UK MOBILE PAYMENTS 2014

A Market Stymied, Despite Potential

JUNE 2014

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EXECUTIVE SUMMARY

Mobile payments promise to revolutionize UK commerce. The UK is a sophisticated and enthusiastic consumer technology market, with smartphone adoption and mobile commerce activity both growing fast and surging ahead of other European territories.

This would appear to have created the platform for consumers and retailers to embrace proximity payment via their beloved handsets. But the UK is also a curious anomaly. Piecemeal technology adoption by both consumers and retailers has created a fragmented ecosystem, in which use of these mechanisms ranks far behind that of other mobile services—at just 2.2 million mobile payment users forecast for 2014, according to Yankee Group—and behind other countries.

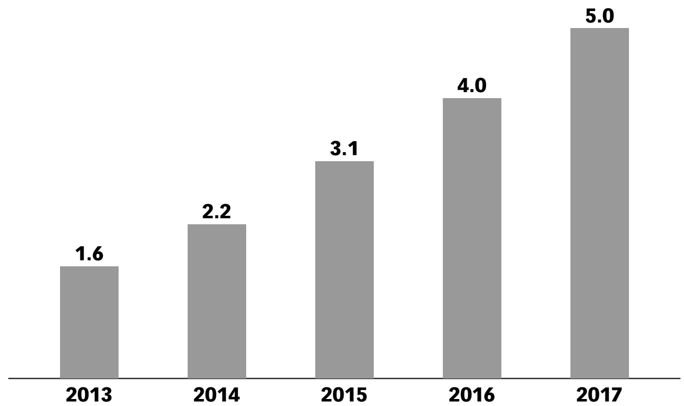
Several retailers in the UK are offering their customers their own mobile payment opportunities, likely reaping greater value from gaining a direct customer marketing relationship than from actual mobile channel sales. But eMarketer believes that new technology initiatives by banks will lay the groundwork for what will be larger-scale adoption.

This report provides an overview of the size and character of the proximity payments market in the UK, and the factors and inhibitors behind its development. It explores emerging new payment technologies and how marketers may alter the opportunity. Finally, it examines how this evolution may change the game for retailers.

KEY QUESTIONS

- **How popular are mobile payments in the UK, and why?**
- **What are the key market opportunities for those in the industry?**
- **What technologies will change the mobile payments landscape?**
- **How should UK marketers best respond to the changing landscape?**

UK Mobile P2P Payment Users, 2013-2017
millions



Source: Yankee Group, "Mobile Marketing and Commerce Forecast," Sep 2013 as cited in company blog, Oct 11, 2013

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THE CURRENT STATE: A STUTTERING START

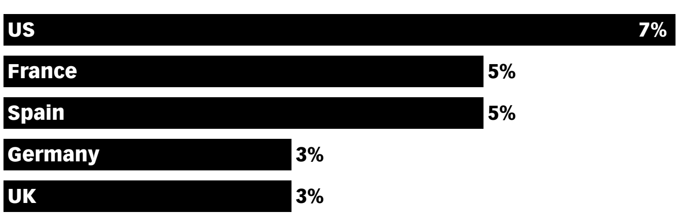
Mobile payments are a multibillion-dollar opportunity still in the early stages of implementation. UK consumers are enthusiastic online shoppers and smartphone users, but infrastructure required for mobile payments to gain equally broad adoption is still being laid. Inertia and competing efforts have allowed several variants and interpretations of mobile payment to emerge.

eMarketer defines mobile payments as transactions for goods or services initiated with a mobile phone at the point of sale (POS). Often characterized as "proximity" or "contactless payments," mobile payments occur in real time in the real world: for example, purchasing a cup of coffee at a local cafe. Mobile commerce is a broader term, encompassing the purchase of digital or physical goods on a mobile device.

Despite the buzz and potential of in-store mobile payments, the reality in the UK is that very few customers are engaged in it. Only 3% of UK internet users said they used their phones to buy goods in-store in 2013, according to a report from Bain & Company. UK adoption is running at around half the rate seen in comparable leading digital nations, compared with 7% in the US, 5% in France and Spain, and on par with Germany at 3%.

Internet Users in the US and Select Countries in Western Europe Who Use Their Mobile Phone to Pay for Products/Services*, 2013

% of respondents in each group



*Note: n=1,688; *either purchase goods in a store or pay for public transportation/taxis*
Source: Bain & Company, "Mobile payments: Finally ready to take off?" Feb 5, 2014

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A TWO-TRACK MOBILE MARKET

At the heart of this small-scale adoption is a contradiction.

Beside payments, the UK is enthusiastically adopting mobile devices and services. eMarketer estimates that the majority of the population (53.7%) will own a smartphone in 2014.

Mobile commerce activity is booming. Mobile's share of UK retail website visits rose from 24.0% to 45.0% between Q4 2012 and Q4 2013, according to the "Quarterly Benchmarking Index" from the Interactive Media in Retail Group (IMRG) and Capgemini. Retail sales from mobile shopping more than doubled in 2013 to total £8.55 billion ($13.36 billion), eMarketer estimates, representing 18% of all retail ecommerce sales. The UK is ahead of the European pack in this regard.

However, in-store smartphone payments haven't followed the same path as other mcommerce activities.

For one thing, much mobile activity is conducted not in stores but in the household. Purchases via tablet devices, typically used at home, make up the majority of UK mcommerce retail sales—60.5% or £5.17 billion ($8.08 billion) in 2013, compared with just 38.0% or £3.25 billion ($5.09 billion) from smartphones. In short, consumers are using their phones to make purchases, but not necessarily in stores.

UK Retail Mcommerce Sales, by Device, 2012-2018

billions of £, % change and % of retail mcommerce sales

	2012	2013	2014	2015	2016	2017	2018
Tablet	**£1.72**	**£5.17**	**£9.28**	**£12.44**	**£15.47**	**£18.39**	**£20.96**
—% change	356.0%	201.6%	79.3%	34.1%	24.4%	18.9%	14.0%
—% of retail mcommerce sales	44.6%	60.5%	65.8%	68.0%	70.1%	72.2%	72.2%
Smartphone	**£2.04**	**£3.25**	**£4.65**	**£5.67**	**£6.40**	**£6.88**	**£7.84**
—% change	123.1%	59.4%	43.2%	21.9%	12.9%	7.5%	14.0%
—% of retail mcommerce sales	53.0%	38.0%	33.0%	31.0%	29.0%	27.0%	27.0%
Other mobile devices	**£0.09**	**£0.13**	**£0.17**	**£0.18**	**£0.20**	**£0.20**	**£0.23**
—% change	71.8%	38.9%	31.9%	8.1%	8.6%	2.6%	14.0%
—% of retail mcommerce sales	2.4%	1.5%	1.2%	1.0%	0.9%	0.8%	0.8%
Total	**£3.85**	**£8.55**	**£14.10**	**£18.29**	**£22.07**	**£25.47**	**£29.04**
—% change	186.3%	122.3%	64.8%	29.7%	20.6%	15.4%	14.0%

Note: includes products or services ordered using the internet via mobile devices, regardless of the method of payment or fulfillment; excludes travel and event ticket sales; numbers may not add up to total due to rounding
Source: eMarketer, June 2014

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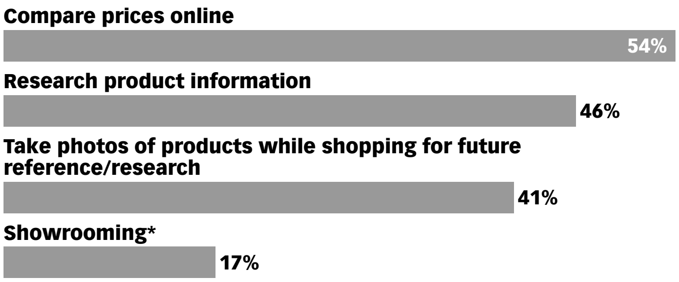
This is not to suggest mobile phones aren't being used at all in retail locations. Some 55% of UK smartphone users said they use their phones in stores, according to a Q4 2013 survey by OnePoll for Cheil Worldwide. But most of them reported using the devices to compare prices (54%), research products (46%) or take photographs (41%). Actual transactions did not figure in the list of top in-store activities carried out by mobile phone. For digital shoppers at physical stores, purchase is peripheral.

In-Store Smartphone Activities Conducted by UK Smartphone Owners, Q4 2013

% of respondents



*Note: ages 18+; 55% of UK smartphone owners use their phones while in-store; *using their phone or tablet to find a better price on a competitor's website and buying there instead*
Source: Cheil Worldwide, "Agile Consumer 2013" conducted by OnePoll, Feb 11, 2014

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While few consumers actually use in-store mobile payments, a significant minority interested in using that type of transaction exceeds actual instances of them doing so. In a March 2014 report by Bain & Company, 22% of UK consumers said they were willing to try, while Lightspeed Research found that 17.9% of UK internet users polled in October 2013 said they would like to use a mobile phone instead of bank cards to pay for goods or services in a shop.

Mobile Phone Features that UK Internet Users Would Like to Have, by Age, Oct 2013

% of respondents in each group

	18-24	25-34	35-44	45-54	55+	Total
Use mobile phone as a satellite navigation system	45.4%	43.5%	39.6%	30.0%	24.9%	34.3%
Use mobile phone to locate your friends/family/children in real time	34.5%	28.2%	26.8%	21.5%	16.0%	23.3%
Use mobile phone as an electronic 'ticket' for public transport (e.g., Oyster card)	37.5%	21.7%	19.1%	16.2%	9.6%	18.0%
Use mobile phone to pay for goods and services in a shop (e.g., scanning your mobile rather than using a credit or debit card)	27.3%	21.9%	20.9%	17.1%	11.3%	17.9%
Use mobile phone as a passport/identity document for traveling	23.3%	19.5%	19.2%	18.8%	13.8%	17.8%
Use mobile phone as an electronic key for your house or car	19.0%	14.0%	13.7%	13.2%	11.6%	13.6%
Wear mobile phone technology, for example in the form of a watch or pair of glasses	14.1%	10.7%	10.9%	8.3%	5.2%	8.8%
None of the above	26.5%	36.2%	40.9%	51.2%	60.1%	46.7%

Source: Lightspeed Research as cited by Kantar, Oct 16, 2013

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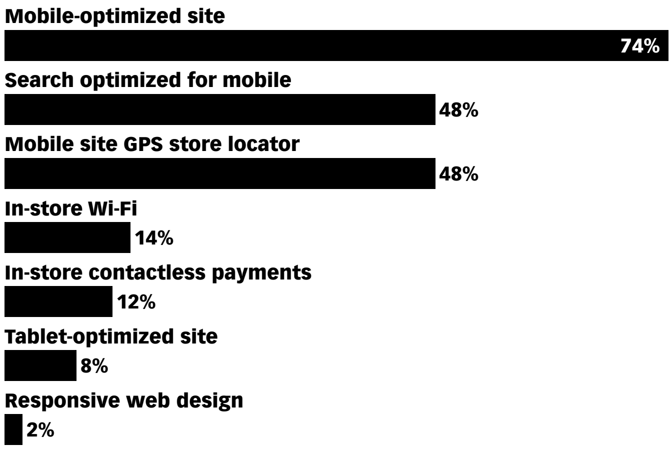
While proximity payments are not the most sought-after mobile phone feature, a sufficient enough spark of interest exists in the UK—especially among younger consumers—to ignite solid growth.

What's holding up wider adoption? There are a variety of factors on both the buy side (consumers) and the sell side (retailers).

Retailers have been slow to support the opportunity. With only 12% of the top 50 retailers offering customers in-store contactless mobile payment facilities, according to a June 2013 survey from the Internet Advertising Bureau UK (IAB UK), there is insufficient infrastructure in place affording consumers the ability to use this channel.

Mobile Optimization Features Utilized by UK Retailers, June 2013
% of respondents



Source: Internet Advertising Bureau UK (IAB UK), "Mobile Retail Audit 2013" as cited in press release, July 22, 2013
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In fact, more retailers offer in-store Wi-Fi than they do mobile payments, meaning they are doing more to support consumers browsing rival websites for cheaper prices than they are to take their actual payments while on the premises. A 2013 survey from mobile payment technology vendor MPayMe found just 7.5% of merchants on London's Oxford Street—Europe's longest and busiest shopping precinct—were able to accept mobile payments.

One reason for retailers' reluctance is the cost associated with the technology required to take payments, such as near field communication (NFC), which has been seen as perhaps the most likely platform for widespread mobile payments.

The cost of installing NFC-capable POS terminals may have put off small- and medium-sized retailers in particular, who are just recovering from the UK's economic downturn and have already faced the need to support the emergence of enhanced contactless debit cards.

Larger merchants might have led the way with NFC, but they were likely unimpressed by early tests from Transport for London (TfL), which operates the city's mass transit system. TfL has had success with contactless payments via its prepaid Oyster cards and initially planned to upgrade terminals to support payments from NFC-enabled phones in 2012. But it abandoned the smartphone support after trials found the technology too slow to process the required volume of transactions. (However, TfL hopes to resume new tests of mobile payments.)

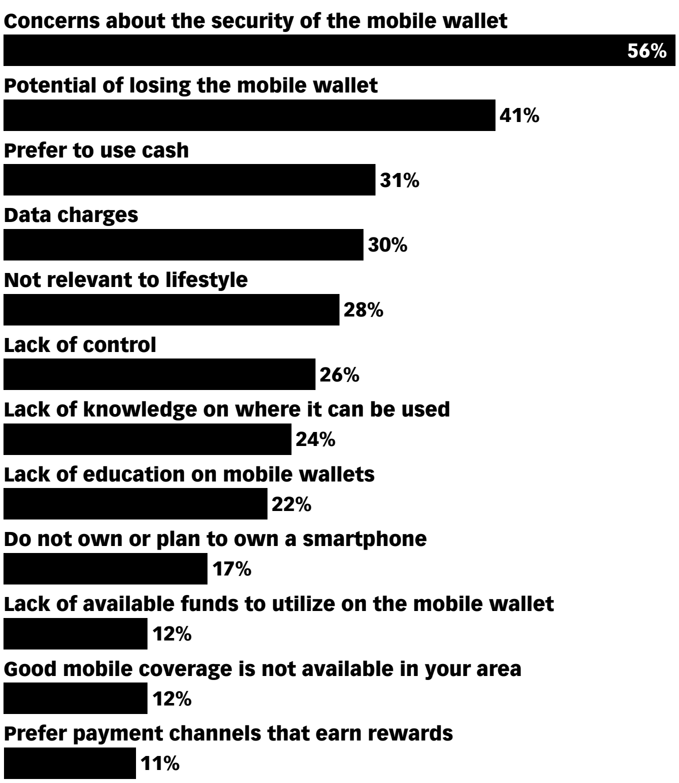
Piecemeal adoption by handset manufacturers has not helped NFC's fortunes, either. With Apple having so far rejected the technology for its popular iPhone, NFC remains principally an Android technology. The recent surge in sales of Samsung Android devices in particular may have placed compatible devices in the hands of many more UK customers. But so far, there is little evidence to suggest consumers are using them, among the array of other Android features, to their fullest extent.

For consumers, security concerns are a key factor holding up widespread adoption of mobile payments. Across three surveys by market research firms, security comes out as the top adoption barrier for mobile payments, with 52% (Ovum) to 65% (Mintel) believing the technology to be insecure.

History suggests security concerns can be overcome if providers can offer persuasive evidence of significant value or convenience.

Today, however, many UK consumers regard mobile payments as less, not more, convenient than current payment methods. The idea that losing their phone will leave them unable to pay is internet users' No. 2 sticking point, according to a Q3 2013 survey by Auriemma Consulting Group, even though this problem and the steps to its resolution are the same as those for losing regular bank cards.

Barriers to Mobile Wallet Usage According to UK Internet Users, Q3 2013
% of respondents



Note: n=1,000
Source: Auriemma Consulting Group, "The Mobile Payments Report," Oct 2013
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Mobile payment vendors must also overcome UK customers' belief that existing methods are "good enough." These include wireless payments in the form of a card, such as TfL's Oyster card. According to eDigitalResearch's "Contactless Payment Index" released in May 2014, the majority of Britain's consumers (55%) own a contactless card, while 38% actively use them.

The emergence of these relatively sophisticated improvements to familiar cards may block the way for phone-based mobile payments.

However, this could be overcome if mobile payment operators provided real incentives for consumers to adopt their technologies. Providers will need to offer users more value or convenience than current payment methods. Short of that, the market will remain stuck in its current chicken-and-egg conundrum—with merchants not seeing sufficient consumer adoption of a single technology to commit to support, meaning consumers have little reason to become mobile payers.

THE MARKET TODAY

Lack of standardized, scaled technology adoption from both customers and merchants in the UK has created a vacant space in which hopeful vendors across the spectrum have attempted to bring to market their own versions of a mobile payment platform. The UK has undergone a veritable Cambrian explosion in the number of mobile payment solutions on offer—and the result is a fragmented patchwork.

Food retailers have been among the keenest to jump in. KFC, Pizza Express, Wahaca, Greggs and others have launched apps featuring an ability to pay in-store for their chicken, pizzas, burritos and pastries. Their methods for doing so—variously involving "checking in" while in range of a store, crediting customer accounts upfront from a bank account, paying direct via in-app PayPal or bank transfer and presenting a phone bearing a QR code for scanning at POS—do not necessarily make paying any more efficient or frictionless than the time-honored practice of presenting some cash or a bank card.

Indeed, the multiplicity of options available means, unlike with established transaction methods, consumers who shop at multiple retailers face a different user experience every time. Retailers are making up for this fact by offering consumers additional value, including faster in-store collection, receipt history storage, free coffee after every seventh transaction, loyalty points management and other rewards.

The most significant new value being derived by retailers may not be sales from actual in-store payment at all, but rather from the ability to establish direct relationships with customers, gathering data about them and driving repeat visits.

For many mid-tier retailers that have witnessed the learnings that supermarket Tesco gleaned through its well-regarded, data-collecting Clubcard scheme, mobile apps are an opportunity to get to know their customers—mobile payment apps are not just for payment; they are also extensions of the traditional loyalty card. The absence of a standardized mobile payment ecosystem is a golden moment for marketers to define these relationships on their own terms.

A host of digital startups have also attempted to bring underlying mechanisms to market—but have not found a broad market yet.

Droplet, for instance, offers paying customers rewards, but operates only in London and Birmingham and requires pre-filling with cash credit, thereby introducing complexity. Yoyo lets retailers segment and target customers with these offers, but has focused mostly on the university student market and sees itself more as a marketing platform. Flypay's system allows customers to scan a receipt and pay via their handset, but so far has been adopted by just one restaurant chain.

Even large-scale efforts by major companies and consortiums haven't managed to gain significant reach. O2 Wallet, launched in 2012, allowed users to link up to three accounts and send and receive money but required being loaded up with money before spending. It incurred fees on transactions and was eventually shuttered in March 2014. In its wake, Orange QuickTap and (following Orange UK's folding in to EE) EE Cash on Tap fly the flag for operator mobile payment initiatives. But these NFC-based systems are useable by owners of just nine new Android handsets, severely limiting adoption.

Similarly, Weve, launched in 2013 as a joint venture of three of the UK's four main mobile networks, has not had a major impact. The app supports transactions through a mobile wallet that links to customers' debit cards. While Weve bills itself as a mobile commerce platform, it appears geared far more toward advancing marketing engagement initiatives with unique qualities that telcos bring—personalized, location-aware campaigns for individual customers, principally delivered via messaging. Weve, then, could be a powerful partner for brands keen to develop loyalty relationships.

One of the best-placed platform solutions for widespread adoption may not rely on telco leverage nor hardware standards at all. PayPal, which has more than 18 million active accounts in the UK, can facilitate proximity payments at over 2,000 UK stores and restaurants.

In March 2014, PayPal established relationships with UK restaurants Prezzo, Wagamama and Gourmet Burger Kitchen, allowing customers to order ahead and, after "checking in" while at the location, to pay at their tables using menus and "check-out" facilities integrated not to the retailers' apps but to PayPal's own.

PayPal's relative breadth suggests it stands a better chance than most hopeful vendors at facilitating in-store payments en masse. By integrating retailer-specific info in its own app, PayPal could drive many customers through its gate.

The company has since announced PayPal Beacon, a Bluetooth low energy (BLE) system that will automate the check-in step. But users will need to be comfortable with location-based transactions if PayPal's more advanced ambitions are to succeed.

Likewise, Apple's own equivalent technology, iBeacon, is positioned to support automatic POS payments when customers are within range of a merchant's BLE transmitter. However, the UK's first trial deployments in May 2014 have focused less on transactions and more on delivering location-based notifications of product —in other words, not on sales but on marketing.

In this sense, iBeacon is particularly useful in large-scale retail environments. Virgin Atlantic is currently using it at Heathrow Airport to display iPhone users' boarding passes, duty-free offers or drink recommendations, depending on their location on the premises, while supermarket Waitrose is alerting in-store customers to offers as they walk corresponding aisles. All payment is carried out via regular means—indeed, iPhone's iTunes Store doesn't support digital payment for physical goods.

THE MARKET TOMORROW

None of the technologies in market today have created the conditions for a mobile payments ecosystem to match the convenience of cash and bank cards at scale. But the rush of competing attempts will, from 2014, undergo an evolutionary shake-out that will sow the seeds for large-scale payments standards, address consumer concerns and, finally, begin to popularize mobile payments in the region.

This year looks to be the tipping point, when UK retailers implement underlying in-store mobile payment technologies with greater gusto. In a Conlumino survey for TLT Solicitors of leaders from 60 multichannel retailers representing 71% of UK retail sales, 37.5% said they planned to install the technology. The survey concluded: "The greatest enthusiasm (of any retail technology) is for the value of mobile payments. Half of retailers believe mobile payment technologies offer the best prospect for growth in 2014. The only firm confidence seems to be in mobile payment methods."

One reason for this enthusiasm may be greater confidence in the emerging capabilities of NFC technology. By storing customer financial data in the cloud—invoked by a payment app, rather than on a handset chip—Host Card Emulation (HCE) could begin to allay consumers' concerns around security and phone loss. While HCE is only supported in the latest 4.4 version of Android and still leaves Apple iPhone users out in the cold, this smoothing out of NFC's edges nevertheless gives retailers greater confidence to invest in this standard for the future.

Meanwhile, eDigitalResearch found that 59% of smartphone owners who had not tried mobile contactless payments said they intended to do so in the future.

But the biggest factor driving improving prospects for UK mobile payments is the awakening of banks. Amid the rush by individual retailers and startups to provide their own plumbing in the absence of scaled underlying infrastructure, banks have been largely absent. While retailer payment apps and third-party gateways alike may pass consumers' money to merchants, this money is typically sourced from customers' own banks.

This year, bank groups will reclaim their role in the payment channel by teaming to launch their own mobile payment systems in competition with other operators.

Launched in April 2014 by The Payments Council and run by leading banks, Paym is designed as a person-to-person payment system, allowing registered users to pay one another by sending funds not to a bank account number and sort code, but to a mobile phone number from a mobile banking app. Using a phone number as a proxy for a bank account in this way is an extension of Barclays' own Pingit app, launched in 2012 and initially only supporting Barclays-to-Barclays transfers. Paym, however, launched with interoperability among nine banks supporting a potential 30 million consumers. Expansion plans are in place to include seven more banks, allowing 90% of current UK account holders to opt in by late 2014.

While Paym is intended for use by individuals and for individuals to pay small traders, an initiative from a parallel consortium of 18 banks will enable mass mobile transactions with retailers. VocaLink, the group which powers the technologies underpinning ATMs and bank payment systems including Bankers' Automated Clear Services (BACS) and Faster Payments, plans a fall 2014 launch of Zapp, a system for completing direct, bank-funded digital transactions with retailers made online or in stores. Zapp's backing is considerable: VocaLink processed over 10 billion transactions in 2013. By offering its solution to merchants, it aims to offer checkout processing in competition with PayPal, but funded in one step—direct from consumers' bank themselves.

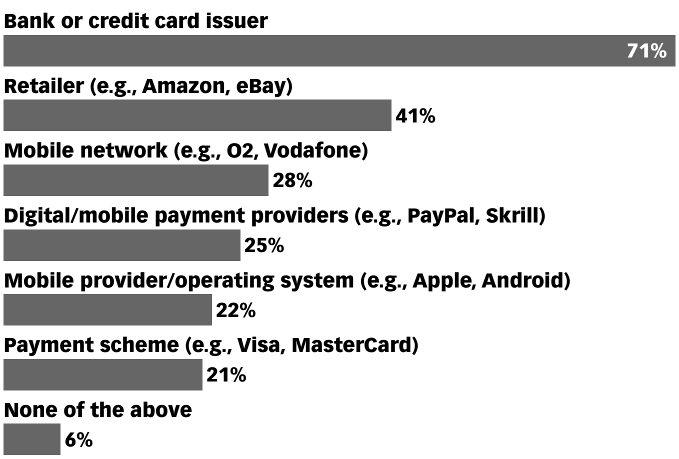
eMarketer believes these initiatives will help kick-start mobile payments more than any other efforts to date. So far, many would-be vendors have framed the mobile payments opportunity as one that will disintermediate banks from the transaction chain. But in the UK, banks will play a bigger, not smaller, role.

Banks in the region are well-used and have a vital practical role in the value chain, not least as the primary safe store of consumers' capital. This relationship will extend to mobile payments. Banks are among the least-trusted business sector in the UK, according to the Edelman Trust Barometer 2014, reflecting lingering consumer anger over the financial crisis. However, with 93% of UK households operating a current account, beside other account types (according to the UK government's Department for Work & Pensions), consumers retain a strong affinity with banks.

Accordingly, it is banks which consumers favor to provide their mobile payment services. In Ovum's survey, some 32% of UK consumers rated banks as their most-trusted mobile payments provider candidate. That parallels Auriemma data from Q3 2013, which showed that banks are overwhelmingly internet users' mobile wallet provider of choice—far ahead of either retailers with their existing apps or intermediaries like even PayPal with its significant scale.

Mobile Wallet Providers that UK Internet Users Would Be Interested in Using, Q3 2013

% of respondents



Note: n=412 who are interested in obtaining and using a mobile wallet
Source: Auriemma Consulting Group, "The Mobile Payments Report," Oct 2013

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They may have security concerns around mobile payments, but UK consumers trust banks with their money more than other vendors. Despite their relative lateness to market vs. in-market rivals, this places Paym and Zapp in a strong position to drive adoption.

The revolution under way in UK consumers' mobile money management will spur usage of mobile payment services introduced by the banks. Customers of the five biggest retail banks in the region downloaded those banks' mobile apps 12.4 million times in 2013, according to the British Bankers Association (BBA). This helped double the volume of transactions from within those apps as consumers welcomed the new convenience vs. branch visits and telephone banking. This increasing comfort with mobile money will condition consumers to try mobile payments when presented with opportunities that satisfy their requirements of security and convenience.

By simplifying the mobile payment process to require payment to a phone number (Paym) or via a one-click checkout button (Zapp), banks' standards will also address consumers' concerns that mobile payment is too complex.

eMarketer expects the foundations being laid by the "from your bank" propositions of Zapp and Paym will supply the impetus and authority required if mobile payments are to take off. The Payments Council's own forecast is bullish, expecting a billion Paym transactions to be made between launch and 2018.

For UK retailers, the emergence of a single, bank-backed standard may come as a relief. A dominant, dedicated vendor of payment services would absolve retailers of the need to invest in creating and managing their own payment apps. Additionally, the onboarding of what could be a large number of Zapp users would significantly grow the base of consumers with the ability to pay via mobile. All of this would allow retailers to focus on their core activities, while taking a greater proportion of sales via mobile.

However, the emergence of these platforms may be a curse as well as a blessing. A powerful platform would displace retailer-owned apps that seek to build customer relationships. If consumers decide to use widespread, bank-level payment options like Zapp in stores rather than retailers' own, this may negate brands' new-found ability to capture consumer data, promote goods and services, and offer incentives for repeat custom.

HOW THE GAME WILL CHANGE

While the prospects are growing for mobile payment uptake in the UK, brands should expect to work in an environment of evolution, not revolution.

With so much uncertainty over whether NFC can yet be endorsed as the mobile payment hardware standard of choice by support from Apple, establishment of underlying common software and network systems is a more productive use of energy for the time being.

No matter whether NFC, BLE or another hardware technology will win the day at the POS, the more interesting question may be which payment method is invoked on customers' handsets at the point of purchase—direct retailer transfers, bank-funded transactions, PayPal, iTunes Store or any other from a range of candidates. This will determine who the biggest winners and losers are in the next generation of retail payments.

This is where the UK's sensible "baby steps" are being trodden, without particular regard to hardware implementation commitments. Zapp will begin first by facilitating purchases for remote ecommerce merchants, only planning to facilitate in-store proximity payments via POS integration in 2015. Likewise, Paym has stated it will integrate with in-store QR and BLE technology only later on. The phase the UK is entering is to establish the payment services that will be used first online and next in-store, regardless of which in-store hardware implementations are settled on.

In this sense, Zapp will start by aiming to alleviate the problem of online shopping cart abandonment, which sees 21% of those smartphone owners who know how to make a mobile purchase back out of doing so due to the perceived complexity of completing a transaction on a handset, according to March 2014 polling from Rocket Communications for Oxygen8 Group.

Reasons Smartphone Users in Great Britain Have Abandoned* a Purchase on Their Smartphone, by Age, March 2014

% of respondents in each group

	18-24	25-34	35-44	45-54	55-64	65+	Total
Security concerns	25%	32%	25%	25%	23%	16%	25%
Difficult to do on a mobile phone	22%	27%	24%	18%	15%	14%	21%
Too many checkout steps before payment is made	13%	13%	12%	10%	13%	7%	12%
Lost/might lose internet connectivity	16%	16%	11%	9%	10%	5%	11%
Ad pop-up windows were off-putting	13%	16%	9%	7%	9%	3%	10%
Had registered payment details previously but forgot password	13%	11%	7%	10%	4%	3%	8%
None of these	14%	13%	19%	20%	24%	29%	19%
Have never abandoned a purchase on mobile phone	28%	23%	29%	35%	38%	46%	32%

*Note: among respondents who know how to make payments on their smartphone; *starting but not finishing a payment on a mobile phone or deciding to use another device to complete the payment*
Source: Oxygen8 Group, "Smartphone Survey" conducted by Rocket Communications, March 25, 2014

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Reducing this checkout friction by the addition of a "Pay by Zapp" button to merchants' websites or apps will place Zapp in competition with PayPal in the near term—but paying by Zapp at brick-and-mortar POS terminals will come later.

This iterative approach will mean the proximity payments opportunity will not suddenly explode. But consumers who become accustomed to using the Paym and Zapp brands in their initial manifestations over the next couple of years are more likely to do so when these standards are also enabled at the POS.

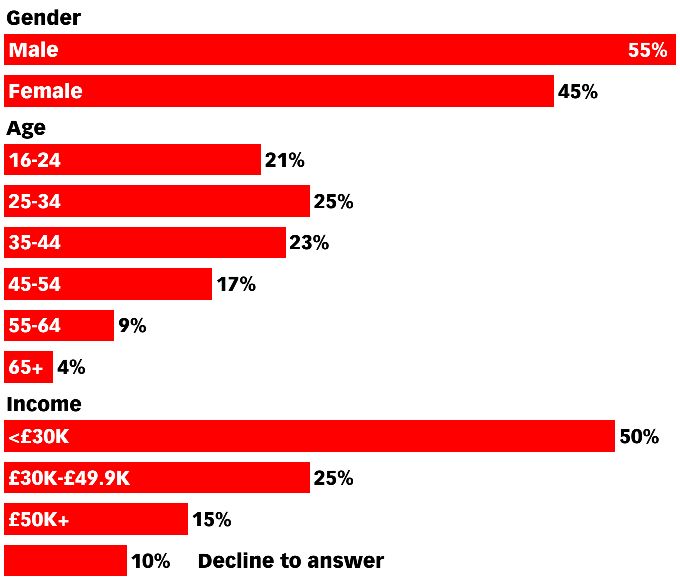
Furthermore, greater adoption of payment-enabled handsets by UK consumers will grow use of the features. Just under half of those with NFC-enabled handsets have used the feature, and 87% have done so more than once, according to respondents in eDigitalResearch's survey. This repetition bodes well for eventual consumer usage once the key parts of the chain are in place.

REACHING THE RIGHT CONSUMERS

Supporting mobile payments will become a greater imperative for brands. But the distribution of and appetite for mobile payments will vary according to customer.

In the UK, internet users most receptive to the opportunity are likely to be male, young and in the lowest-income bracket, according to Auriemma.

Demographic Profile of UK Internet Users Who Are Interested in Owning and Using A Mobile Wallet, Q3 2013
% of respondents



Note: numbers may not add up to 100% due to rounding
Source: Auriemma Consulting Group, "The Mobile Payments Report," Oct 2013

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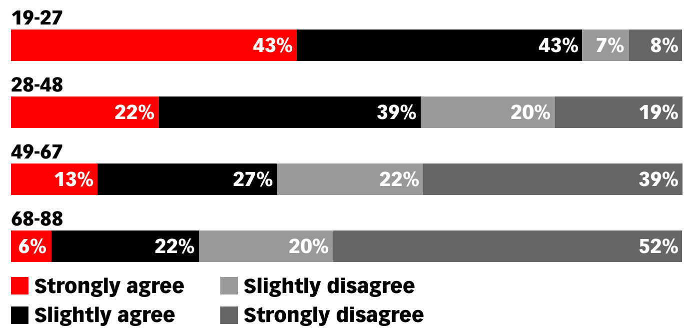
While this last fact may appear counterintuitive or even disheartening to merchants hoping to attract higher-income customers, the fact is that younger users naturally are lower earners and greater mobile phone users. Furthermore, elder consumers are less likely to shop online, while smartphone penetration is also lower among those older than 50. So young users are likely where early adoption will spread most easily.

The Auriemma survey data aligns with September 2013 polling from Kalixa, which found that younger users would be more likely to make mobile payments if there were some kind of financial value offered in return.

UK Internet Users* Who Would Make More Payments via Mobile Phone if Offered Loyalty Points or Financial Incentives, by Age, Sep 2013**
% of respondents



*Note: numbers may not add up to 100% due to rounding; *who have a current bank account; **instead of paying with a traditional plastic card*
Source: Kalixa, "Payment Generation Gap" conducted by Opinion Matters, Oct 2, 2013

168741 www.eMarketer.com

Taken together, the data suggests that mobile payments are most likely to be used with small purchases, at least for now. Just as Oyster cards have succeeded on the busy London Underground, frequently purchased, lower-priced consumables bought in high-trafficked stores may be better candidates for proximity payments than occasional big-ticket items, which need greater reflection.

IMPLICATIONS FOR RETAILERS

The outlook for mobile payments is brightening in the UK. Yet as the market conditions improve, retailers face a tough choice: Should they continue to build and manage their own payment service, ally with one or more of the fragmented array of current providers, or should they commit to support UK banks' new technologies?

The outcome of this decision may necessitate a commitment to new platforms, a focus on mobile loyalty and marketing in lieu of payment, or a combination of approaches. Despite the growing prospects for the technology, there continues to be no silver bullet, with each option and each prospective partner bringing something different to retailer strategy.

The lack of clear commitments to POS integration by Zapp and Paym, until at least the year following launch, certainly do not make them immediate in-store priorities—that piece of the puzzle may not get solved until greater clarity is provided around hardware standards.

Rival platforms may enjoy less widespread adoption than Zapp could theoretically attain, but at least they have in-store payment solutions in the market today. Furthermore, the creation by banks of two separate standards—one for P2P and small business transactions, the other for retail transactions—risks replicating the kind of proliferation and fragmentation already seen in the marketplace.

Partnering with Zapp and Paym early and on a nonexclusive basis to ease friction with online mcommerce transactions could be an effective way for brands to condition customers to use these standards online first and in-store later, while continuing with alternate partners for distinct purposes.

Retailers might also explore using Zapp, Paym or PayPal to facilitate transactions in a loyalty app that is otherwise owned and operated by retailers themselves. This integrated experience could provide retailers and customers alike with the best of both worlds.

However, while Zapp may bring the promise of mobile payments to tens of millions of UK account holders, it remains unclear how many of these consumers will opt in to use the service. Indeed, Zapp itself should, like retailers, consider how loyalty rewards can drive underlying service adoption.

If mobile payments are to achieve greater adoption in the UK, retailers and platforms alike will have to think beyond their own motivations and act primarily to provide consumers with greater value.

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