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**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
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**LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM - Session III: Competition
and Payment Card Interchange Fees**

– Contribution from Brazil –

20-22 September 2021

The attached document from Brazil is circulated to the Latin American and Caribbean Competition Forum FOR DISCUSSION under Session III at its forthcoming meeting to be held on 20-22 September 2021, via a virtual Zoom meeting.

Ms. Lynn Robertson, Competition Expert, OECD Competition Division - Lynn.Robertson@oecd.org.

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Session III: Competition and Payment Card Interchange Fees

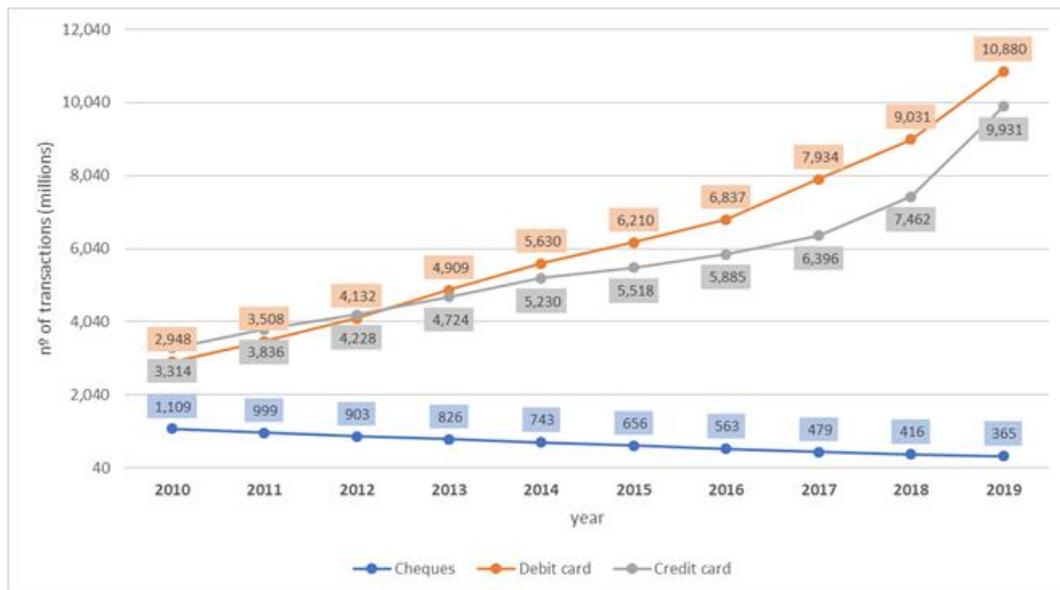
Fostering competition in the payment card industry¹

- Contribution from Brazil² -

1. Introduction

1. In Brazil, the payment card industry has undergone a significant expansion, particularly driven by the technological progress and the economic stability reached in the recent years. The inflation control achieved in the 1990s highly contributed to consumers' trust, boosting the demand for these payment methods. The number of debit and credit card transactions increased more than 269% and 199% respectively, from 2010 to 2019. At the same time, the number of transactions done by cheques has decreased.

Figure 1. Number of transactions by payment methods (2010 – 2019)



Source: Central Bank of Brazil - Prepared by: Department of Economic Studies (DEE)

2. In this context, the greater use of payment cards instead of paper money and cheques contributed to the development of electronic payment methods and the appearance of new types of financial services – FinTechs or Financial Technology. The expansion of

¹ This document brings together information presented in CADE, *Mercado de instrumentos de pagamento*, Cadernos do Cade, Brasília, 2019. Available at: <<https://cdn.cade.gov.br/Portal/centrais-de-conteudo/publicacoes/estudos-economicos/cadernos-do-cade/mercado-de-instrumentos-de-pagamento-2019.pdf>>.

² This document was prepared by Guilherme Mendes Resende, Chief Economist of CADE, and Marina Haddad Tovoli, Deputy Chief Economist of CADE.

the payment card industry, in turn, contributed to the complexity of the industry and has brought new challenges to antitrust authorities in terms of competition law enforcement.

2. Main competitive concerns

3. It should be noted three main challenges related to the complexity of the payment card industry and its own specific features in Brazil. These three characteristics are particularly important to better understand the singularity of this industry and the environment in which new anti-competitive practices emerged.

2.1. A multi-sided platform

4. One challenge faced by CADE in its analysis of cases involving the payment card industry is the adjustment of its tools: as a multi-sided platform, the payment card industry demands other tools than the traditional microeconomic ones, which do not consider the existence of network effects between its different groups (issuers, acquirers, and scheme owners/card brands)³.

2.2. Market concentration ratio

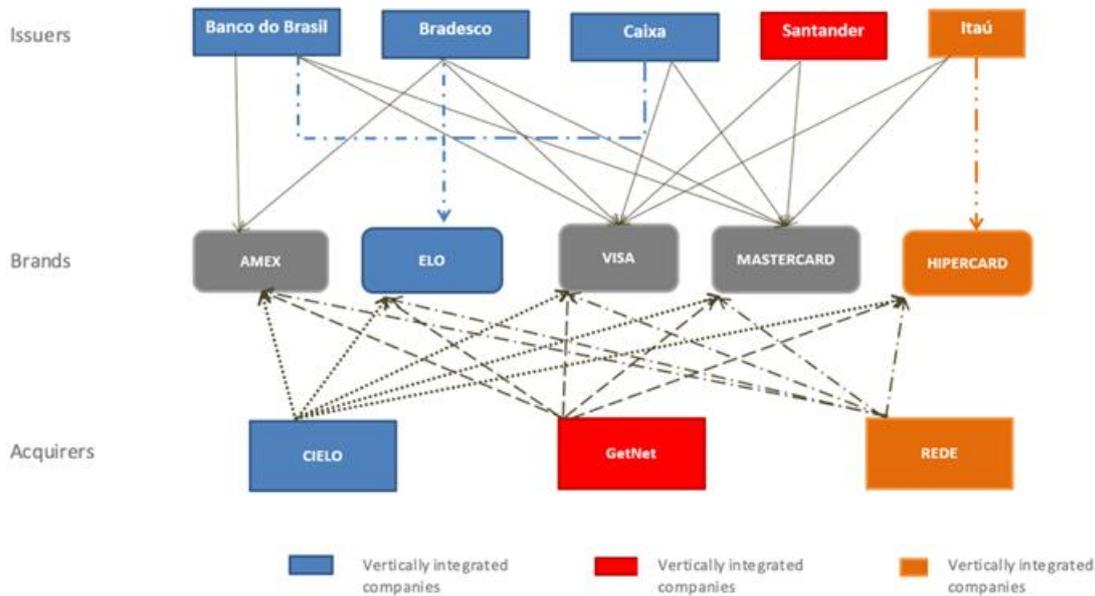
5. Moreover, the Brazilian banking system is the main sector responsible for issuing payment cards. During the 1990s, many state-owned banks were privatized and other ones that were facing financial problems ended up being acquired by major players. This scenario contributed to the increase of market concentration in the banking system. Nowadays, five banks (Caixa, Santander, Itaú Unibanco, Banco do Brasil and Bradesco) manage the card-issuing process and have some control over the card brand side and the acquirer side.

2.2.1. Vertically integrated companies

6. Another issue that raises concerns in the payment card industry is the potential effect vertical integration may have on its competitive dynamics. Even though vertical integration is not illegal per se, since the payment card industry is already concentrated, as incumbent banks started to take control over other links of the value chain, these circumstances led to new anti-competitive practices. Vertical integration not only contributed to a favourable environment for the emergence of anti-competitive conducts, but also imposed entry barriers to new competitors that could foster competitive pressure and innovation.

³ For example, the existence of network effects makes the number of consumers an important factor in the attractiveness of a platform: the higher the number of card brands captured at the Point of Sale (POS), the more attractive the POS will be to consumers (in this case merchants). Similarly, the higher the number of different POS that capture a specific card brand, the more attractive the latter will be to cardholders.

Figure 2. Vertical relations in the Brazilian payment card industry



Source: Prepared by the Department of Economic Studies (DEE)

3. Interventions in the payment card industry

7. Regarding the interventions in this industry, from 1995 to 2019, CADE initiated a total of 14 conduct investigations related to the payment card industry. Out of these investigations, 5 were archived and the remaining ones resulted in “Cease and Desist Agreements”. Among other conducts⁴, exclusive agreements represent 43% of the anti-competitive practices investigated by CADE⁵.

8. In terms of exclusionary practices, the breakage of the Visa and Visanet exclusive agreement was one of the first interventions conducted by CADE. Although this practice is not per se illegal, since the payment card industry is characterized by network effects, there is no sense in establishing such agreements between the acquirer and the card brand sides.

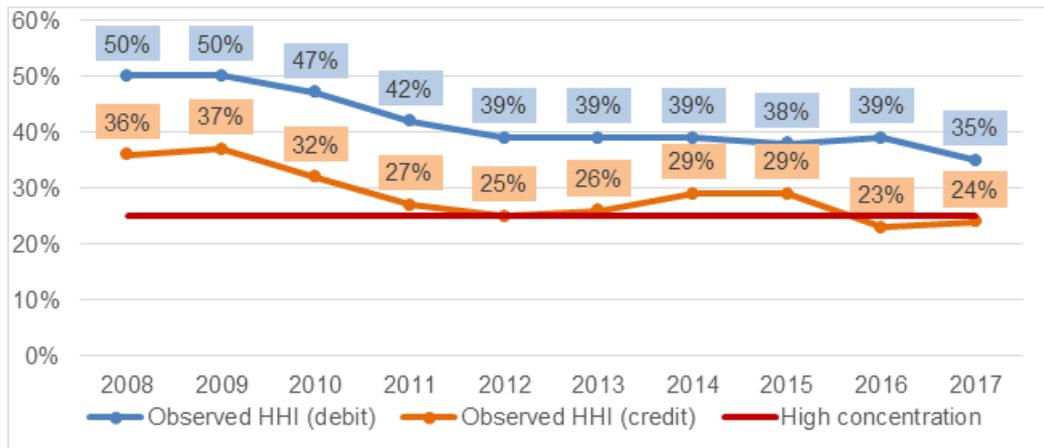
9. Before 2010, there was a duopoly on the acquirer side. Visanet (Cielo) and Redecard (Rede) dominated the market and hold exclusionary agreements with the card brands Visa and Mastercard, respectively. There was no interoperability between the network service provider, entailing higher prices and entry barriers. In response to this scenario, CADE opened the Administrative Process no. 08012.005328/2009-31 to investigate exclusionary practices between Visa and Visanet. As a result, there were two “Cease and Desist Agreements” that prohibited the existing exclusionary agreement between incumbents, ensuring that other companies could engage in Visa and Visanet (Cielo) systems.

⁴ Discriminatory treatment, refusal to contract, tie-in sale and cartels.

⁵ This type of contract was not restricted to the acquirer and card brand sides. CADE also analyzed cases involving agreements established between issuers and card brands, issuers and vouchers, acquirers and payment gateways, and grocery stores and card brands.

10. In light of this, it appears CADE's intervention of prohibiting exclusionary practices opened the market, increasing the possibility of market entry, which was very limited due to card brands' exclusive access to incumbent acquirers. For example, analysing the market share of acquirers in debit and credit transactions, since 2009 there has been a decrease on the HHI, which reached 0.35 and 0.24 in 2017 in debit and credit transactions, respectively.

Figure 3. The HHI of acquirers – Debit and Credit (2008 – 2017)



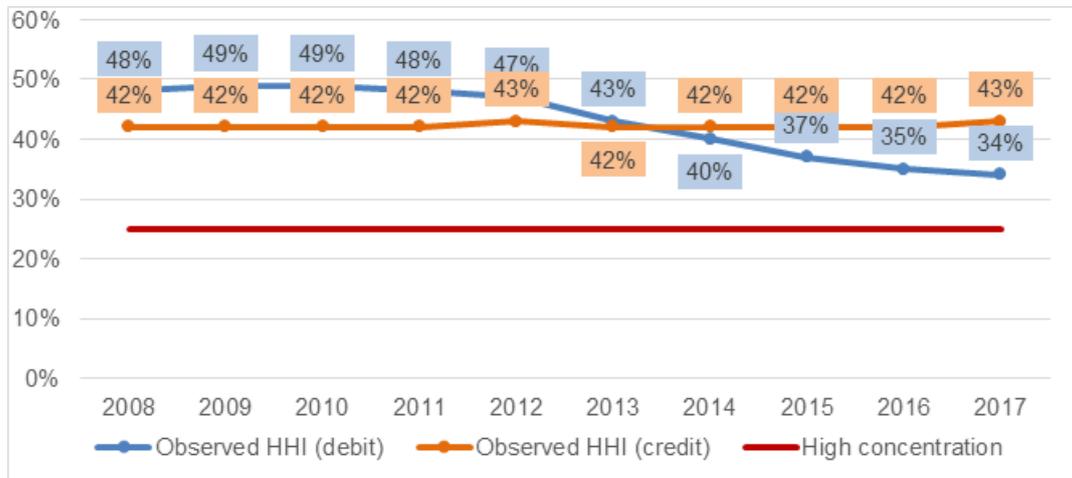
*The red line indicates the value of HHI (0.25). Markets with an HHI higher than 0.25 are classified as highly concentrated markets⁶.

Source: Central Bank of Brazil - Prepared by the Department of Economic Studies (DEE)

11. This trend is observed in the card brands market as well. The HHI decreased from 0,48 in 2008 to 0.34 in 2017 in debit transactions. In credit transactions, the HHI remained at 0.43 in the same period.

⁶ CADE, *Guia Análise de Atos de Concentração Horizontal*, Brasília, 2016. Available at: <http://cdn.cade.gov.br/Portal/centrais-de-conteudo/publicacoes/guias-do-cade/guia-para-analise-de-atos-de-concentracao-horizontal.pdf> >.

Figure 4. The HHI of card brands – Debit and Credit (2008 – 2017)

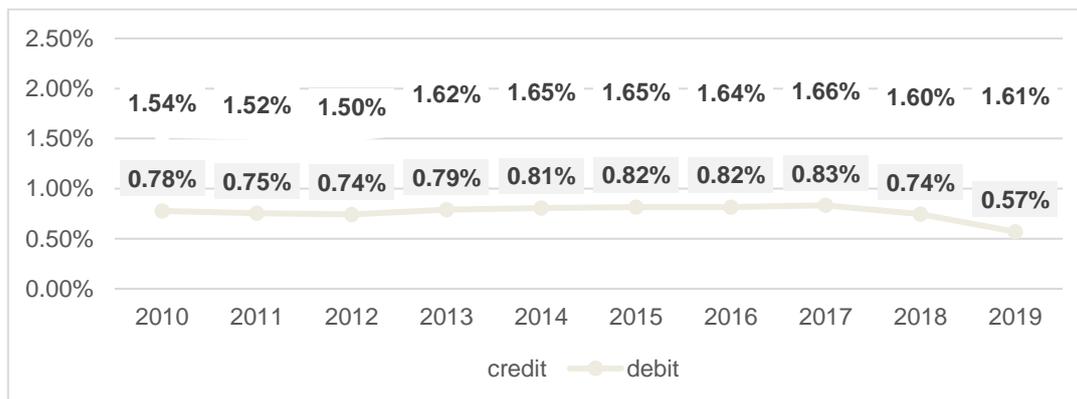


*The red line indicates the value of HHI (0.25). Markets with an HHI higher than 0.25 are classified as highly concentrated markets.

Source: Central Bank of Brazil - Prepared by the Department of Economic Studies (DEE)

12. In addition to the breakage of the Visa and Visanet exclusive agreement, it is worth mentioning that the Central Bank of Brazil (Bacen) also played an important role in reducing transaction costs in this industry. In 2018, the monetary authority established a cap on interchange fees charged on debit card transactions. A recent study published by Bacen⁷ shows that the introduction of maximum limits for interchange fees not only reduced costs, but also provided greater transparency in the pricing dynamics of this market. Figure 4 indicates that, between 2018 and 2019, the average interchange fees for debit transactions has presented a considerable drop.

Figure 5. Average interchange fees – Debit and Credit (2010 – 2019)



Source: Central Bank of Brazil Prepared by the Department of Economic Studies (DEE)

⁷ Available on: <[<Avaliação do resultado regulatório da introdução de limites para a tarifa de intercâmbio de cartão de débito \(bcb.gov.br\)>](http://avaliacao.do.resultado.regulatorio.da.introducao.de.limites.para.a.tarifa.de.intercambio.de.cartao.de.debito.(bcb.gov.br))>.

13. Many other competition concerns have already been identified by CADE in the payment card industry and additional measures had to be taken to ensure the maintenance of its competitive dynamics. The interventions mentioned herein are only a fraction of the main measures adopted so far by the Brazilian antitrust authority and other institutions thus far. Recently, CADE published a document in which it presents all the jurisprudence related to the authority's experience in this industry - between 1995 and 2019⁸.

14. Among other issues, the different sides of this industry continue to show a high concentration ratio associated with vertically integrated players. This combination still benefits incumbent companies since they have more resources to invest in innovation and advertising. Additionally, as mentioned before, as technological progress takes place, tools for analysing these markets are becoming outdated.

4. Final remarks

15. The complexity of the payment card industry poses many challenges to the Brazilian antitrust authority. As pointed out, three main elements impose competition concerns.

16. Given the complexity of this multi-sided system, new tools are needed to better understand their functioning and their competitive dynamics. Unlike in traditional markets, the structure of this industry entails network externalities that directly affect the incentives of consumers to continue using a payment platform. As such, pricing strategy is complex and demands new tools to assess its effects on competition.

17. The high concentration ratio of this industry, combined with vertically integrated players, benefits incumbent companies, since they have more resources to invest in innovation and advertising. For instance, the biggest banks in Brazil have turned into vertically integrated conglomerates, controlling large portions of each chain of this industry. In face of these challenges, the Brazilian antitrust authority, the Central Bank of Brazil (Bacen), and the Secretariat for Competition Advocacy and Competitiveness (SEAE) had to join efforts.

18. In 2010, CADE prohibited the existing exclusionary practices. At about the same time, Bacen, SEAE and the former Secretariat of Economic Law (SDE) published a report about the payment card industry, which identified exclusionary agreements between acquirers and card brands as one of the main problems of the market. Along the same lines, and as per Law 12865/13, Bacen started requiring card brands to disclose their rules, which increased transparency and promoted the entry of new players into the market.

19. Moreover, in 2018, Bacen and CADE signed a Joint Normative Act no. 1 (ANC no. 1), aimed at enhancing the efficiency of both institutions in the analysis of mergers and antitrust practices involving financial institutions.

20. The joint efforts of the institutions – the Bacen's regulation, the Cease and Desist Agreements established by CADE and SEAE's advocacy actions – have contributed to a reduction of entry barriers and the emergence of new entrants, resulting in competitive pressure on incumbent players and the improvement of competition in the payment card industry.

⁸ *Mercado de instrumentos de pagamento*, Cadernos do Cade, Brasília, 2019. Available at: <<https://cdn.cade.gov.br/Portal/centrais-de-conteudo/publicacoes/estudos-economicos/cadernos-do-cade/mercado-de-instrumentos-de-pagamento-2019.pdf>>.

21. It is also worth highlighting the role innovation plays in improving competition by reducing costs and increasing the efficiency. For instance, the digitalization of financial services has made mobile banking the preferred channel for financial services in Brazil. As Over time, traditional services provided by incumbent banks proved to be much more expensive than digital options.

22. This new environment was especially beneficial for the payment and the loan markets, since FinTechs have found opportunities to grow in Brazil. Nowadays, these companies are becoming more and more appealing to consumers who look for transparency and customized services. Some FinTechs that have recently been in the spotlight are Nubank, Next, Original, GuiaBolso, Stone, Inter, PagSeguro and BeeTech.

23. Finally, along with PIX, the new instant payment system, the Central Bank of Brazil (Bacen) recently introduced the so-called open banking, that tends to encourage the growth of new fintechs, reducing costs, increasing transparency, and improving competition.