About this paper
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EXECUTIVE SUMMARY

Debit cards are deeply woven into the fabric of commerce. Our consumer research has revealed that uptake is significant and use is growing, with strong preference for debit across a wide swath of merchant verticals and transaction types. This is particularly the case for consumers from rural areas and those banking with community and regional financial institutions, who show the highest favoritism for debit.

Given the popularity of debit cards, consumers are understandably frustrated when they encounter a merchant that does not accept debit as a form of payment. Our survey results show that this experience can have near- and long-term consequences for merchants. Not only does non-acceptance impact the amount customers are likely to spend, it also decreases their propensity to return.

Our merchant research shows that debit acceptance is widespread, with many businesses attributing a significant percentage of their annual revenue to debit transactions. Large merchants, in particular, have the most favorable view of debit and are most likely to prefer their customers use it for purchases. Furthering acceptance with small merchants will require continued education, particularly as it relates to cost and debit’s many advantages over paper currency.

Looking ahead, our research has revealed several pertinent debit growth opportunities. Increasing debit’s share of digital commerce via digital wallets, displacing cash in sub-$25 transactions and driving acceptance with small businesses represent areas that will serve to expand debit volumes further.

KEY FINDINGS

- More than one in four respondents said they are using debit cards more often than they were last year at this time.
- Respondents that bank with community and regional financial institutions chose debit cards as their top preference for ‘everyday transactions.’
- Grocery, discount stores (e.g., Walmart, Target) and small/local businesses are the top categories where respondents prefer to use debit.
- 55% of respondents who have encountered a merchant that doesn’t accept debit cards indicated they are unlikely to return to that merchant.
- More than one in three merchant respondents said debit accounted for half or more of their annual revenue last year.
- 63% of merchant respondents stated that their customers are using debit cards more often compared to this time last year.
- 84% of merchant respondents with 1,000 or more employees prefer their customers to use debit cards when making purchases.
Methodology
In Q1 2018, we surveyed 2,032 US consumers aged 18 and above who have a relationship with a financial institution. The survey was designed to better understand their payment method preferences and payment experiences. Of these respondents, 52% were customers of a national bank, 25% were customers of a regional bank/credit union, 21% were customers of a community bank/credit union and 2% were customers of an online/virtual bank.

We simultaneously ran a survey with 257 business-to-consumer (B2C) merchants that primarily operate in the US. The survey was intended to investigate payment acceptance trends and pain points. Respondents qualified for the survey only if they had an understanding of how their business handles customer payments, and included titles such as CEO/president, business owner, CFO, CIO, COO, treasury/finance manager and controller. A third of respondents were from businesses with 1-50 employees, 26% were from businesses with 51-250 employees, 24% from businesses with 251-1,000 employees and 17% from businesses with 1,001 or more employees.

Market Overview
Debit cards are widely adopted by a large portion of the US population that uses banks. As shown in Figure 1, 89% of respondents to our survey use debit cards, and more than one in four have increased their usage compared to this time last year. Overall, debit exhibited a net usage increase year-over-year (YoY).

Our survey also revealed that cash and check usage is decreasing; 29% of respondents indicated they are using cash less often, and 43% indicated they are using checks less often compared to the prior year. We believe debit cards are playing a significant role in displacing cash and check volume, which has in part led to the rise in YoY debit usage. We anticipate this trend to continue in coming years.

Figure 1: Debit cards are widely adopted, and usage is increasing
Source: 451 Research
DEBIT DIFFERENCES: UNDERSTANDING RURAL CONSUMERS AND COMMUNITY/REGIONAL BANK CUSTOMERS

Debit cards have earned a role as the go-to payment method for the daily purchases of many consumers. This is particularly the case for consumers living in rural areas of the US, for whom debit is their top choice for ‘everyday’ transactions (e.g., coffee, dining, groceries). As shown in Figure 4, 44% of respondents who said they live in a rural area prefer debit for ‘everyday’ spending, besting credit cards, cash, checks and digital wallets. Respondents from metropolitan areas are close behind, with 38% preferring debit for everyday purchases – just three percentage points behind credit.

Figure 2: Rural consumers prefer debit for ‘every day’ transactions over all other payment methods

Source: 451 Research

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Figure 2: Rural consumers prefer debit for ‘every day’ transactions over all other payment methods

Source: 451 Research

What payment method do you prefer for everyday transactions?

Rural consumers are most likely to bank at community or regional financial institutions, compared to those living in suburban or metropolitan areas. We found that nearly two in three respondents living in a rural area are customers of either a community or regional bank, compared to 46% who live in suburban areas and just 24% that live in metropolitan areas.

Perhaps unsurprisingly then – given that rural consumers have an affinity for debit for everyday spending – community and regional bank customers show a noted favoritism for debit for many types of transactions. As shown in Figure 3, debit was their top choice for everyday transactions, transactions in the $25-100 range and digital wallet use (for those that are digital wallet users). Community and regional bank issuers would be wise to ensure they are effectively marketing and promoting these top use cases to their debit cardholders.
Regional and community bank customers are also more likely than customers who bank with national or online financial institutions to have a preference for debit when shopping across different merchant segments. As shown in Figure 4, this is a trend that holds true across all merchant segments where we asked respondents to state their preferred payment method.

In our survey, grocery, discount stores (e.g., Walmart, Target) and small/local businesses emerged as the top categories where shoppers prefer to use debit. Discount stores and gas had the largest gap in debit preference between the two cohorts of bank customers, of 10 percentage points and seven percentage points, respectively. But despite the debit preference differential between the two bank cohorts across all segments, the order of the merchant segments in which they prefer debit does not differ in a meaningful way.

Across both groups, online payments, such as shopping with a retailer, making recurring payments (e.g., cable bill) and booking travel (e.g., hotel, airline) saw the lowest preference for debit. However, they present a clear-cut growth opportunity for debit issuers – especially community and regional banks – to target by promoting the use of digital wallets.

Figure 4: Grocery, discount stores and small/local businesses are the top merchant categories where consumers prefer debit
Source: 451 Research
Debit Cardholders and the Customer Experience

While the majority of shoppers have not been denied the option to use debit at checkout, one in five said they encountered a merchant over the past year that did not accept debit cards. Merchants that choose not to accept debit cards must understand that their decision to limit customers’ payment options at checkout results in much more than just a minor inconvenience. It can have near- and long-term consequences that can hinder the performance of their business.

Figure 5: Merchants not accepting debit cards face significant consequences

Source: 451 Research

As shown in Figure 5, a variety of serious business repercussions can result from a merchant failing to provide customers with the option to use debit. These include:

- **Negative perception.** Shoppers are four times more likely to place the blame on the merchant for not accepting debit cards than their bank that issued the card.
- **Decline in loyalty.** Non-acceptance directly impacts customer loyalty and future visits because more than half of respondents who encountered a merchant that didn’t accept debit cards indicated they are unlikely to return.
- **Smaller ticket sizes and lost sales.** The lack of option to use debit resulted in 23% of respondents spending less at that merchant, and 15% leaving the business and making the purchase elsewhere.

For merchants that don’t accept debit today, it’s critical to consider the total impact of non-acceptance. Payment options are a component of the overall customer experience, and limiting them has a direct impact on sales success. In the following section, we take a deeper dive into merchant acceptance trends.

Merchant Acceptance Trends

Given widespread adoption and use among consumers, debit cards are understandably an important source of revenue for merchants of all sizes. As shown in Figure 6, two-thirds of merchant respondents said that a quarter or more of their annual revenue is generated from debit card transactions, and more than one in three said debit accounts for half or more of their revenue.

However, not all merchants are equal when it comes to the impact of debit on their bottom line. Businesses with 1-50 employees are most likely to see debit account for the smallest percentage of their sales, with nearly one in four stating that debit accounts for less than 10% of their annual revenue. On the other hand, large businesses with 1,001 or more employees experience the most pronounced impact from debit; 46% said that debit drives half or more of their revenue.
Figure 6: One in three merchants derive half or more of their annual revenue from debit cards

Source: 451 Research

Mirroring our consumer survey finding that many respondents have increased their debit card use YoY, merchant respondents have noted that debit card transactions are on the upswing. As shown in Figure 7, 63% of respondents stated that their customers are using debit cards more often compared to this time last year. Nearly a third said that the increase in debit use has been significant.

From an organizational size standpoint, the increase in use has been experienced most significantly by merchants with 1,001 or more employees, where 73% have seen debit transactions increase YoY. As expected, merchants with 1-50 employees saw the smallest – yet still significant – growth in debit card transactions, with 43% indicating a lift in customer usage.

Underscoring the growing opportunity for debit online, our survey also revealed that businesses with significant e-commerce revenue had the largest YoY lift in customers’ usage of debit. For those merchants that said half or more of their annual revenue comes from e-commerce, 77% saw an increase in debit usage, compared to just 28% for merchants that have less than 10% of annual revenue derived from e-commerce. Online and mobile channels are becoming increasingly important areas where debit issuers must ensure they are promoting spending.
A TALE OF TWO BUSINESSES: UNDERSTANDING SMALL AND LARGE MERCHANTS

Our survey revealed that not only do respondents from large businesses see debit account for the most significant – and fastest growing – component of their revenue as compared to smaller businesses, they also more likely to have a favorable view of debit. As seen in Figure 8, more than four out of five businesses with 1,001 or more employees prefer their customers to use debit cards. Similarly, 69% consider debit to be a ‘highly important’ payment option they offer to their customers.

Debit’s popularity with large merchants is in part attributed to its cost-effectiveness; more than two in three large merchant respondents said debit cards offer them favorable economics. A primary driver for this was the passing of the Durbin Amendment in 2010 as part of the Dodd-Frank Act, which significantly lowered debit interchange pricing for cards issued by banks with more than $10bn in assets. This has resulted in measurable cost savings, particularly for merchants handling a high volume of transactions.
While debit acceptance among respondents from large businesses was universal, small business respondents showed the lowest acceptance rate, with nearly one in five not currently accepting debit cards (see Figure 9). We believe this lower acceptance rate can largely be attributed to cost-related concerns, which are pervasive among businesses with 1-50 employees.

**Figure 9: Nearly one in five businesses with 1-50 employees do not accept debit**

Source: 451 Research

As shown in Figure 10, cost concerns are top of mind for small businesses. Companies with 1-50 employees cited lowering payment acceptance costs at their top challenge for 2018 when it comes to accepting payments from customers, and cost/budget was listed as the primary obstacle to adding new payment options for customers.

Clearly, cost-related issues have played a lead role in the decision by many small businesses to accept only cash and checks. We believe further education is necessary to help inform small businesses of the potential cost advantages debit can provide in comparison to paper currency. Cash and checks entail a variety of hidden costs that are often overlooked. These include handling costs and the risk of losses via counterfeiting and bounced payments. Education should also focus on the missed sales opportunities that result from turning away debit cardholders.

We recommend card issuers, networks and acquirers consider monetary support as another strategy to drive debit acceptance with small businesses. Subsidizing point-of-sale terminals and reducing acceptance costs could help sweeten the case for businesses with 1-50 employees to accept debit and would likely result in long-term benefits across the debit value chain.
Outlook and Recommendations

The outlook for debit is promising. Our surveys have revealed that debit cards are seeing growing consumer usage and are a preferred payment method for a variety of transaction types. On the acceptance front, the perception of debit is favorable, and debit drives a significant percentage of merchants’ annual revenue. Looking ahead, we have identified three emerging opportunities that harness the potential to drive debit growth further:

- **Sub-$25 transactions.** We see an opportunity for debit issuers to increase their volume by displacing cash for small-ticket transactions. Cash is still the top form of tender for low-dollar-value purchases, with nearly two in five respondents stating they prefer cash for transactions under $25. Debit isn't far behind, however, garnering the preference of roughly one in four respondents for transactions of the same size. We recommend issuers increase cardholder messaging and promotion for the use of debit at merchant segments where cash use is popular and ticket sizes are generally small, such as quick-service restaurants and small/local businesses.

- **Digital commerce.** Transaction volume continues to migrate into online channels with speed. 451 Research finds that online and mobile transactions are increasing at three times the rate of in-store, with nearly $1 trillion in digital commerce spending anticipated in the US by 2022. While our survey shows that credit is the dominant tender type for online transactions, debit issuers have an opportunity to tap into this growth via digital wallets. We found that 48% of respondents who are digital wallet users already use a debit card in their digital wallet. Debit issuers should target this audience to further encourage and drive the use of digital wallets for online transactions.

- **Small businesses.** Our survey revealed that debit acceptance is weakest among small businesses. We recommend that debit issuers collaborate with acquiring partners to expand acceptance with small businesses through awareness, education, and promotional campaigns. Their messaging should in part focus on the risks of non-acceptance, such as lost sales. For instance, remember that 31% of respondents prefer to use debit cards at small and local businesses, and 15% of respondents who encounter a business that doesn't accept debit will leave the business and make their purchase elsewhere. Small businesses must be made aware of customers’ demand for debit card usage and its growing popularity as a payment method.