition there are various mandated or voluntary fraud checks that can add considerable friction and drop off through checkout.

When businesses expand internationally, these issues are often accentuated. Across Europe, card schemes and payment preferences are fragmented and auth rates vary considerably depending on the businesses payment service provider (PSP). Being based in the UK or US, you'd be forgiven for assuming Visa, Mastercard and Amex account for the vast majority of online payments, but this isn't the case. 60% of online payments in the Netherlands, for example, were done via local bank-to-bank payment provider iDEAL in 2019. Merchants end up having to work with a range of PSPs in a bid to optimise for the best fees, market coverage, and auth rates.

So what are the opportunities?

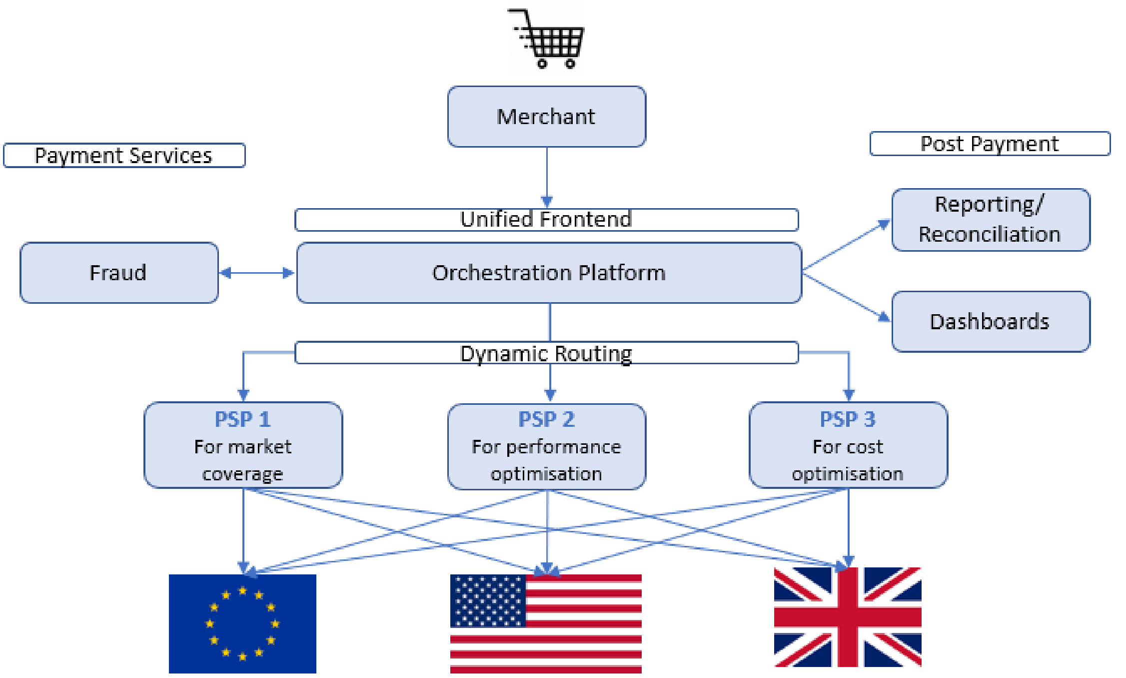
1- The emergence of payments orchestration platforms

This move away from single PSP setups towards a more fragmented payment stack can prove difficult to manage. A challenge that can be managed via payments orchestration platforms.

Although their approaches vary, most startups in this space (Primer, PayDock, Apexx, Gr4vy) use technology to consolidate various payment methods into a single API. They can then dynamically route each payment to the most effective provider (optimising for auth rates and fees); very easily add new payment providers or services (e.g the latest Buy Now Pay Later solution, or alternative payment method); and massively simplify the backend reporting and reconciliation that comes with using multiple providers.

Although the early players (like Zooz and Optile who have both been acquired, and Spreedly) have been around for a decade, it’s a market that’s now becoming mainstream. Largely driven by the number of maturing retailers now selling cross border, and the growing level of sophistication amongst ecommerce merchants.

Payments orchestration layers consolidate the complex payments stack



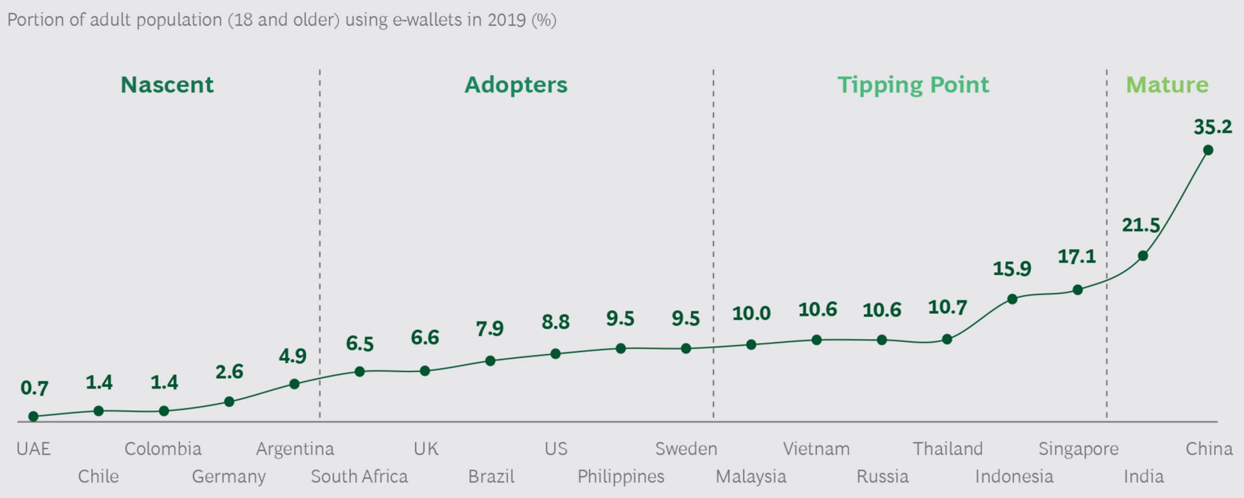
2- The rise of alternative payments

Western e-commerce is built upon card-based infrastructure, but commerce in the rest of the world functions differently.

The growth in e-wallet usage, particularly in China, India and Southeast Asia has been remarkable in recent years. Without much legacy card infrastructure or consumer bank account penetration, they’ve effectively skipped card payments altogether and moved straight to using mobile payments/e-wallets online.

Covid is simultaneously acting as a big accelerant away from cash, and towards e-wallet adoption. Some 17% of e-commerce transactions outside the US are now made via e-wallet.

EXHIBIT 1 | China and India Lead in E-Wallet Penetration, but Southeast Asia Is at a Tipping Point



Sources: Statista; World Bank; BCG analysis.
Note: Nascent = penetration less than 5%; Adopters = penetration between 5% and 10%; Tipping point = penetration between 10% and 20%; Mature = penetration greater than 20%.

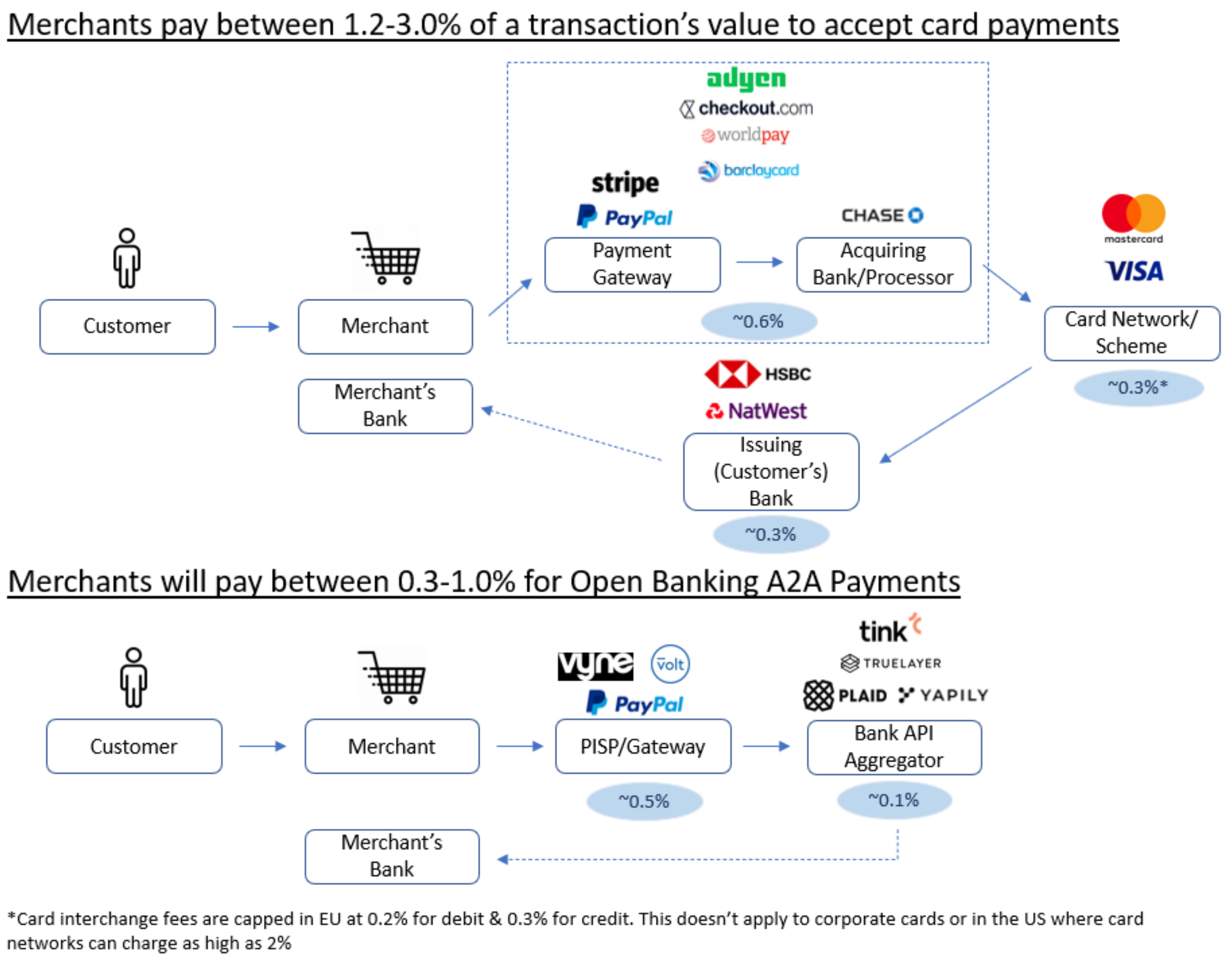
As Western merchants expand into these markets, allowing payments via the preferred local payment methods (often including cash) is crucial. Our portfolio company, Rapyd, is perfectly placed to serve these merchants - they've built a "network of networks" which gives access to over 1,000 different payment methods.

Elsewhere, services from Apple, Google, Samsung and Amazon, plus PayPal are making it easier for consumers to store payment information and reduce checkout friction. By 2023 e-wallets are expected to become the most popular online payment method in the UK, accounting for 33% of the market.

3 - Open banking payments gains adoption

We have no doubt that Open Banking is a once in a generation regulatory shift, creating a wealth of opportunities for disruptors. Initial use cases have centred around "reading" consumers transaction data, such as Cleo in our portfolio.

We’re now on the cusp of open banking becoming technically viable for B2C payments as well. There are still obstacles to overcome, such as reducing chargeback fraud and removing friction from the convoluted checkout flow (especially on desktop), but the potential cost saving vs card payments could make it a powerful way for merchants to reduce their fees and improve cashflows.



At the infrastructure level, the bar for facilitating payments vs just reading financial data is much higher. Plaid could happily enough have a 5% failure rate when reading data, but this kind of failure rate for payments would be unacceptable. Bank coverage and acceptance rates will be key to winning the biggest and most valuable merchants as they look to embrace this new payment method. We think Yapily is very well placed in this crowded field.

4 - The consumerisation of B2B payments

Beyond the world of B2C, we've spent a lot of time in the B2B space. To give a sense of how full of friction this space is, more than 50% of B2B payments in the US are still made by cheque.

This is, in part, because the payment methods and workflows are vastly different to B2C, and current solutions almost non-existent. The bulk of B2B payments are still made through manual invoices, emails and phone calls. Both Melio and Libeo in our portfolio have seen amazing traction over the past 18 months with a focus on solving this for SMBs.

We're also particularly excited about the opportunity at the B2B online checkout. There were huge tailwinds, even before Covid, of B2B sales moving online. 2019 saw a 18% YoY increase in ecommerce sales. Yet the infrastructure doesn't exist to facilitate payments in an automated and streamlined way at checkout.

These are some of the areas we're hoping to focus on this year, and with so much potential in the space, we're looking forward to finding the next Transferwise or Melio that will propel the payments world forward.

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