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# Keys to success in Japan's crowded payment app market

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## Executive Summary



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*Japan's payment services market is crowded with mobile payment apps that use QR codes or barcodes as inputs. The companies that have released such apps are spread across various sectors. They are providing payment services by combining point-of-sale (POS) payment technologies with settlement channels. Competition to capture users with generous point rewards is underway. The players best able to find ways to attract users and merchants should emerge as winners.*

## Payment apps abound

“Cashless” is a new buzzword in Japan. The current interest in cashless payments partly reflects that the government is planning to soften the blow from an October 2019 consumption tax hike by issuing tax rebates in the form of reward points on cashless purchases. Various companies are announcing and launching new cashless payment services, apparently to coincide with the rebate program. Many such services are smartphone apps that enable their users to make payments by scanning QR codes or barcodes (collectively referred to below as “QR/barcodes”). Most of them have a name that ends with “pay.”

Despite being similarly named, the new payment apps are not all the same. How they differ is a source of confusion for some. I attempt to clear up such confusion below.

## Payment app taxonomy

### (1) Classification by payment service provider

A plethora of payment apps has hit the market over the past few years. They include apps released by banks and credit card issuers (e.g., Ginko Pay, J-Coin Pay, Smart Code, Bank Pay)<sup>1)</sup>, telecom carriers (e.g., d Pay, PayPay, au Pay), Internet companies (e.g. Line Pay, Rakuten Pay, Amazon Pay, Merpay), FinTech startups (e.g., Origami Pay, Pring, Atone QR, Quo Pay) and even retailers (e.g., 7pay, FamiPay).

For the purposes of this discussion, I am disregarding non-QR/barcode-based

#### NOTE

1) Ginko Pay is owned by Bank of Yokohama, Bank of Fukuoka, Japan Post Bank et al.; J-Coin Pay, by Mizuho Bank et al.; Bank Pay, by MUFG Bank, Sumitomo Mitsui Banking Corporation, Mizuho Bank et al. Smart Code is owned by JCB et al.

payment apps like Apple Pay and Google Pay (both of which use contactless IC chips) and POS payment services for merchants like AirPAY.

### **(2) Classification by POS payment technology**

QR/barcode-enabled payments are broadly classified as either CPM (consumer-presented mode) or MPM (merchant-presented mode) payments. Payments Japan, which is working on standardizing QR codes while educating the public on cashless payments, classifies payments into four categories: CPM (barcode), CPM (QR code), MPM (static) and MPM (dynamic). Some payment services can accommodate more than one of the above categories of payments and even contactless-IC and plastic card payments.

### **(3) Classification by settlement method**

In addition to the various POS payment modalities, there are also a number of ways in which payments are settled between consumers and payment service providers. The three major ones are (1) prepaid, (2) direct withdrawal from a bank account at the POS and (3) postpaid, each of which has multiple variations.

Means of prepaid settlement include prepaid cards, remittance services and bank prepayments. Prepaid cards are regulated by the Payment Service Act as a prepaid payment modality. They offer a great deal of freedom in terms of how money can be loaded onto their prepaid cards, but cash refunds for prepaid card purchases are prohibited. Payment service providers are required to deposit 50% of prepaid card balances into a custodial account. Remittance services are regulated by the Payment Services Act as funds transfers. The remittances are generally funded in cash or charged against a bank account. They can be refunded in cash or to the account from which they originated. Remittance service providers are required to maintain cash balances sufficient to fully cover all unsettled charges. Bank prepayment services are funds transfers provided directly by banks pursuant to the Banking Act.

Payments withdrawn directly from bank accounts at the POS are similar to debit card purchases debited directly against the cardholder's bank account. Such payment services may be provided directly by banks or by electronic payment service providers.

Postpaid payment services include credit cards with periodic billing cycles, postpaid mobile phone or Internet plans and retail charge accounts payable in full

monthly.

Some payment services are compatible with more than one of the above settlement channels and multiple use cases. The ways in which payment modalities can be combined with settlement channels are complex.

### Keys to success

We will likely see a major trend toward services that offer multiple payment modalities and have multiple settlement channels. A lot of attention is focused on QR-code-based payment modalities because, if they are CPM, they use customers' smartphones, obviating the need for issuance of a card or other physical medium. CPM payment technologies that use barcodes tend to be especially easy for merchants to adopt because they generally are compatible with POS registers' existing barcode readers. MPM (static) payments likewise do not require merchants to install new payment terminals. Their compatibility with various technologies allows merchants to use their existing contactless IC or credit card terminals.

For settlement as well, we will likely see a trend toward payment services giving customers a choice of using any settlement channel they like. Payment services will have to accommodate the customer's individual money-management preference, whether it be prepaid, credit or bank-account debit.

However, such multiplicity of payment modalities and settlement channels will increase apps' complexity and complicate registration processes, possibly causing confusion for first-time users. With payment app providers constantly endeavoring to improve their user interfaces, UX will likely become a key axis of competition.

Additionally, the payment modalities that payment services offer will differ depending on the provider's service, strategy and customer base. Most providers already have core businesses other than payment services and plenty of customers. Many of them have recently been working on expanding their business domains by not only providing payment services with which to purchase their own merchandise or services but also broadly popularizing their payment services externally. In response, payment app providers without a large customer base and regional banks with small geographic footprints will likely expand their scale by partnering with each other.

In any event, payment services are a business in which expansion hinges on growth in both usership and merchant network. In Japan, where the cashless share of payments is still low, competition to gain users and sign up merchants will continue for a while. A battle to woo users with cash-back and point rewards is already underway. Amid such competition, the extent to which payment apps can capture loyal users and grow their merchant networks will separate the winners from the losers. The big question is how effectively the payment service providers can market their apps before reaching their presumptive ultimate objective of applying payment data to their core businesses.

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