Faster payments' public option will harm competition

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In August the Fed announced it intends to launch a real-time interbank payments service called FedNow. The central bank wants to do good. That's neither sufficient nor its call.

Rep. Denver Riggleman, R-Va., cautioned the Fed against spending hundreds of millions of dollars to enter the real-time payments market. It'll cost considerably more.

As an individual representative perhaps his tenor is appropriate, but for Congress it's unduly deferential. While Congress has too often abdicated its constitutional prerogative to make law, set policy for and instruct the "independent" and executive agencies, Congress is supposed to be master and the Fed its servant.

At the Senate Banking Committee's Sept. 25 pro forma hearing on "Facilitating Faster Payments in the U.S." senators, for the most part, were even more deferential than Riggleman.

President of the Kansas City Fed Esther George testified other providers alone couldn't be expected to provide the service "with reasonable effectiveness, scope and equity," there was "a clear public benefit," and the Fed would fully recover its cost "over the long run." When gently pressed on the need for FedNow she insisted rural and community banks could only be well served by the Fed. Hiding behind the skirts of politically sympathetic community banks is a time-honored practice in Washington.

Senators and witnesses extolled competition, and, with big banks' cooperative processor The Clearing House in mind, worried about centralization and concentration of power. Ranking member Senator Sherrod Brown, D-Ohio, vilified big banks. The ultimate concentration of power in the financial system, however, isn't TCH or dastardly large banks. It's the Fed.

In contrast, Senator John Kennedy, R-La., asked why the Fed should spend taxpayer dollars to compete with the private sector and suggested FedNow advocates "just wanted to expand government."

Former FDIC Chair Sheila Bair contended the payments system is a "public utility" and was keen for the central bank to expand its role. But, where practicable, America has long preferred robust private-sector competition over public utilities exempt from antitrust law. In retail electronic payments, government has never played a significant role. Competing networks like Visa, Mastercard, American Express, PayPal, Discover, Star and NYCE deliver enormous value, relentless innovation and near-ubiquitous access. TCH has been an interbank processor since 1853.

The Fed used its bully pulpit to socialize the value of faster interbank payments and encourage the private sector to enter the market. TCH took the challenge and spent $1 billion building a real-time-payments system, launched in 2017. A single provider, however, would be a bad outcome. The only thing worse would be no supplier. Indeed the most compelling rationale for the central bank entering the instant-interbank payments market would be to ensure there wasn't a monopoly. If you define a market narrowly enough you can always conjure a monopoly.

However, in addition to TCH, there are a handful of competing real-time interbank payment systems.

Leveraging their card-delivery systems, marquee networks Mastercard and Visa, and processing behemoths FIS and Fiserv, serve the market. Mastercard and Visa in particular could be more formidable faster-payments competitors. Directly or indirectly they reach virtually every DDA in America. Moreover, Mastercard owns the U.K.'s faster interbank payments system Vocalink and is selling the service worldwide. Bank cooperative Early Warning Systems' Zelle too provides instant interbank payments. All have ample technical prowess and existing networks. As competitors they would likely enhance their services, ensuring universal access and providing value continuously market to market.

A whiff of competition works wonders. Cryptocurrency phenom Ripple's nascent cross-border payments challenge forced Swift to up its game. Ripple could as well turn its sights to the U.S. market.

Riggleman rightly notes there's a patent conflict of interest in the Fed competing with entities it supervises and regulates. He fails to note that's been an issue for decades with the central bank's ACH and Fedwire operations competing with the private sector. The conflict suggests the paramount financial system regulator should divest them.

Even if the Fed weren't regulating private-sector real-time systems, it shouldn't compete with them.

The Fed's entry into the market will have a chilling effect on competition and innovation. Nobody will be keen to go toe-to-toe with the financial systems' paramount regulator and central bank with virtually unlimited resources. It will deter and suppress private-sector operators from investing more in real-time payments. That won't be good for banks, or businesses and consumers they serve.

The Fed like most agencies will take all the leash it's given. Congress should bring it to heel.

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