What *Really* Drives Consumer (Payment) Choice?
Using Academic Models to Develop Business Applications

Visa Payment Panel Study: Discussion
Jon Zinman
Dartmouth College
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Overview of My Comments

- Describe data
- The possibilities: examples and benefits of “modeling” approach
  - What really drives payment choice
- Back to data: a few additional pieces needed for modeling approach
- The applications: business
  - Pricing strategy
    - Debit fees
    - Checking account fees
    - Rewards
    - Credit card interest rates
  - (Truly) targeted marketing: what features speak to consumers?
    - Price vs. value-based
  - Product development strategy
    - If consumers are indeed using debit for spending control, there are other (more direct ways) of providing this service
The Visa Data

• Fantastic
  – Credit and debit
  – In principle ability to link transaction and account characteristics at individual (or better yet household) level

• Superior to anything currently available:
  – For free (government datasets)
  – For sale (possible exception of new Forrester data)
The Possibilities

• Test hypotheses (rather than just describe trends)
  – “Modeling” approach
  – Use micro, not aggregate data
    • Use consumer and transaction-level data
  – Some financial institutions and consulting firms do this, but unlikely they are fully optimized
  – Many institutions do not do this at all
    • Economies of scale and scope in data mgmt/analysis

• And thereby learn something about how consumers *really* make retail payment choices.

• What do I mean by this?....
Example #1 of Modeling Approach (vs. purely descriptive approach)

• Descriptive: “more use debit because of broader acceptance”

• Model. Test hypothesis: “When the proportion of merchants with POS PIN terminals increases by 5%, debit use increases by X%”
  – Subtext: acceptance clearly matters, useful to know how much…
  – BUT there’s clearly a deeper value proposition for consumer here…
  – Why is there demand for debit in the first place… “we built it, why have they come?”
Example #2 of Modeling Approach (vs. purely descriptive approach)

• Descriptive: “Despite their loyalty to debit cards, debit users have not reduced their use of GPC”

• Model. Test hypothesis: “Debit does not cannibalize credit.”
  – Modeling enables us to address question: “What would have happened to credit growth if not for debit?”
  – My view: debit and credit are substitutes
    • Zinman (2005)
    • Credit usage leveled off despite major product improvements: lower rates, broader acceptance, more generous rewards, better security, lower annual fees….
  – This has practical implications
    • For marketing
    • For pricing
    • For product development
Example #3 of Modeling Approach (vs. purely descriptive approach)

• Descriptive: “Debit is the card of choice at discount stores…."
• Model. Test hypothesis: “Consumers prefer to use debit at discount stores because doing so helps them manage their spending”. I.e.,:
  – Transaction characteristics drive choice per se (holding everything else constant)
  – Consumers who multi-home based on transaction characteristics spend less (of their discretionary dollars)
• Alternative explanations
  – Acceptance
  – Customer mix. Maybe discount shoppers:
    • Less likely to have credit rewards (and more likely to single-home with credit)
    • More likely to be revolving at high rates (and less likely to “borrow-to-charge”)
What We Can Learn From Modeling Approach: Overview

• What’s the relative importance of the each of the following features:
  – Price. May be implicit, includes:
    • Rewards
    • Cost of borrowing-to-charge for credit card revolvers
  – Acceptance
  – Perceived spending control

• Do this not only on average (across all consumers), but by segments, and….
What We Can Learn: Truly Targeted Marketing

• Identify *individual customers* as particular types:
  – Price-driven
  – Miles-driven
  – Value (e.g., spending control)-driven
  – Indifferent

• And then tailor prices, products, and product presentation accordingly
Missing(?) Pieces

• Additional microdata needed for modeling approach:
  – Cash back*
  – Acceptance*
  – Late credit card payments?
  – Rewards generosity?
  – Checking account terms (including overdraft provisions)?
  – Link individuals for household-level analysis
The Applications

• Pricing strategy
  – Debit fees
  – Checking account fees
  – Rewards
  – Credit card interest rates

• Government relations strategy
  – Antitrust implications
  – Research with value beyond retail payments (savings and Social Security)

• (Truly) targeted marketing: what features speak to different “types” of consumers?
  – Price vs. value-based
  – Market to indifferent guys?

• Product development strategy
  – If consumers are indeed using debit for spending control, there are other (more direct ways)
    of providing this service
    • Commitment savings products
    • Customer-set monthly spending limits on credit
    • Text or email notifications whenever spending (by category) exceeds a customer-set target