The Storm Before the Calm

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The pandemic is wreaking havoc on multiple fronts in the payments business. But if we let market forces work their usual magic, look for a recovery next year.

The Covid-19 pandemic is roiling the payments industry. State shutdowns have taken a whopping 29% of the U.S. economy offline. Moody's reports eight in 10 U.S. counties are locked down, and they represent 96% of national output.

"Dr. Doom" economist Nouriel Roubini predicts a deep depression. Former Fed Chair Janet Yellen warned unemployment rates "may go to Depression levels."

Payments volume and mix have been drastically altered.

Borders are closed. International air traffic has come to a grinding halt. Close to 100% of highly profitable card-present cross-border payments have evaporated. Domestic payments in many sectors have plummeted.

Hospitality has been particularly hard hit. Hospitality and restaurant transactions for merchant processor Shift 4 Payments for the seven days up to and including April 8, against the week of Feb. 2, took a nosedive.

Storied department stores such as Nordstrom's, Macy's, Kohl's, JCPenney, and Sears are closed. The novel coronavirus will cull the herd of struggling big retailers. Movie theatres may be toast.

However, e-commerce, with exceptions like gym subscriptions, is booming. Emarsys reported that, in the 14 days prior to April 4, retail e-commerce in the U.S and Canada was up 43% year over year.

E-commerce colossus Amazon is hiring 100,000 new workers. Walmart's grocery app has seen record downloads, surpassing Amazon's by 20%. Costco's March online sales were up 48% year-over-year.

Grocery is also booming. At the physical point of sale, Walmart, Costco, and many supermarkets have struggled to keep shelves fully stocked.

Contactless And Cash

Then there's contactless. For a quarter of a century, the U.S. payments industry has half-heartedly tried to spur contactless payments. In 1996, Mastercard in Manhattan and Visa at the Atlanta Olympics ran pilots. It wasn't compelling for either consumers or merchants. Swiping cards was habitual and nearly frictionless.

Google Wallet, Apple Pay, and Samsung Pay launched in 2011, 2014, and 2015, respectively. Mobile-wallet evangelists enthused they would usher in an era of contactless payments at NFC-enabled merchants. Cardholders and merchants didn't bite.

The coronavirus is more persuasive. Cardholders and merchants don't want to touch cards, terminals, or PIN pads. Issuers are rushing to put contactless cards in consumers' leather wallets.

Now there's pressure on cash. Roughly 15.1% and 24.6% of 2018 U.S. consumer-payment volume and transactions, respectively, were in cash, excluding mortgage payments. In most countries, cash is still the leading retail-payment system. But the coronavirus has made merchants and consumers leery of transacting in potentially contaminated cash, accelerating the worldwide secular migration to electronic payments.

The virus will boost interest in digital currencies. Ideally, digital cash will be issued by competing banks like banknotes of yore. Launched in 2018, Signature Bank's dollar-anchored digital currency, Signet, supports instant interbank payments. It's built on a private, permissioned form of Ethereum's blockchain.

Signature Bank isn't alone. In 2019, Chase launched the dollar-backed JPM Coin to enable efficient settlement of B2B transactions. Last year

Wells Fargo announced its plans to launch its own dollar-denominated digital cash in 2020.

None of these digital dollars targets retail use cases. But the coronavirus may spur these digital-currency pioneers to broaden their ambitions.

Payments Protectionism
Borders and control of goods and services critical to national welfare are at the fore. Simmering payments nationalism is going to come to a boil. The argument payment systems are critical national infrastructure resonates in a world with closed borders and scrambling for masks, ventilators, and pharmaceuticals.

China, India, Russia, Turkey, and Indonesia mandate in-country payment processing and have national payment-system champions. Payments protectionism will spread, like a virus.

The European Union already has an abiding hostility to Mastercard and Visa, as it does to Google, Microsoft, and Facebook. It pines for a supranational EU retail-payments system.

Will there now be pressure on interchange rates as a result of the pandemic? The National Restaurant Association has asked President Trump, House Speaker Nancy Pelosi, and Senate Majority Leader McConnell to reduce credit card interchange fees.

Restaurant lobbyists hoped to piggyback credit-card-interchange price caps on the Coronavirus Aid, Relief, and Economic Security Act. But restaurants are in dire straits because of being closed by government and fear of a virus, not interchange fees.

Adapt, Weather, Emerge
So, how does the payments industry come out of the malaise?

The Coronavirus Depression will be as deep at the Great Depression and what journalist James Grant called the Forgotten Depression of 1920-21. Whether it’s a sharp V-shaped recovery will depend on beating the virus and on government letting market forces do their magic as they did in 1920-21, but not in the Great Depression.

While I'm no fan of his central-planning mindset, my college classmate, oncologist Zeke Emanuel, is right in saying, "We will not be able to return to normalcy until we find a vaccine or effective medications." One hundred and twenty vaccines are in some stage of development. In the interim, we can take baby steps by loosening restrictions to forestall a prolonged depression.

Commerce at the physical point of sale will come back. Virtual bars, restaurants, and barbershops don't cut it. Nobel-prize winning economist Vernon Smith observes, "Once the pandemic passes and vaccines and treatments appear, people will be ready again to spend on services, travel, and hotels."

Despite the havoc of 2020, the payments industry will adapt to, weather, and emerge from the coronavirus storm, likely in 2021.

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