

Inquiry into Mobile Payment and Digital Wallet Financial Services Questions on Notice to the Reserve Bank of Australia

Public hearing – 26 July 2021

3. Potential savings from least-cost routing of dual-network debit card transactions.

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Mr HILL: If you could take this on notice, unless you have an instant answer: I'm curious, with regard to least-cost routing, what the Reserve Bank's estimate of savings is. It's been put to me in discussions that the commonly touted estimate of 40 per cent savings, which some retailers and some participants put about, is significantly overstated. Tyro's website talks about 8.5 per cent savings. Have you done any work on it, what's your best estimate as to the savings and what are the technical barriers as to why this hasn't been done? The more I've looked at it the more I've understood that it's very complex and not a straightforward thing, seductive as it sounds. Any response to that, if you have a number? If not, take it on notice.

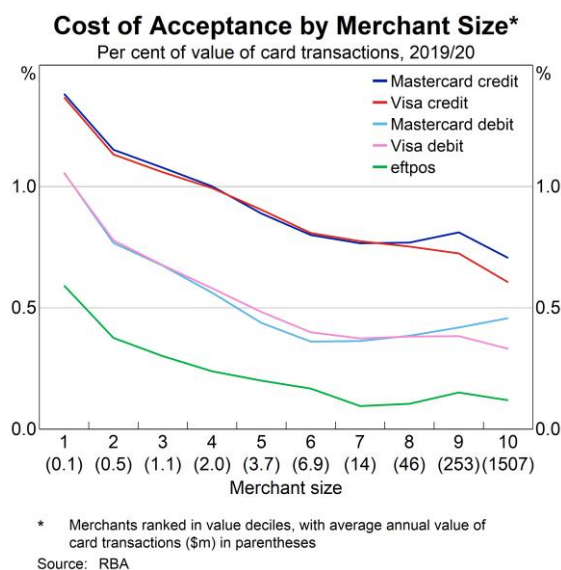
CHAIR: They will take that question on notice.

Response:

The savings from LCR will vary considerably across merchants depending on their card mix, average transaction value, size, industry and pricing plan.

To understand the *potential* benefits of LCR (as well as the impact of its regulatory policies), the Bank monitors the average industry-wide costs of the different debit schemes through its Retail Payments Statistics collection. These data show that, on average, acquirers charge merchants 48 basis points to accept Visa/Mastercard debit transactions, but charge only 28 basis points to accept eftpos (so that, on average, eftpos is around 40 per cent cheaper). The Bank has also periodically collected merchant-level data to conduct analysis on the average cost of accepting card payments for merchants of different sizes. The latest merchant-size-matched analysis (based on data from 2019/20) shows that, on average, acquirers charge merchants around 20-40 basis points less to accept eftpos transactions, than Visa/Mastercard debit transactions (Graph 1).¹

Graph 1



1 A similar analysis of the cost difference between Visa/Mastercard debit transactions and eftpos in 2018/19 was published in an RBA [Bulletin article](#).

However, these *average* data do not necessarily provide a like-for-like comparison of the cost of accepting transactions via the different debit schemes, for two main reasons:

- Compositional differences in the types of transactions processed by each scheme. For example, eftpos has only recently begun processing online transactions and does not process any transactions using foreign-issued cards (which tend to be significantly more expensive than domestic card transactions). This would mean that the difference in the average cost of all debit transactions would overstate the cost difference for similar *in-person* transactions on *domestic-issued cards*.
- Differences in payment plans. About one-quarter of merchants are on pricing plans where the acquirer charges a single price for Visa/Mastercard debit *and credit* transactions. Because credit transactions are more expensive than debit transactions (at the wholesale level), this single price is higher than what the price of debit transactions would be if the merchant had a plan that priced credit and debit separately. (Indeed, a comparison of merchant fees under different plan types shows that merchants on bundled (debit and credit) plans pay significantly more for Visa/Mastercard debit transactions than merchants on other plans.) This practice would make the average cost of Visa/Mastercard debit transactions higher than eftpos, even if the *wholesale cost* of debit transactions through each scheme was exactly the same.

When we try to control for these differences to get a like-for-like comparison, Visa/Mastercard debit transactions appear to remain materially more expensive than eftpos transactions on average for most merchants, and especially smaller ones.

Whatever the current average price differential between eftpos and Visa/Mastercard debit transactions, this price difference is unlikely to be a particularly good estimate of the savings that can be achieved through least-cost routing. In particular, not all debit transactions can be routed, so merchants will be able to realise savings on only a proportion of their debit transactions.² Also, when a merchant requests a switch to LCR, their acquirer may take the opportunity to review their pricing and card/transaction mix; the Bank's understanding is that merchants' plans are often reviewed only quite infrequently and so may not be reflective of the current levels of wholesale costs.

² Debit transactions that cannot be routed in include those made: using a mobile phone; using a physical card that is inserted into the payment terminal; and most online transactions (LCR online is in its infancy).