

FINANCE & PAYMENTS

Payments overview

Unless you are a UK or American business, it will not be surprising that payments cards are not the most popular form of payment in Germany.

In fact, credit card penetration is around 20%, with only 36 million credit cards issued in 2014.

The card picture is starting to change however. There are more cards in circulation every year (27.5m in 2012, 36m in 2014) and is an ongoing trend which should continue as fees are on the decline due to regulatory pressure. There is also an element of generational change that is affecting the use and adoption of cards.

The four payment methods below are the most common in Germany as of 2015: open invoice, PayPal, credit card and direct debit. On mobile devices, open invoice and PayPal are the preferred options. For some readers, it is important to highlight direct debit usage. In many countries, this payments mechanism is used primarily for regular, fixed amounts. For example, monthly bills such as utilities. In Germany, a direct debit can easily be set up for a one-off transaction. The benefits to the merchant include a lower cost of processing and direct transfer of funds to the merchant account. Likewise for the customer, direct debit is easy to control and includes a mechanism for disputing transactions.

How consumers will adapt/adopt to new payments methods is hard to predict. Likewise, new developments often need critical mass before both businesses and consumers feel happy about adopting them. Brands such as Apple Pay go some way to mitigate this but, perhaps widespread adoption will be a generational change.

Many e-wallets ('wallets') are based on debit/credit card and direct debit payments in the background and whilst credit card usage is limited, debit cards are much more widely available. Wallets consist broadly of a technical solution that contains the core account details required to process a payment. They replace cards as a form factor and store multiple payment types, allowing the user to select the most appropriate one for a transaction. Most commonly they are available as an app for popular mobile devices.

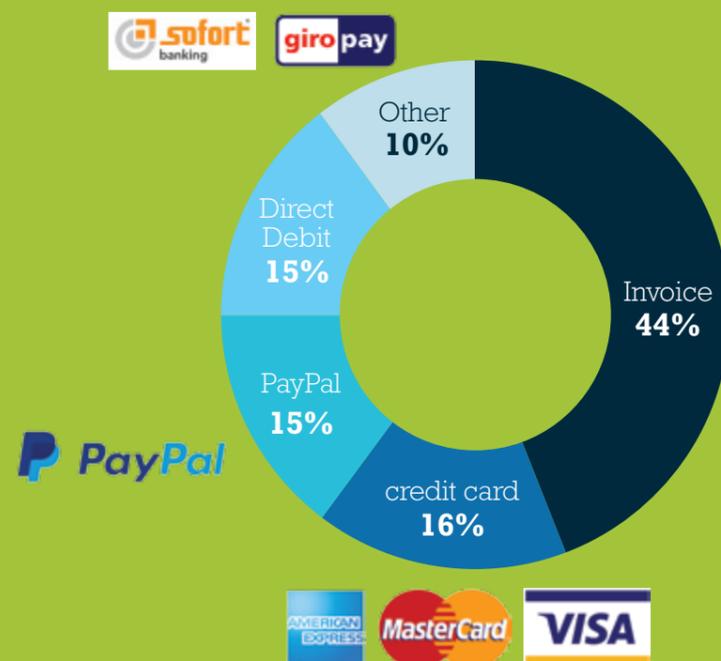
As the market matures customers are getting more used to electronic payment methods like PayPal and SOFORT.

Open invoice is on the decline based on the payment methods share, but due to the growing ecommerce market is steady in numbers. In some sectors, such as fashion, open invoice is still preferred by consumers due to the high return rates.

Table 2: Overview of popular online payment methods in Germany

Source: 4 www.statista.com

- Sofortüberweisung is a kind of cash in advance
- Giropay is similar, but processed directly through a merchants website



Implementation

Complexity of implementation depends on how the payment flow is implemented in general. For methods like PayPal Express Checkout or Amazon Payments the shipping and billing address doesn't need to be collected by the webshop, but will be provided by the wallet itself. This means different process flows for different payment methods. For other methods such as debit/credit card payments and open invoice you still need to collect this data yourself. This doesn't mean that the methods should be avoided at all as this might be more convenient for the customer. Advance payments and cash on delivery are hard to implement and handle/reconcile.

Currently a typical mixture of payment types merchants make available to the customer in Germany are:

- PayPal
- Open invoice
- Direct debit
- Debit / credit card
- SOFORT

Common payment methods like credit cards and direct debit have been consolidated over the past years with the emergence of wallets like PayPal or MasterCard MasterPass. The convenience of the payment and checkout process has been the focal point of most providers, as this is something that you can change rather quickly in contrast to the perception of security. Ensuring that payment methods are also supported via mobile devices has been on the agenda for many payment providers.

Credit cards are still not very common for German customers; even when debit cards are included, this is the case especially compared to other countries (credit/debit cards make up 20% of payment method share in Germany, 80% in the UK). The bias toward credit cards is despite the fact that they are outweighed by credit cards by a ratio of 5:1 (Source: Paypers 2014). This is because in Germany the majority of debit cards are not currently supported. However, due to the wallet solutions, the continuously strong economy in Germany and the future cap on card fees there is no reason to believe that this payment method won't continue to grow.

Open invoice is still very popular for industries with high return rates, where customers order more goods than they would like to keep, e.g. a pair of shoes in two different sizes. Customers then only pay for the pair they keep and return the other one. Based on customer experience and convenience this is not very likely to change. PayPal introduced their own open invoice solution just this year (PayPal Plus).

Access to the local payment methods is usually via a specialised local supplier or payment service provider (PSP). Your current PSP may have international connections that aggregate these services and make acceptance much easier. Some services also require a local bank account for acquiring and acceptance.

Consumer attitudes towards online payments

Germans are very risk-averse and have reservations about new alternative payment methods different from the ones they are used to, like open invoice or direct debit.

However, tech-savvy and younger customers are much more likely to try out/use new electronic payment methods. For those especially, convenience is the key driver for user acceptance.

Consumer recourse on payments

Aside from the regular consumer protection laws that account for any transaction made regardless of the payment method, there are several others. The most important one is the standard SEPA (Single European Payments Area) regulations for direct debit. Returns until 8 weeks after settlement without declaration of reason. If there is no valid mandate SEPA direct debits can be returned 13 months after settlement. Other payment providers offer further buyer protection (e.g. PayPal) that may increase financial exposure for the merchant.

Common payment types

There are too many payment method options available (>350) to list them all here, so the following list focuses on the most popular. Processes are outlined below and do not include any reconciliation requirements.

Overview of process

Direct Debit	<ul style="list-style-type: none"> Customer provides account details (BBAN/sortcode or IBAN/BIC) Customer signs mandate (e.g. clicks that he accepts it) Direct debit request is sent to the merchant bank Merchant bank collects money from the customer's bank account
Open Invoice	<ul style="list-style-type: none"> Customer receives goods with invoice Customer transfers money to merchant's bank account based on the invoice details, including correct references
Wallets	<ul style="list-style-type: none"> Customer stores credit card or bank account details (for direct debit) in wallet Customer selects wallet as payment option and is redirected to the wallet page Customer logs in via user/password Customer selects payment instrument (optional in case there are multiple credit cards or accounts in the wallet) Customer confirms payment Merchant will be paid by wallet vendor
Online Banking	<ul style="list-style-type: none"> Customer logs in via login details for the customer's online banking Customer is redirected to online banking (e.g. Sparkasse) Customer confirms payment via PIN/TAN Payment initiated to merchant

Degree of popularity

Direct Debit	HIGH
Open Invoice	HIGH
E-wallets	
Paypal	HIGH
MasterCard MasterPass	LOW
Online Banking	
SOFORT	MEDIUM
Giropay	MEDIUM

Any decision that impacts the customer offer should be based on a knowledge of their requirements. For some brands, their customer is unlikely to have an iPhone so looking at Apple Pay at the moment wouldn't bring any benefit. Likewise, customers with a poor credit history might be declined for open invoice payments. Therefore, it is important not to just understand the customer, but to also offer a degree of choice in payment methods.

Fraud & risk management

A fast-growing ecommerce market like Germany requires increased attention by the merchant on fraud and risk management. The implementation of proper risk settings and a system infrastructure is the key for an efficient interaction of risk and fraud management. To be able to offer customers various payment methods during the checkout process, it is important to reduce risk but at the same time to maintain a high conversion rate. The German market has relatively lower use of payment cards online, the payments type mix provides additional challenges. For example, open invoice-related fraud phenomena (can be first party and/or third party fraud), account takeover, new account fraud, friendly fraud and identity theft. But open invoice should be considered as a payment option, because it is a conversion booster as you can see in the following graphic. It shows that if open invoice is rejected due to risk checks, and only alternative payment methods are offered, conversion rates diminish extremely.

Conversion benefits of offering Open Invoice



Source: *avarto*

Some service providers in the ecommerce market are offering active payment control tools which are able to keep the conversion rate at a high level as well as reducing the risk of a payment default. These tools are the most effective way to check the credit information of a customer and to offer based on defined parameters the best selection of payment methods. These services require skilled risk managers and a risk management system which can be adjusted to needs of a company.

However, the market is continuously in a changing and challenging landscape, with the result that efforts are getting bigger and the technology to combat fraud is becoming increasingly important. Due to the rising desire of companies to develop more markets and to offer their customers the latest payment methods, four main criteria arise in regards to fraud:

Growth of global ecommerce activity Fraud patterns are specific to different markets.	Emergence of mobile eCommerce New channel for fraudulent activity. Number of mobile users is rising.	Organized crime - focus on ecommerce Fraudster's continuously developing new ways of attacks.	Focus on data security Risk of lost data is rising, as well as the need of enhanced security measures.
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Source: *avarto*



TOP 8 FRAUD ATTACKS



Source: MRC Global Fraud Survey 2014

If a merchant decides to enter the German market, the monitoring of cross-border transactions and activities are important to prevent fraud before it starts and in this context to be able to recognize new upcoming fraud patterns. The same goes with the emerging mobile ecommerce market. Since the use of mobile payment and dynamic multichannel ecommerce activity is becoming increasingly important for companies and merchants, new channels for fraudsters are formed for their fraudulent activity.

As part of opening new channels, companies are seeking an omnichannel business model which is increasing the business potential but which again is opening new ways of fraud. This needs to be tackled at the origin, through improved fraud detection and awareness of fraud agents. A system which offers the cross-covering of different marketplaces and markets is of great importance to ensure a high fraud prevention rate.

The constant improvement of fraud prevention systems and skilled fraud agents is a process which should not be neglected. Fraud in the area of ecommerce is not a new phenomenon and therefore it is not surprising that it has evolved to an organised crime structure. Fraudsters are becoming more professional, their methods have bigger impact and the chances of preventing their attacks are shrinking.

It is to mention in this context that the topic of data security and how customer data is stored should be on the agenda of every ecommerce-involved party. Security issues and lost customer data can have a significant impact on fraudulent activities and is offering fraudsters a wide range of possibilities.

Useful technology such as device fingerprinting or automated fraud checks based on fraud security models can help to reduce fraudulent activity to a minimum. Since there is no "one size fits all" system or service, every fraud prevention activity is dependent on the merchant and the industry. Experienced fraud management teams are able to reduce the risk of fraud additionally by conducting manual fraud checks.

The last point is an increasing problem due to various data breaches and is the enabler for most of the fraud types mentioned above.

In general, the value of ecommerce fraud in Germany is worth about 0.5% of turnover. Fraud levels on international and mobile transactions are higher.

The tools available to merchants in the German market are very similar to other markets – 3D secure for bank cards (e.g. Verified by VISA), profile tracking, risk scoring, email validation/verification, behavioural analysis, biometric verification and entity link analysis. None of these alone can be relied on to stop fraud but combined they provide a range of tools that mitigate the risk.



- **Fraud losses in 2012: €144.3m**
- **More than 15% of orders are screened for manual review**
- **The activation of 3D secure reduces conversion by more than 20%**

Source: MRC 2014, Paypers 2014

	CREDIT/ DEBIT CARDS	DIRECT DEBITS	BANK TRANSFERS	E-WALLETS E.G. PAYPAL	OFFLINE PAYMENTS
OVERALL LOSS RATE	0.5%	1.5%	0.5%	0.7%	0.1%

Source: Merchant Risk Council global fraud survey 2014

