Insights to win in e-commerce in Latin America

A merchant-focused look
into e-commerce payment collection

By Americas Market Intelligence, March 2017

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- AMI is a member of sCIP—Strategic and Competitive Intelligence Professionals

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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 of 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

+1 (305) 873-4311
llehr@americasmi.com

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Introduction

In mid-2016, AMI put out a white paper entitled *Payments in Latin America: Under Digital Transformation*. Throughout 2016, we saw smartphone penetration reach nearly 50%, double-digit e-commerce growth reach a market size of nearly $59 billion and global digital giants prioritize Latin America as a market for growth. As the critical mass of smartphone holders and web-navigators consolidates, Latin America presents exciting growth opportunities for those looking to the world's emerging markets.

Yet despite the spread of globalization and significant advances in technological adoption, the region remains decidedly Latin American. This is neither a critique nor a compliment; it is simply a fact. While payments in Latin America are undergoing a digital transformation, the preferences, behaviors and motivators of Latin American consumers are fundamentally different than in the United States and Europe. This means that merchants desiring to increase their penetration among Latin American e-shoppers must adopt new tactics.

A key cause of differing consumer behavior in the region is the rigidity of banks and limited access to financial services. While banks throughout Latin America are dabbling in fintech and financial inclusion, efforts to expand access to banking—and access to the digital economy—have been underwhelming. Thus, credit card penetration still stands below 30% in most markets.

For many international merchants, this fact alone deters them from considering Latin America as a profitable place to do business. But by taking a closer look, global players will see that enterprising local merchants and payment processors have developed strategies to overcome these challenges and are reaping the benefit as a result.

The series of articles that follows touches on several ways in which the Latin American payment landscape is unique. The overall theme is that the bottom 75% of the pyramid is still underserved by financial institutions, making selling to these consumers a challenge. Here, the importance of local payment methods—domestic-only credit cards, debit cards and cash—cannot be overstated. Herein, merchants will learn about the peculiarities of the local market, pitfalls to avoid and insights needed to win. Easy and simple it is not. But for adaptable, forward-thinking e-merchants, Latin America offers a new frontier of opportunity.

1.

Merchants—Not Banks—Are Driving LatAm Payment Innovation

Merchants have more motivation and leverage than almost anyone else to change the payment landscape in the region.

Payment innovation in Latin America, or the lack thereof, has traditionally been driven by banks. Credit cards, achieving huge success in the region, became the principal electronic payment method with banks lazily offering other products, such as debit and prepaid cards. Flush with cash, facing little competition and enjoying a growing middle class, they have had little incentive to innovate. As such, banks have categorically failed at banking the middle and lower-middle classes or delivering creative ways to pay.

Around 2012, mobile operators in the region thought they might play a role in determining how people pay via mobile money platforms for the unbanked. Fast forward four years later, however, and mobile money penetration has reached only ~3% of the total population.

Similarly, the fintech revolution is expected to alter payments in Latin America. Online lending and branchless banking are areas in which fintech has thrived, forcing banks to think seriously about innovation. Banks, including Banco do Brasil, BBVA, Scotiabank, Bancolombia and others, have responded by creating their own startup accelerators.

Additionally, in 2015, banks across the region finally starting releasing their own iterations of payment technologies, including digital wallets for mobile payments, e-commerce wallets and payment wearables. In Mexico and Colombia, there are upwards of a dozen of such products, each fighting tooth and nail for market share. But volumes remain tiny: consumers are skeptical of digital payments for fear of theft of their personal information and none provide a better user experience than credit cards or cash.

Thus, since 2012, traditional payment methods have remained agonizingly sticky in Latin America and a huge chunk of the population still does not have any digital payment method. Some estimates say 90% of payments in Latin America are still made in cash. When will the digitization revolution in the region occur? And who will make it happen?

There is a major player in the payments ecosystem that has so far managed to fly under the radar. Latin American merchants are quietly moving the needle on financial inclusion and digital payments—and they seem to be doing so without anyone taking notice.

LATAM Airlines leverages cash

Merchants are achieving this by harnessing the power of cash. A prime example is LATAM airlines. In Peru, where banking penetration is only 30% and the culture of online payments is still underdeveloped, LATAM (then LAN) built its own cash-based payment system for its website at the complete exclusion of the national banks. Using LATAM's proprietary online platform, customers can purchase an airline ticket, print out a voucher and pay for it in cash at a large network of supermarkets. This approach has been so successful that LATAM is widely recognized by every player in the market as the leading e-commerce merchant nationwide. LATAM alone effectively captures 10%+ of Peru's total e-commerce market.

Netflix doubles its market with debit cards

In similar examples, merchants are changing the way people pay across Latin America. Take the example of Netflix in Mexico. Until only recently, banks refused to enable debit cards for use in e-commerce. Throughout Latin America, banks are acutely concerned about fraud on debit cards, because fraudulent transactions result in the theft of customers' actual funds. This is in contrast to credit card fraud, in which banks have the ability to deny chargebacks and liability falls to the merchant.

However, only 25% of Mexico's population has a credit card, meaning Netflix was not reaching its full audience, due to the simple fact that would-be customers did not have a way to pay. Netflix thus went knocking on the doors of Mexican banks to convince them to enable debit cards for payments to Netflix. This had two main results. The immediate impact was that Netflix's addressable market size nearly doubled. It also began a process of portraying debit cards as a safe and viable payment method for e-commerce, a trend that will continue to develop in the immediate future.

Uber, Linio and Facebook get creative with cash

In October 2016 the ride-sharing app launched a co-branded debit card in partnership with online-only bank Bankaool, precisely to cater to non-credit cardholders in Mexico. Uber also accepts cash in Mexico, Colombia, Brazil and Peru, as do Cabify and Easy Taxi. Facebook in Brazil altered its payments model for purchasing advertising credit by switching from a post-paid to pre-paid model to enable cash payments via *boleto bancario*, a popular cash-based payment method. Linio, a large regional marketplace, has been the pioneer of promoting cash-on-delivery for e-commerce across the region.

Driving the markets

In Latin America, merchants have a simple but strong motivation for innovation when it comes to payments: increasing sales. This basic fact is often overlooked by payments executives. The fact is, bank-driven payments innovation such as contactless wearables and NFC wallets is not what the market is asking for. Instead of pushing new-fangled (and unwanted) ways to pay into the market, a wiser approach may be to:

1) Identify who wants to buy what

2) Give them the mechanism to do it

Winning hearts, minds…and money

The influence of merchants on LatAm's payments and e-commerce industries will continue to grow. Besides winning the hearts of consumers, global merchants like Netflix have the leverage to influence banks. They amass huge groups of customers, many of whom are new to e-commerce and represent incremental income to banks. They also have the resources to tolerate a higher level of risk than small merchants and so are more willing to try new things. And they are not going anywhere: Uber has shown resilience in the face of a brutal regulatory crackdown in the region. Netflix is feverishly rolling out original and local content, including the first Argentinian series that premiered in late 2016.

Moreover, services like Netflix and Uber have become household must-haves and users are thus willing to adopt banking products to access them despite the deep-seated distaste that many Latin Americans have for banks in a region traumatized by financial crises. So as these new users become accustomed to e-commerce, they will use their digital payment methods on other websites and grow the pie overall. Thus, banks have a large incentive to work with popular digital merchants and indulge their desires.

Can merchants solve the mobile wallet mystery in LatAm?

One of the persistent challenges in Latin America is convincing the unbanked to keep funds stored in mobile wallets, as opposed to withdrawing it all in cash. Our prediction is that it will be merchants who solve this conundrum—not banks, telecommunications companies or fintech startups.

Increasingly, the bottom of the pyramid wants to consume digital goods and services—be it ringtones, taxi rides or online education. So if popular digital merchants—whose services cannot be purchased with cash—integrate with mobile wallets, this would provide a direct incentive to keep mobile money in digital form. Popular digital merchants have unprecedented reach and influence and therefore the ability to motivate those who are outside the banks' reach. Going forward, banks will lose control of payment methods and merchants' influence will grow. As such, banks in Latin America must embrace collaboration with merchants and welcome the newly banked into their community.

2.

Scaling E-Commerce Depends on the Uptake of Debit

The ability to accept debit cards will grant merchants access to millions of additional customers.

In Latin America, overall banked levels as reported by governments are reaching surprising levels. Colombia, considered one of the most cash-dependent economies in the region, claims that 76% of its citizens have a bank account. In Peru, the number is 66%.

These cheery numbers appear optimistic, but they do not tell the whole story. To calculate these figures, governments consider people ‘financially included’ if they have any type of formal financial product, regardless of type or usage.

For example, millions of Colombians have basic savings accounts and are thus considered ‘financially included,’ even if their accounts have zero balance and sit inactive for months or years. What’s more, a bank account is not tantamount to a payment card and having a payment card is not tantamount to using it. For example, around 500,000 Peruvians own a savings account where they receive government benefits and affiliated debit card. However, 95% of these funds are withdrawn in cash from a teller within 24 hours of them being deposited.

Certainly, the term ‘financial inclusion’ is misleading at best and deceitful at worst, considering the complex levels of access and barriers to banking that still exist in the region.

Growth of debit card penetration

While most often we conceive of financial inclusion in terms of access to payment methods, it is often a function of merchants’ ability to accept them. Nowhere is this more apparent than in e-commerce. Credit card penetration in the region is still low, since banks lack the tools to properly evaluate creditworthiness. Debit card penetration, however, has climbed at a decent pace in the past three to four years, in large part thanks to banks pushing out payroll cards.

LATAM PAYMENT CARD PENETRATION, 2017

Country	Credit	Debit
Brazil	30%	70%
Mexico	25%	37%
Colombia	26%	52%
Argentina	51%	69%
Chile	55%	71%
Peru	20%	32%

Source: World Bank Findex, AMI analysis.

This offers some interesting potential for e-commerce, except for enablement issues. Most debit cards in Latin America lack a CVV code and are thus not enabled for e-commerce purchases. Traditionally, banks have been concerned about fraud on debit cards, because fraudulent transactions result in the theft of customers' actual funds. This differs from credit card fraud, for which bank liability lies with the merchant and banks have almost absolute power in denying chargebacks. So while an estimated 230 million Latin Americans have debit cards, only the 113 million who also have credit cards can consistently make purchases online.

Changing over from cash

This is part of the reason why cash payment methods are so prevalent in e-commerce. Lacking an acceptable payment card to buy online, many Latin Americans use vouchers that must be printed and paid for in cash at affiliated agents—sometimes up to 72 hours after the order was placed. Once printed, only about 30% of all vouchers are actually paid for, creating uncertainty and inventory problems for merchants.

USE OF CASH PAYMENT IN LATIN AMERICAN E-COMMERCE, 2016

Country	% of Overall Spend
Brazil	25%
Mexico	22%
Colombia	34%
Argentina	40%
Peru	33%

Source: E-Bit, PayU, the Papers AMI PCI, AMI analysis.

Even though the risk of fraud is greater, online merchants across the board prefer payment cards for their convenience and efficiency and have been leading the charge to get banks to become less strict about debit—and banks are slowly coming around. In 2015, BCP, Peru's largest bank, began the slow process of migrating its seven million debit cards to e-commerce-ready. Banco de Bogotá in Colombia started this process only at the end of 2016.

Mexican banks have been particularly stern; in response, both payment processors and merchants have gone knocking on doors, convincing issuers to enable debit cards for their customers.

Brazil is the market where the most work needs to be done. While only 30% of Brazilians have a credit card, a whopping 70% have a debit card. Yet the use of debit in e-commerce is negligible, barely reaching 2%, as banks apply additional security measures that decimate conversion rates. This in part explains the success of the *boleto bancario*, Brazil's famed cash-payment voucher. However, an added cost to merchants for issuing *boletos* thanks to a regulatory change in 2016 means the availability of *boletos* as a payment method in e-commerce may decline this year. This will leave many Brazilians out of luck when it comes to buying online.

Driving debit

Some forward thinkers in Brazil see the missed opportunity in debit and are developing solutions. Payzen, a French payment gateway operating in Brazil, has developed a merchant plug-in for debit, which helps bypass bank authentication measures for selected cards and increase conversion. Payment processors, banks and merchants are likely to follow suit this year.

However, enabling debit for e-commerce is only the first step in achieving widespread usage. Once banks decide to enable debit, they must then educate consumers. This should be a collective effort between banks, card networks, processors and merchants. Certainly Visa and MasterCard stand to benefit from increased use of debit in e-commerce, but they have done little to advertise this capability to consumers. Co-branding debit cards with digital merchants, as Bankaool, MasterCard and Uber have done in Mexico, is a brilliant strategy to this end.

E-commerce in Latin America still has many years of robust growth ahead, thanks to the millions of Latin Americans who will come to the channel for the first time. Debit cards will be at the head of this growth trend, as credit card usage in the channel matures. Payment players waging a war on cash must first enable and then incentivize debit to lure the middle class away from their beloved *boletos* and Oxxo payments. Banks who do not get on board for fear of fraud risk missing the boat altogether.

3.

Cash Payments for E-Commerce: Growing, not Declining

An under-leveraged opportunity is materializing.

For years now, card networks, banks and governments have agreed on one thing: cash is the enemy. Governments want to shrink the informal economy to increase their tax base. Banks want to reduce the cost of handling massive cash volumes. Visa and MasterCard see cash as their most dangerous competitor. These parties have labored tirelessly to loosen the grip of cash on Latin American consumers.

In theory, e-commerce is an area in which credit cards have an obvious advantage; you can't feed cash into a computer and click 'Buy.' But in Latin America, only 27% of consumers have credit cards and an even smaller percentage is willing to put its credit card information online.
To accommodate non-credit card holders, local payment companies in Latin America have for years enabled cash as a payment method for online purchases, by which consumers print out a payment voucher and pay in cash at one of thousands of affiliated agents. Boleto bancario in Brazil, Oxxo in Mexico, Efecty in Colombia and PagoEfectivo in Peru are among the cash payment market leaders. Considering the low penetration of credit cards, cash has an astounding presence in e-commerce, reaching up to 40% of sales in some markets. On the next page, you'll see a table breaking down the major LatAm markets where cash is an important e-commerce payment method and the leading cash payment providers in each one.

To the chagrin of card networks and banks, cash payments for e-commerce in Latin America will grow in the short term, rather than decline. This is due to several key drivers:

1. E-commerce is growing faster among non-credit card holders than credit card holders

2. Cash payment providers are innovating to improve their service

3. International merchants are able to offer cash payment methods by integrating with local PSPs

#1 Faster e-commerce growth among non-credit card holders

Traditionally, Latin American e-shoppers represent the wealthiest segment—upper-middle class, professionals, early technology adopters. These folks have been happily buying online for the past 10+ years, catered to by banks and international merchants like Amazon and eBay.

Country		Cash payment penetration of all e-commerce sites	Cash payment providers
	Brazil	25%	safetypay, Boleto Bancário
	Mexico	30%	safetypay, OXXO, 7-Eleven
	Colombia	34%	safetypay, efecty, VIA, Baloto
	Peru	33%	safetypay, Pago Efectivo
	Argentina	40%	Pago Fácil, rapipago, Cobro Express

Sources: E-bit, PayU, AMIPCI, interviews done by Americas Market Intelligence

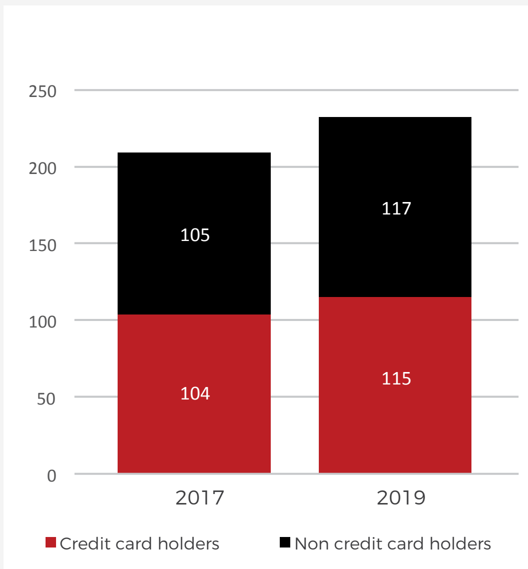
E-commerce has reached decent penetration among this population; they will continue to buy steadily online, but their numbers are not growing.

AMI commonly uses smartphone holders in Latin America as a loose proxy for Internet users; they are online, connected to social media and consume digital content. In 2017, 50% of smartphone holders have a credit card, but 50% of them do not, meaning they are online and want to consume but have limited payment options. The latter group is growing faster than the former, since there are far fewer barriers to smartphone adoption than there are to credit card adoption. These consumers use cash as their main payment method for e-commerce and as awareness spreads and smart merchants market toward them, they are driving cash payment growth. PSPs in Mexico report that cash payments grew between 40-50% in 2016, compared to approximately 30% for credit card payments.

#2 Cash payment providers are innovating to improve their service

Compared to a card payment, cash payments are inconvenient for consumers and merchants. Knowing this, cash payment providers are working to improve the customer experience.

# of smartphone holders in Latin America
In millions



In February 2017 Oxxo, Mexico's leading cash collector for e-commerce purchases, announced the launch of its product Oxxo Pay in collaboration with PSP Conekta. Oxxo Pay includes improvements to its cash payment service such as incorporating a reference number of a barcode (making it compatible with mobile), real-time reporting to merchants when a payment is made, customizable expiration dates and plans to soon launch recurring payments. With a network of 15,500 branches in Mexico, Oxxo is in a preferential position to harness the huge potential of cash payments within e-commerce. Today, Oxxo alone accounts for an estimated 20% of all e-commerce payments in the country.

Others also see the opportunity. PayPal in Brazil will purportedly enable *boleto bancario* as a payment method in 2017. This would be the company's first incursion into cash payments in the region and it isn't inconceivable that Mexico would be soon to follow. PagoEfectivo, Peru's premier cash payment option, reported growth of 60% in 2016 as it evangelizes its service to merchants and other PSPs. SafetyPay, another leading cash provider, is growing at close to 50% per year, outpacing overall e-commerce growth in the region.

#3 International merchants offer cash payment options via local PSPs

A third phenomenon driving cash payments in e-commerce is that of greater access by international merchants to local payment methods. Traditionally, global merchants who want to integrate with local payment providers must set up an entity in each country, a cost-prohibitive exercise for most. However, a growing group of payment service providers are offering global merchants a new model of payment collection, in which they can accept local payment methods without ever stepping foot in the local market.

This model began with Latin American startups AstroPay (now dLocal) and EBANX in 2009 and 2011, respectively, who have grown in the triple digits each year since. These companies process payments for merchants outside of Latin America and act as the local merchant of record, providing an ideal model for digital merchants who do not need a physical presence in Latin America to manage distribution. Following in their footsteps are other PSPs like PayU and allpago. All four of these companies have opened sales offices in San Francisco since 2015 in an effort to recruit the world's digital giants. On average, 30% of funds collected by these payment providers are in cash.

Merchants using this model today include tech giants Airbnb, Spotify, AliExpress, Uber, GoDaddy and Symantec; their ranks will increase as these pioneering PSPs march onward. At the end of 2016, dLocal announced its partnership with global payments company Digital River (DR), to enable local payments processing to DR's portfolio of global merchants. Merchants are becoming wise to the fact that enabling cash payments for e-commerce is a winning strategy and with the right payment partners, doing so is feasible and affordable. The dLocal-Digital River partnership is a strong indication that cash and other local payment methods will champion growth going forward.

This is not to say that credit card payments in e-commerce are declining. On the contrary, card payments represent the bulk of e-commerce transactions—around 70%—and merchants should take care to serve their credit card-holding customers, who are on average wealthier and spend more money than cash payment customers. However, what is certain is that the top of the Latin American pyramid has been well penetrated and there is a large, underserved population that represents incremental sales opportunities. Merchants who understand this and strategize accordingly will have a competitive advantage over rivals.

Opportunities for credit card companies

Credit card companies can also look at cash in e-commerce as an opportunity. Generally speaking, merchants prefer card payments because they are automatic, more efficient and offer co-branding opportunities. In the long term, Latin America will continue to digitize and electronic payment options will slowly cannibalize cash. Thus, card networks can strategize by partnering with merchants to offer incentives for card payments, profile and loyalize customers and offer prepaid cards specifically for e-commerce. This may take some patience, as cash is still king even in the digital world, but a long-term strategy should consider the cash users of today as card users of tomorrow.

4.

M-Commerce Growth Requires Understanding of Local Challenges

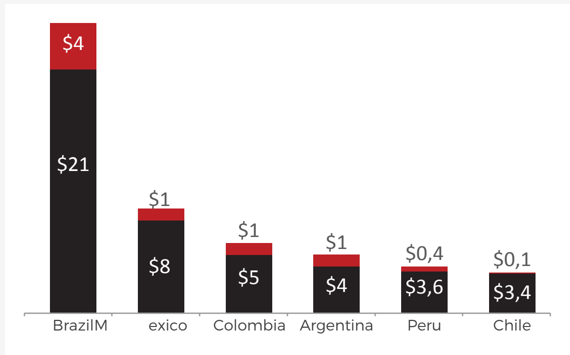
M-commerce has been slow to launch in Latin America, with a number of structural factors inhibiting its growth.

Both merchants and consumers have yet to scale the m-commerce learning curve: it is estimated that in Brazil, by far the region's most mature market, fewer than 10% 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 in 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 2G. As a result, m-commerce represents only around 10% of total e-commerce sales region-wide.

But the groundwork is being laid for swift m-commerce growth, due in large part to the rapid expansion of smartphone penetration and 4G coverage. Currently, roughly 49% of Latin Americans aged 15-65 have smartphones. By 2019, this number will exceed 70% in Mexico, Colombia and Chile. In all of Latin America, 57% of the mobile phone user population will have smartphones by 2019.

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, mobile commerce sales are projected to grow 40-60% in 2017, depending on the market.

E-commerce and M-commerce Sales
in LATAM, 2016



M-Commerce growth driven by homegrown solutions

Certain segments will champion this growth much more than others. In Latin America's traffic-choked cities, the on-demand economy is a major driver of m-commerce. 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 an m-commerce low-hanging fruit 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% made from a mobile device—iFood estimates it is capturing 60% of the online takeout market, valued at $1.5 billion. A large part of its success comes from enabling small, informal restaurants to take part, even if they do not have a broadband connection. This is done via a special iFood POS device connected via 3G, which receives and prints orders. This is crucial in a country where broadband penetration is limited, particularly among local, mom-and-pop establishments.

iFood is not alone: its competitors include HelloFood and PedidosJá. But restaurant food is only a small slice of the enormous delivery market being disrupted by m-commerce. Rapiddo is an Uber-style delivery service, providing on-demand package delivery via motorbike, bicycle or van. In Colombia, taxi hailing company Tappsi has just partnered with mega online marketplace, Linio, to make same-day deliveries. In Sao Paulo and Bogota, where traversing the city can take longer than an international flight, such services are embraced wholeheartedly.

In Latin America, 90%+ of mobile users are on a prepaid plan, purchasing data in bundles to be used on social media and messaging. Customers are averse to spending their data on 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 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 150% and the mobile channel now represents 40% of all NetShoes' online traffic.

M-commerce will continue to climb, even in Brazil, which is coming out of a painful recession. But international 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 who understand these dilemmas have a leg up.

M-commerce payments

Despite the opportunity, limited penetration of electronic payment methods remains a large barrier. In Brazil, cash-based *boletos bancarios* are a mainstay of e-commerce shopping, but on-the-go goods and services consumed in the mobile channel are not compatible with this payment method. In Brazil and other less developed markets, the preference for cash is a quagmire for merchants hoping to conquer the mobile channel.

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 their phone and 56% of users report to have never made an m-commerce purchase. The most often-reported reason for hesitancy is fear that mobile transactions are not secure; the second reason 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 10% of all e-commerce sales and is heavily dominated by taxi apps 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. Entel represents only 7% share of mobile users, however. Telecom giants Movistar and Claro have not yet developed these capabilities.

Thus, outside of Brazil, m-commerce has a long road ahead and both merchants and payment companies must coordinate to promote its adoption. There is a clear opportunity to develop and evangelize card-on-file capabilities in mobile apps and sites. Visa is leading this space with last year's launch of Visa Checkout and a flurry of similar products are being launched by local banks and payment processors. There is ample room for competing products from gateways, 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 20% in Peru, precluding a huge population from access to card-only m-merchants. Although costly to merchants, enabling cash-on-delivery attracts first time users to m-commerce, especially those with no other device by which to place orders. While mobile will grow, organic growth can only take merchants and payment providers so far; smart innovation that works around local problems is essential to win.

5.

Mass Disbursement for Marketplaces: More Demand than Supply

Choosing the right partner for payouts may be just as critical as for payment collection.

In many ways, Latin America has been a pioneering region for online marketplaces. MercadoLibre, founded in Argentina in 1999, was one of the first marketplaces in world to scale and is today among the top e-commerce sites in Latin America. Following in its footsteps, marketplace Linio launched in Mexico in 2012 and tripled in size in five years.

With the onset of service-oriented marketplaces in emerging verticals like transportation (Uber), hospitality (Airbnb) and education (Udemy), marketplaces are becoming even more commonplace. And rapid growth of these companies is changing how Latin Americans live, consume and pay.

For example, as of August 2016, Uber was operating in in 65 cities in Latin America and had completed 45 million rides, a ten-fold increase from August 2015. Bloomberg Technology reports that Mexico City is Uber's busiest city in the world, while Brazil is its number-three world market. Uber probably contracts close to 200,000 drivers throughout the region. Likewise, of Airbnb's two million global hosts, about 300,000 of them are in Latin America. Udemy, a startup marketplace for online learning, has 2,000 Latin American instructors selling their services on the Udemy platform for a fee.

The mega-success of these companies in Latin America is inspiring local entrepreneurs to start similar companies— think "Uber" for dog-walking, babysitting, food delivery. Technology is enabling more and more vendors to sell their products and services, creating a challenge but also huge opportunity for payment companies.

Twice the transactions

Marketplaces present a challenge to payment service providers because twice as many transactions need to be processed. Two transactions are needed for each purchase: payment collection from the buyer and a payout to the seller. And these transactions do not take place symmetrically—while payment processors collect funds from buyers at the time of purchase, sellers are paid later in a consolidated fashion, most often weekly. For payment companies working with clients like Uber, with 50,000 drivers in Mexico City alone, the task is daunting. As such, the stellar growth of marketplaces worldwide has brought about an entirely new payments product: mass disbursement.

Banking barriers

However, mass disbursement in Latin America is challenging for a few reasons. One is the lack of access to banking. In most countries, smartphone penetration still exceeds bank account penetration, most acutely in Mexico, Colombia and Peru. Marketplaces most commonly pay vendors via a weekly bank transfer, so aspiring Uber drivers with no bank account cannot get paid. While most drivers who own their own car likely are banked, Uber operates a secondary model, particularly in Mexico, in which fleet owners manage a group of vehicles and drivers. Under this model, the driver looks more like a traditional employee, is in a lower socioeconomic category and is much more likely to be unbanked. Paying these vendors all of a sudden becomes a huge headache. And in local marketplaces with much lower barriers to entry—like dog-walking—a high percentage of these sellers are unbanked with no efficient way to get paid. This threatens the very existence of local startups, which depend not only on recruiting customers but also sellers.

SMARTPHONE VS. BANKING PENETRATION

Country	Smartphones	Bank Account
Brazil	48%	72%
Mexico	60%	48%
Colombia	62%	63%
Argentina	53%	72%
Chile	66%	69%
Peru	43%	39%
Others	36%	32%

Source: World Bank Findex, eMarketer.

Border hurdles

A second challenge is that many marketplaces operate across borders. This means payment service providers serving international marketplaces also have to manage and settle several international currencies, make international bank transfers, face currency risk and grapple with endless regulation. For many Uber and Airbnb transactions in Latin America, the customer is an international traveler transacting in dollars, while the driver and host must receive funds in their local currency. To the extent that cross-border payouts become more accessible to marketplaces, Linio and MercadoLibre are themselves turning into cross-border companies, enabling their sellers to sell goods abroad.

Lack of bandwidth

The third problem for the rise of mass payouts is the lack of supply compared to the sheer volume of demand. Most e-commerce gateways and payment service providers do not have the proper capabilities to handle mass payouts and merchants may not be aware of the solutions available in the market. dLocal, a leading payment service provider for Latin America, provides mass disbursements to some of the world's largest tech companies, but so far they have kept a low profile. Visa and MasterCard both have mass payout services but have failed to properly market these products and take advantage of the growing opportunity in the region.

Bridging Banking Barriers with Prepaid Cards

Some payment companies are trying to address these challenges. Most notable is Payoneer, which has pinned its success on helping small and midsized companies succeed in e-commerce. Its solution is an e-wallet connected to a prepaid debit card where sellers receive their funds. This helps provide unbanked sellers with an electronic means of receiving their compensation. Doing so brings unbanked sellers into formal banking infrastructure and creates a world of new opportunities for banks and others who want to sell them services.

This solution may also help to solve the decade-long conundrum around prepaid in Latin America, which by all definitions has failed to scale, even among the unbanked who have no other electronic payment method. This is because the prepaid card has always been conceived of as a way to pay rather than get paid; to pay, cash is always an acceptable alternative and therefore a prepaid card is superfluous. However, if a seller's patron insists on a prepaid card as the only way they will disburse funds, interested sellers will be eager to adopt them.

Border crossings

Payoneer, which specializes in cross-border payments, is also helping marketplaces operate internationally. In March 2016, Linio announced that it selected Payoneer as its vendor to handle cross-border payouts, providing sellers on its site access to the full addressable e-commerce market in Latin America of roughly $60 billion. As Payoneer and others expand this model in Latin America, intra-regional cross-border e-commerce, which today is tiny, will become a more and more exciting channel for sellers to explore.

Next steps and key takeaways

While Payoneer is succeeding on the payout side, it does not handle payment collection. This is lamentable, since most merchants would prefer to work with just one payments processor. The problem is that very few companies handle both sides of the business. dLocal is one with capacity for high volume and expertise on both sides. MercadoPago, the payment company owned by MercadoLibre, conducts both within its MercadoLibre ecosystem. PayPal dabbles on both sides but works with local merchants in Brazil and Mexico only. The opportunity will surely attract more the space.

Final lessons

Thus, the lessons are multi-fold. Marketplaces need to prioritize the seller side of their business and find efficient, low-cost ways to manage disbursement via an experienced payment partner. Payment companies—including PSPs, card networks, and others—should watch this market for emerging marketplace verticals to understand where growth will come from in the short term and tackle those opportunities. While dLocal, Payoneer and the few others providing disbursement on a large scale are facing limited competition thus far, this will change as the opportunity becomes more visible. And finally, the more services a PSP can provide, including payment collection and processing, remittances, payouts, fraud management, etc., the more sticky the relationship with the merchant becomes. This is perhaps the best defense against encroaching competition.

Find out how Americas Market Intelligence can help you identify, develop, and implement winning strategies in Latin America.

Lindsay Lehr
Senior Director
llehr@americasmi.com
+1 (305) 873-4311

Americas Market Intelligence

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