

Growth in pre-paid cards brings new opportunities

Written by an independent journalist on behalf of ACI Worldwide



The use of pre-paid cards is growing rapidly worldwide. Although pre-paid cards could be placed in the same category as debit or credit cards, they are more likely to be used to replace cash, cheques or vouchers, providing benefits such as convenience, cost effectiveness and security. The growing acceptance of pre-paid cards among governments, businesses and consumers presents an opportunity for banks, alongside the major card networks, to identify new segments of the market that can benefit from the pre-paid format.

It is difficult to generalise about pre-paid cards, because their potential uses are so varied. Different business drivers and uses are emerging in different parts of the world, but these can broadly be categorised as:

- **Consumer initiated** — Cards that people purchase for their own use or the use of others, including public transport, road tolls and parking, gift cards or youth spending cards. Pre-paid mobile accounts also fall into this category;
- **Business initiated** — Usually payroll cards that act as a replacement for cash and cheques, particularly for employees without bank accounts. Expense accounts, bonuses and corporate gifts can also work in a pre-paid card format;
- **Government initiated** — To reduce opportunities for fraud and to streamline the issuance of benefits, many governments are starting to issue pre-paid cards.

Pre-paid cards can be either for single use, as is often the case with gift cards, or re-loadable. A further distinction can be made between pre-paid cards that operate in a closed environment and those that are open. Closed environment cards are those such as gift, or stored value cards that can only be redeemed in a particular store, or transport cards that are used for a sole purpose. Those that operate in an open environment are linked into the major card networks and so can be used

for purchases or cash withdrawals at ATMs and points of sale. In this way, they operate as a kind of ‘bank account-lite’.

Business and government

Around the world there are many market-specific drivers for pre-paid adoption, but a few general trends that apply. In both developed and emerging markets, catering for the unbanked is a major problem. “For many banks, the challenge is to provide banking solutions for as much of the population as possible, while not making a loss,” says Mathew Fidler, head of debit product development for Central Europe, Middle East and Africa at Visa International. “Pre-paid cards enable banks to issue a safe and convenient payment tool to those for whom an account linked to an online-only debit card, such as Visa Electron, is not suitable.”

But the number of unbanked in a society isn’t just a matter of banks’ reluctance to take on low-income customers. Often, the consumers themselves make a deliberate choice to not have a bank account. Aaron McPherson, an analyst at Financial Insights, says that the 2001 Survey of Consumer Finances, published by the Federal Reserve, shed some light on the situation. “There are around four million benefits recipients in the US that have no bank account,” he says. “But a survey showed that only 14 percent of these felt they didn’t have enough money to warrant an account. Other reasons stated include high bank fees, or just not liking banks at all.”¹

For both governments and companies, paying people in cash can cause security problems and cash-handling costs can be high. Introducing pre-paid cards is a more efficient and secure means of issuing salaries or benefits. In some markets, it has been shown that people are generally accepting of this method of payment, but that it takes time for them to get out of the cash mentality. South Africa and Russia are good examples of places where this is happening.

¹ p. 10 of the January 2003 Federal Reserve Bulletin article, “Recent Changes in U.S. Family Finances: Evidence from the 1998 and 2001 Survey of Consumer Finances

Pre-paid cards

“We’re also starting to see interest from some governments in Africa for other uses of pre-paid,” says Fidler. “Countries with foreign exchange restrictions want to manage their currency flows. Traditionally outgoing foreign exchange may have been recorded in travel documentation, but the amounts are quite difficult to track. Pre-paid cards provide reconcilable audit trails and a means of taking money abroad, so that governments can have access to accurate and up-to-date information on currency flows.”

In Poland, Kredyt Bank has plans to issue 750,000 pre-paid MasterCard Electronic cards to replace paper-based vouchers issued by state-owned companies to employees as year-end bonuses. This is the first MasterCard Electronic card used for this purpose. Similarly, Polish companies who used to issue tax-deductible food vouchers to employees are moving the scheme to a bank-backed pre-paid card. Now, banks in France and Spain are looking to introduce similar schemes.

Consumer cards

In the consumer sector, MasterCard says its member banks in Europe and SAMEA are issuing between 500,000 and one million pre-paid cards a year. “These range from youth spending cards, which are popular in southern Europe, to cards that enable migrant workers to remit money back to their homeland,” says Gertjan van de Klashorst, Global Platform Development at MasterCard International.

“These cards are particularly popular in Saudi Arabia and Israel where workers send loaded pre-paid cards to their relatives back home as a cheaper means of repatriating funds than the traditional channels such as Western Union.” The MasterCard Pre-paid Platform is processing pre-paid transactions from all regions.

There are many possible applications for pre-paid cards, which will depend on social and cultural profiles and the level of financial and retail infrastructure in a particular country. Banks and the card networks are already playing a major role in certain areas within the pre-paid card industry, but particularly in the closed consumer card environment, transport bodies and retailers are the ones pushing the concept further.

Large retailers in parts of Europe, such as the UK and Italy, have led the introduction of single-use pre-paid gift cards to replace paper vouchers, greatly increasing customer convenience and reducing the

chance of fraud. A logical next move for retailers would be to tie these pre-paid cards to loyalty schemes, and perhaps enable some kind of top-up capability. Banks generally have no involvement with pre-paid retail cards at this stage of their development.

Likewise, banks have a limited involvement with the range of pre-paid transport cards that are starting to proliferate, particularly in Western Europe. Many toll road systems use pre-paid cards to ease the flow of traffic through busy toll gates, and London is following in the footsteps of some Asian cities by introducing pre-paid contactless smart cards for metropolitan public transport. Banks are involved only in a top-up capacity, with transport Web sites enabling travellers to make a debit or credit transfer onto their pre-paid cards.

But banks have become more closely involved with another form of pre-paid, the pay-as-you-go mobile account. And some banks are offering the ability for consumers to top-up their mobile accounts from ATMs. This points to an opportunity for banks to bring this trusted channel to partnerships with other pre-paid card or account issuers.

“With so many different uses for the pre-paid format emerging, on a case-by-case basis financial institutions might not easily identify opportunities that match their capabilities,” says Ed Kountz, senior analyst in the Emerging Technology Solutions practice at TowerGroup. “But, taken on aggregate, it becomes clear that banks need to monitor the situation closely to avoid missed opportunities.”

Infrastructure

“Issuing or supporting the issuance of pre-paid cards, for corporate or consumer use, has become an important consideration for banks, whether they look to introduce a new platform themselves or outsource it to a third party,” says Fidler.

In some countries, the card networks have already invested in a third-party card processing platform to support their member banks. But now that banks are increasingly interested in opportunities for pre-paid cards, they are looking to add pre-paid functionality to their platforms.

Pre-paid cards

Andy Brown, senior product manager, payment systems at ACI Worldwide, says that while some forms of pre-paid schemes, such as generalised electronic purse systems, have been around for quite a few years, the key difference now is that schemes are building on the existing infrastructure and card technology rather than demanding completely new systems.

“Banks that have a payments infrastructure that is flexible will be best placed to handle the addition of various types of pre-paid schemes,” says Brown. “They will be able to more easily manage and personalise the card accounts, and authenticate, route, switch and authorise each card transaction.”

The impact of EMV

Although there are many different uses for pre-paid cards, the widespread use of EMV chip cards will likely have an impact on the way many of them operate. For any multi-application chip card, whether debit or credit, there is also an opportunity to include a pre-paid function — for use in an open or closed environment. But with some organisations reluctant to go down the multi-application route at the moment, the most imminent impact of chip cards on the pre-paid market will be on the choice it gives card issuers for online and offline authorisation. This could take the form of a hybrid pre-paid/debit card known as a pre-authorised debit card.

Pre-authorised offline debit operates through a shadow or memorandum account. An amount is reserved on the bank account for offline spending and is recorded on this shadow account. This could be the full deposit value or some agreed amount up to the full deposit value. Through the EMV scripting function, the reserved amount is mirrored on the card associated with the account.

This type of model is particularly useful for countries without extensive telecoms infrastructure to support lots of ATMs and terminals with connections back to a host system. A good example is in the Republic of Rwanda, where ACI Worldwide is currently working to build a national inter-bank card payments network, including a pre-authorised debit card programme.

An eye on the future

As the pre-paid card concept matures, and becomes just as entrenched as debit and credit accounts have in many countries, there will no doubt be new opportunities for banks. By monitoring what is happening with pre-paid in other parts of the world, and working closely with the card networks, there is a chance to extend their traditional range of financial services to governments, the corporate sector and consumers. And by keeping a close eye on pre-paid developments in other industries, there may be opportunities to use the bank’s channels, card issuance and management expertise to form new partnerships and branding opportunities.