

Association for Payment
Clearing Services

The Way We Pay

A Market Review of the
Plastic Card Industry in 2003



APACS

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1 Introduction

Welcome to *The Way We Pay*, a review of the plastic card market, produced by the Association for Payment Clearing Services. In this report, we lay out – for the first time – key data on the use, and role, of plastic cards in our society over the last year.

Britain is truly a “plastic society” – but not in the sensationalist way that many newspaper headlines would make you believe. Without “plastic”, our society would virtually grind to a halt.

Debit cards have become, in a relatively short period, our favourite method of payment after cash. When was the last time you wrote a cheque? And when was the last time you got money from anywhere other than a cash machine?

The credit card sector too has grown, strongly, over that period. We have the most competitive market in the world – where else do you have a choice of thousands of different products, that give you such flexibility over what you spend, how much you borrow, and how and when you pay it back?

The British plastic card sector is amongst the most sophisticated in the world. We are world leaders in competitiveness and choice of services. We are world leaders in tackling fraud and in fighting Internet crime.

Our industry has 39.1 million customers holding debit cards, and 30.4 million holding credit cards. We facilitate payments in the UK, and in every country around the world. Every second, 246 plastic card transactions are made on UK-issued cards.

Although banks already are one of the most regulated industries in the country, in the last 12 months the payments industry has experienced more scrutiny than almost any other in the UK.

We have accepted and engaged with this scrutiny. Where we have agreed that better policies are required we have acted; where we believe such policies would be harmful to our customers, we have explained why.

Credit cards have become somewhat demonised as one of the principle causes of over-indebtedness. Yet all our main indicators show – and have shown for many years – that the overwhelming majority of us use credit cards responsibly.

Seventy-seven per cent of credit card expenditure is incurred by customers who pay in full in the next billing cycle, incurring no interest charges. Twenty per cent of credit card expenditure is made by people who sometimes pay in full and sometime use credit. And only three per cent is incurred by people who make regular minimum repayments.

In 2003 we had much to be proud of, introducing a number of initiatives outside of regulatory requirements. Chip and PIN represents a £1.1 billion investment in fighting plastic card fraud (putting the UK ahead of any other market in the world); the Summary Box, which gives consumers a simple and easy-to-understand comparator between credit card products; policy guidelines covering credit card cheque marketing and use; and set in place policy guidelines on credit limit increases on credit cards.

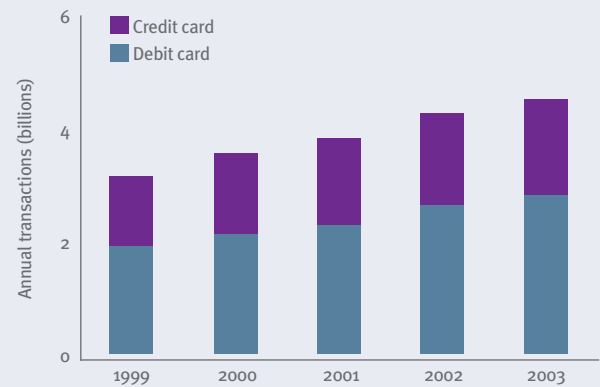
We feel proud of the role that we play in the UK.

2 The year in numbers: 2003

In 2003...

- There were 160.6 million plastic cards (debit cards, credit cards¹, cash machine-only cards and cheque guarantee cards) in issue in the UK, representing 3.5 cards per adult.
- The number of plastic cards in issue grew by 13 million (nine per cent); debit cards grew by six per cent and credit cards by 13 per cent.
- There were 39.1 million debit cardholders, who used their cards for 3.4 billion UK purchases, accounting for nearly £130.5 billion, an increase of 21 per cent.
- There were 30.4 million credit cardholders, who used their cards 1.8 billion times, accounting for £113 billion, an increase of 10 per cent on 2002.

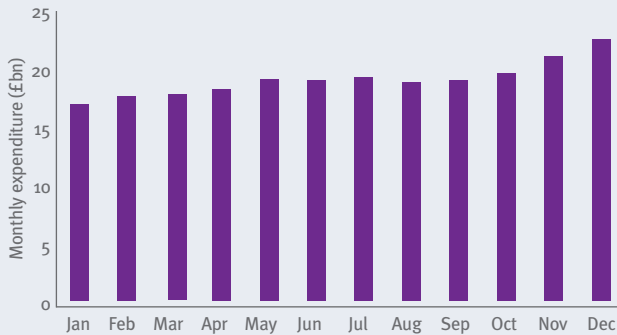
Plastic card transactions 1999-2003



- There were 31.6 million regular cash machine users, withdrawing more than £144 billion, in 2.4 billion transactions – increases of six per cent and five per cent respectively. 97 per cent of these withdrawals were made at no cost to the cardholder.

¹ All figures for credit cards include both credit and charge cards

Total plastic card expenditure 2003 (credit and debit cards)



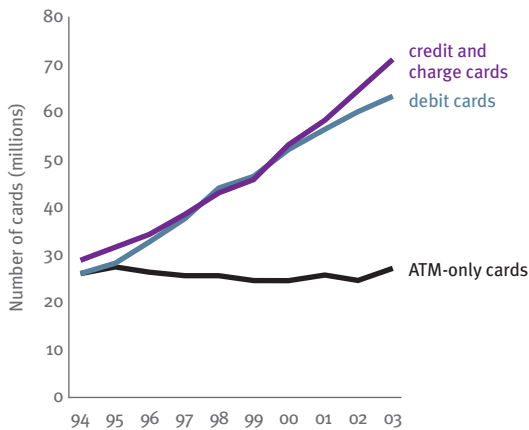
- 96 per cent of expenditure by individuals on credit cards throughout the year was repaid in full.
- Fraud losses on plastic cards fell by five per cent to £402.4 million, the first reduction in card fraud levels in eight years.
- 200,000 chip and PIN cards were used by 150,000 customers in 1,000 retail outlets in the successful public trial of chip and PIN in Northampton.
- There were 30 million Internet users in the UK, of whom 18 million purchased goods or services online, up 50 per cent on 2002. Plastic cards were the most popular method of payment; credit cards accounted for 69 per cent of the 200 million online transactions. The remainder were mostly debit card transactions.
- In any one second, there were 246 plastic card transactions in the UK.

3 Plastic: the great enabler

'Putting it on your plastic' has become something of a pejorative term, carrying implications of reckless spending on credit.

Yet without 'putting it on your plastic', our society would not function as smoothly. There are 160.6 million plastic cards in use in the UK, representing 3.5 plastic cards per adult. During 2003, almost 15,000 card purchases or cash withdrawals a minute were made.

Number of cards in issue at year-end



Eight in ten of all current account holders regularly made payments with their plastic cards. The majority, 14.0 million, were regular debit card-only users; 11.1 million were regular debit and credit card users; and only 8.2 million were credit card-only users.

£243.9 billion was spent on plastic cards during the year, of which 55 per cent was spent on the High Street. Another £133.5 billion was withdrawn as cash from cash machines.

All retailers accounted for 55 per cent of debit card spending, compared to 70 per cent of volume.

More than 700,000 outlets accept plastic cards, on more than 860,000 terminals. During the year the average outlet processed around 7,400 transactions, to a total value of £344,000, although in fact supermarkets took 39 per cent of all debit card transactions.

Around two-thirds of purchase transactions – 3.36 billion, or 64.9 per cent - were on debit cards, accounting for £130.5 billion (53.5 per cent).

Around a third of purchase transactions – 1.82 billion or 35.1 per cent – were on credit cards, accounting for £113.4 billion (46.5 per cent).

180 million purchases were made overseas, accounting for £13.0 billion.

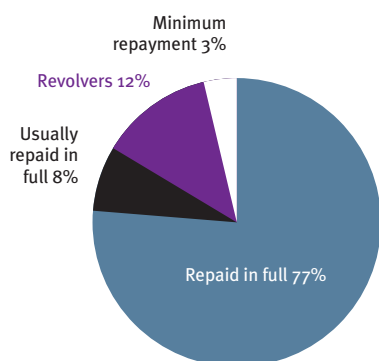
Together, these figures paint a picture of a society which could not function in the way it does today without the significant contribution made by cards. Plastic cards offer convenience, security and ubiquity – just think of the last time you tried to pay with a card and couldn't (and think how frustrating it was).

Even when considering credit cards alone, the idea that 'putting it on your plastic' somehow represents reckless borrowing could not be further from the truth.

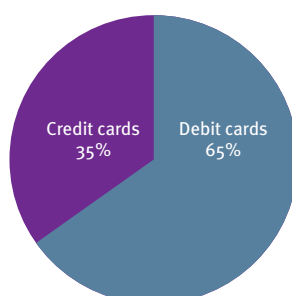
Seventy-seven per cent of credit card expenditure was paid in full in the next billing cycle, incurring no interest charges, according to APACS research last year. Ninety-seven per cent of expenditure was made by people who always pay in full, or who sometimes pay in full and who sometimes use credit.

The remaining expenditure was represented by people who make regular minimum payments – but this includes those switching balances to take advantage of zero per cent interest deals (when it is actually beneficial to make the minimum repayment, for the life of the zero per cent rate).

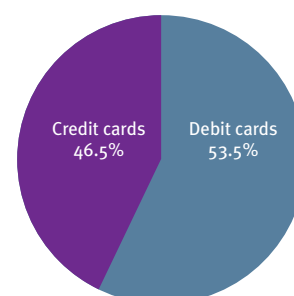
Credit card expenditure by repayment types 2003



Share of plastic card transactions 2003



Share of plastic card expenditure 2003 (£billion)



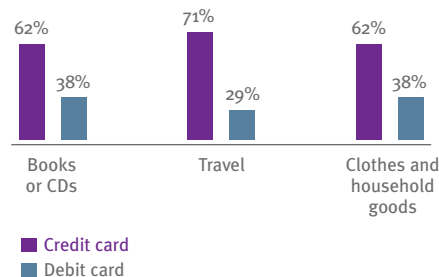
In spite of these figures, the industry continues to develop policies to further ensure responsible lending and use of credit. In 2003, according to the FSA, at least £35-40 million was spent on financial education by a combination of Government, industry, charitable trusts and the FSA itself. The industry also commissioned a new independent review of indebtedness in the UK, which provided clear pointers to policy-makers in how to measure and track the scale of this problem more effectively.

Plastic cards are also stimulating Britain's leadership in e-commerce. Real e-commerce growth clearly depends on secure methods of payment that plastic cards provide.

Following the dot com boom that continually hyped e-commerce use, 2003 was when the great e-commerce revolution took place, and could be regarded as the year that e-commerce came of age in the UK. More than 18 million people made Internet purchases last year, a 50 per cent growth on 2002, making 200 million purchases in total.

Credit cards remain the most popular tool for Internet purchases, accounting for 69 per cent of transactions and £10 billion of spending (nine per cent of credit card spending). This perhaps reflects awareness of the additional consumer protection that credit cards offer. Consumers are also protected from any fraudulent use of their card details.

Plastic cards have established themselves as the preferred method of payment in large portions of traditional and online retailing. Indeed, as we detail later, 2004 is expected to see a major milestone – the year in which spending on plastic cards reaches the same level as cash spending.

Proportion of internet shoppers using card type¹ by retail sector

¹Most recent purchase online

4 The debit society

2003 was a milestone year for debit cards in the UK. For the first time, more than half of all adults used debit cards on a regular basis to make purchases.

25 million cardholders, 53 per cent of the adult population, were regular users of debit cards in 2003. Nearly seven in ten of all 25 to 34 year olds were regular debit card users, and debit card users were only in a minority in the youngest (16 to 24) and oldest (65 and over) age bands.

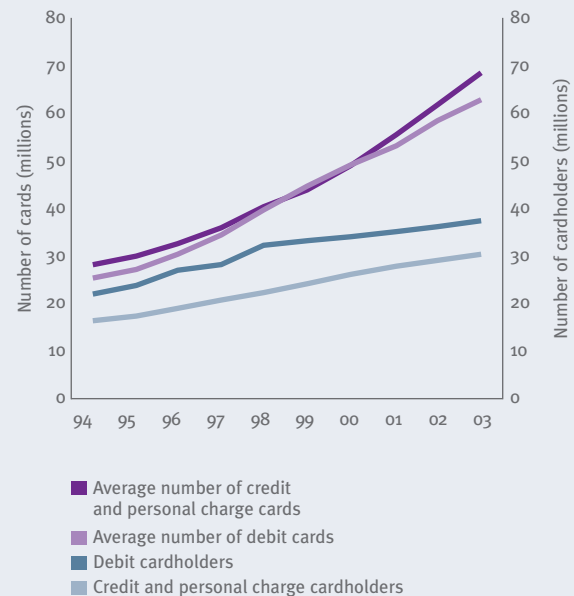
It marks the continuing evolution since their introduction in the late eighties, which has seen debit cards establish themselves as our preferred payment choice after cash.

Since 1993, the annual number of debit card transactions has grown nearly five-fold from less than 700 million to more than 3.3 billion last year.

The amount we spend on debit cards has grown even more dramatically. Less than £18 billion of goods and services were paid for by debit card in 1993; by last year this had grown nearly seven-fold to more than £130 billion.

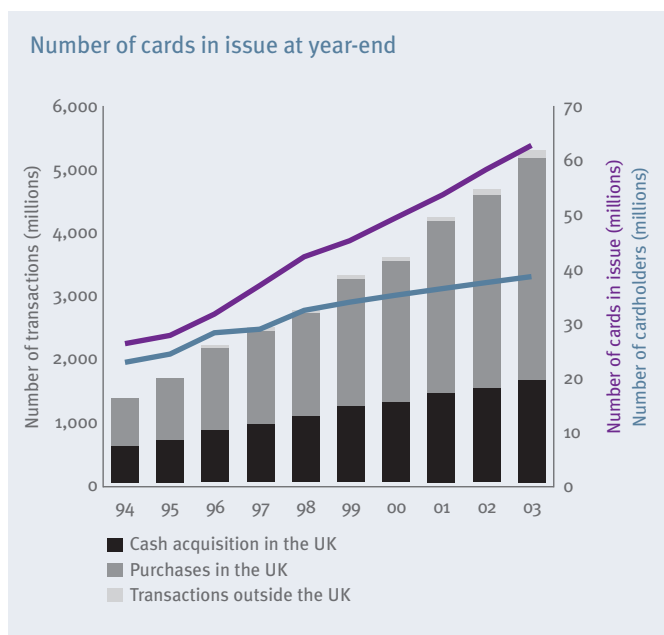
In that period, debit cards have also become our preferred choice of 'plastic'. Two thirds of plastic card transactions are now made using debit cards and more than half of all plastic card spending is made using debit cards.

Payment cards: number of cards compared with number of cardholders 2003



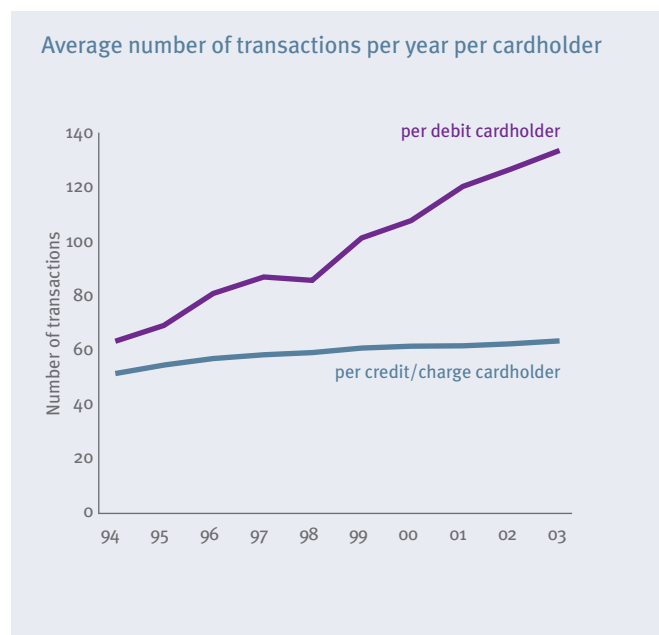
The number of card holders has risen steadily, and last year 39.1 million adults held a debit card.

They used their debit cards in increasing numbers. Purchases of goods and services in the UK rose by 12.4 per cent in 2003 to 3.4 billion transactions and spending was £130 billion, 21 per cent more than in 2002. Each regular user spent an average of £100 per week on their debit card last year.



The average value of a debit card payment rose at well above the rate of inflation to £38.83, from £36.02. In part this may be due to the changing pattern of personal debit card use with a greater proportion of transactions for higher value purposes. Although these transactions are still very small in volume terms, they have a significant impact upon average values. A further reason may be the growing popularity of debit cards with small businesses, as business payments will be of a higher average value than personal payments. It is estimated that up to one million debit cards are issued on business accounts.

The way we use debit cards has remained fairly stable. In 2003, 39 per cent of debit card payments were made in supermarkets, and, together with department stores, other retailers and garages, face-to-face locations accounted for nearly 90 per cent of all debit card payments. Internet debit card purchases accounted for two per cent of volumes last year; consumers prefer to use credit cards online.



The number of debit cards in issue grew by 3.4 million in the course of 2003 to reach 62.9 million at the end of the year. Today, the rise in cards in issue comes mainly from increases in multiple current account holding. Competition in the current account market has been intensifying and developments such as the system for transferring direct debits or standing orders have made switching accounts easier.

In 2003, more than two million adults opened a new current account. Typically customers do not close down their old account when switching and the average number of current accounts per current account holder is rising – last year it stood at 1.5.

5 Credit cards and society

2003 saw increasing interest in the credit card sector from Government, regulators and the media.

Barely a week passed without front-page news coverage of the sector, the bulk of it overwhelmingly negative. The industry was charged with lack of transparency, irresponsible lending and being a driving force behind a consumer credit boom that threatened imminent disaster for the economy.

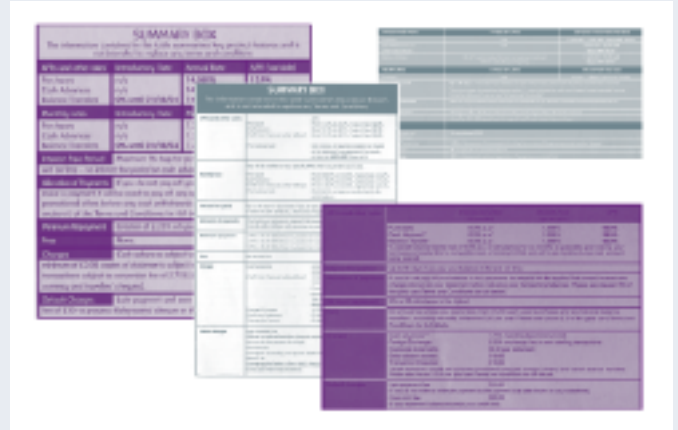
Where we agreed that better policies were required, we have acted; where we believed such policies would be harmful to our customers, we have explained why.

In the last 12 months, the industry has made significant strides to improve policies in a number of areas.

During 2003, we launched the Summary Box, a concise précis of the key features of credit card products, laid out in a common format on marketing material by each card issuer.

The Summary Box contains details on APRs and other interest rates; length of the interest-free period; how payments are allocated; what the minimum repayment is; all fees for having the card; and all charges that might be incurred.

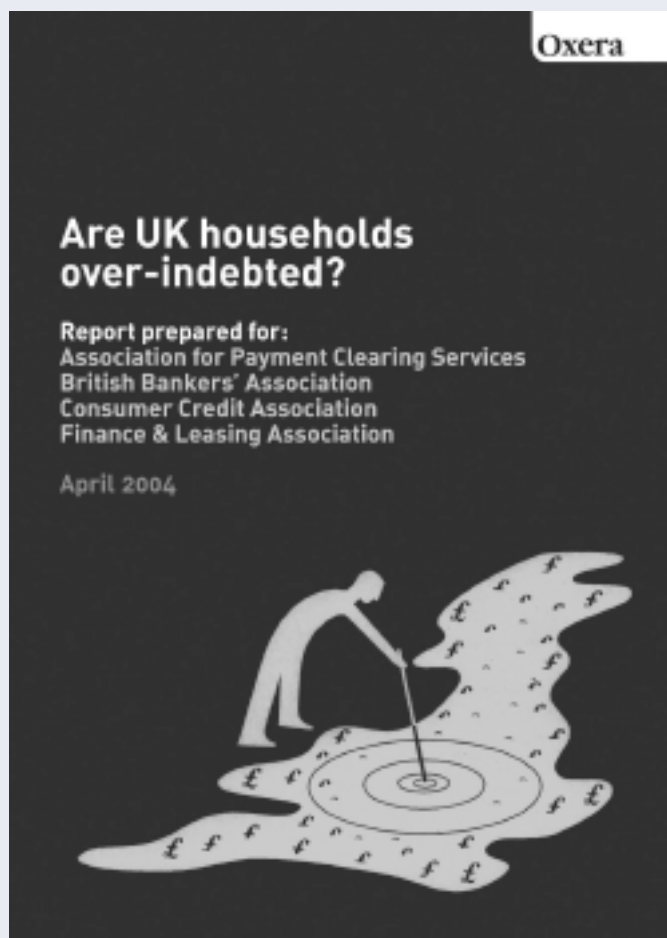
First introduced in October 2003, the Summary Box has since been adopted by all issuers, and the industry is now reviewing its impact, with further minor enhancements expected during 2004.



During the year, the industry also worked on the development of new industry guidelines for credit card cheques covering how they are marketed, and how credit limit increases are made. Again, these policies have been rolled out across the whole industry in 2004 and they have been put forward for inclusion in the next revision of *The Banking Code*.

APACS and its members also worked closely during the year with the Treasury Select Committee, and continues their close working relationship with the Department of Trade and Industry, the Office of Fair Trading and European regulators on a range of regulatory issues.

There have been many criticisms of the industry which are unjustified. Rather than jumping to conclusions, however, the industry has considered and investigated each area of criticism carefully before responding.



In late 2003, we commissioned an independent study into over-indebtedness, in conjunction with the British Bankers' Association (BBA), the Consumer Credit Association (CCA) and the Finance & Leasing Association (FLA), together representing the large majority of unsecured credit providers in the UK.

The study, conducted by Oxera, showed that over-indebtedness affects only a minority of UK households, is typically a temporary problem and that the number of households facing financial difficulties has remained stable for the last nine years.

The industry recognises the severity of any level of over-indebtedness and continues to work hard to combat it.

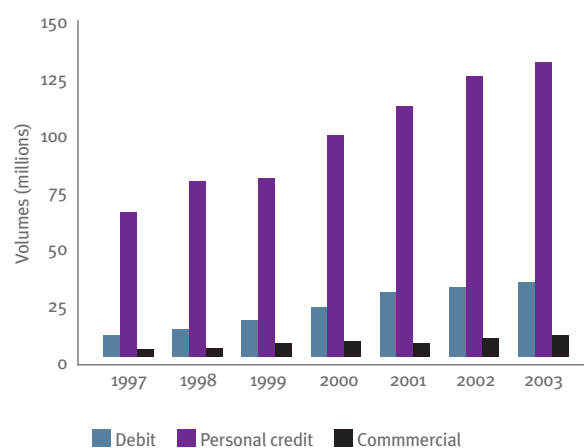
It is true that credit card spending rose during the year, by 10 per cent to £113 billion. Yet this lagged the 21 per cent growth in debit card spending (to £130 billion) and reporting of the rises regularly ignored the fact that repayments kept pace with spending.

The proportion of total personal sector debt accounted for by credit cards actually fell slightly during the year, from 5.7 per cent to 5.5 per cent.

Plastic travels

UK cardholders are using their plastic cards overseas with increasing confidence and regularity. Customers will often prefer to use a credit card while on holiday, including those who are regular users of debit cards in the UK. Consequently, credit cards accounted for eight in 10 of all cross border personal card payments in 2003, compared to around one in three of all domestic payments. Last year £9.8 billion was spent overseas on personal credit cards in 142 million purchases. Overseas purchases represented 9.6 per cent of all personal credit card spending last year, a proportion which has not changed significantly in recent years.

Cross-border payment volumes (UK-issued cards)



6 Fighting crime

2003 was a landmark year in the fight against plastic card crime.

A successful chip and PIN trial was completed during the middle of the year and the system is now rolling out nationally. And the industry's existing programmes were rewarded with the first reduction in fraud for eight years.

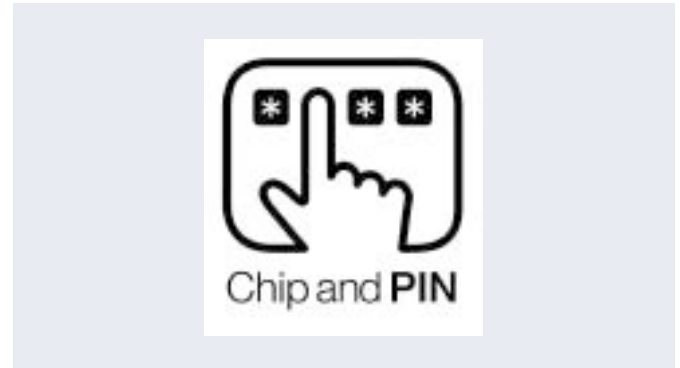
The high levels of card usage in the UK have made the market an attractive target for organised crime and the last decade has seen consistent growth in the types and amounts of card fraud.

'Cloning' or 'skimming', identity fraud, card-not-present fraud and straightforward theft of cards are all ways criminals try to get hold of our money. In the last five years, card fraud has more than doubled, to more than £400 million a year.

Even at this level, fraud accounted for only a tiny fraction – 0.13 per cent – of all card expenditure in 2003. Yet the industry has introduced a wide range of programmes to tackle the criminals, both here in the UK and abroad.

Chip and PIN is foremost amongst these. A total investment of around £1.1 billion will lead to the largest change in the way we pay since decimalisation. By 2005, the majority of debit and credit card transactions in the UK will be made on high-security chip-protected cards, using PIN authorisation instead of signature.

The public trial, in Northampton, was a resounding success. 83 per cent of people in Northampton were in favour of chip and PIN. As an added benefit, retailers saw shorter queues as PIN proved to be faster than signature at the point-of-sale.



Cards, shop tills and cash machines are all being upgraded and by the end of 2004, nine out of ten cardholders will have at least one chip and PIN card, and will be using them for the majority of their transactions.

Most European countries will follow the UK in introducing this technology to an agreed global standard.

Chip and PIN will help tackle more than 50 per cent of current card fraud, particularly counterfeit and fraud on lost or stolen cards.

But chip and PIN is only one element of the industry's fight against crime.

There is a whole range of initiatives both in place and under development to further safeguard cards and cardholders. One such example is the industry-funded specialist police squad, the Dedicated Cheque and Plastic Crime Unit (DCPCU). APACS and its members provide fraud investigators and administrative staff to work alongside police personnel in tracking and preventing fraud, particularly targeting the organised gangs who profit from this type of criminal activity.

Since its inception, the Unit has recovered more than 36,000 counterfeit cards and compromised card numbers and around 3,000 cheques earmarked for fraudulent use. It has seized assets and recovered property valued in excess of £2.1 million from raids on suspected criminals. And it has seen a success rate of almost 100 per cent in cases taken to court.

To date, its work has resulted in savings of more than £60 million.

The APACS Fraud Intelligence Bureau shares intelligence between the banking industry and police to combat skimming, the main form of counterfeit card fraud. In 2003, it tracked 15,000 compromised card numbers back to the place where the criminals skimmed the card. Subsequently, close liaison with the police led to the arrest of more than 270 criminals involved in card fraud.

APACS also plays a significant role in educating consumers and retailers on how to protect themselves against fraud. Our *Spot and Stop Card Fraud* pack has been used by more than 40 major retailers and more than 2,000 fraudulent cards have been captured as a direct result.

In June 2003, we published *Identity Fraud – the UK Manual* in conjunction with CIFAS and the Finance & Leasing Association, a pack that advises businesses on how to protect against this growing form of fraud. And in November 2003, the industry's Card Security Initiative focused on card-not-present fraud – where criminals use stolen cards or card details to buy via telephone, fax, Internet or mail order – securing widespread media coverage and retailer understanding of the issue.



The 2003 fraud figure fell five per cent from £424.6 million to £402.4 million, the first reduction in eight years. Chip and PIN, and other initiatives, will improve our protection against criminal activity but the industry remains vigilant.

We know that criminal gangs will continue to seek weak points in the systems. Our investment in leading-edge anti-crime work will continue.

The good news for cardholders remains the protection offered by the cards, and that unless they themselves have been negligent they don't lose out from fraud.

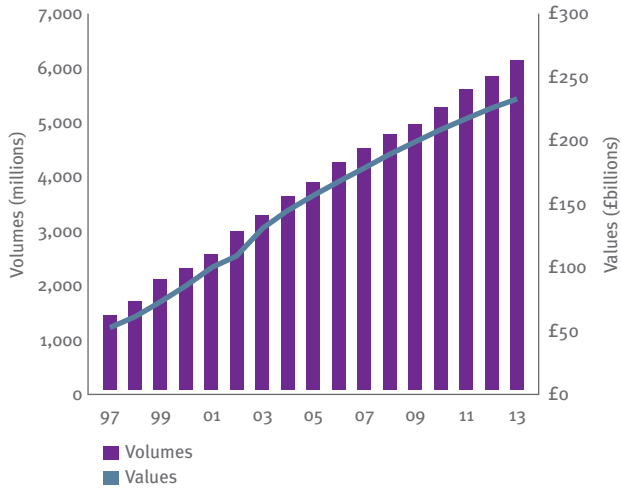
The fight against crime is not limited to fraud. In March 2003, APACS, the Children's Charities' Coalition for Internet Safety

(CHIS) and the Internet Watch Foundation (IWF) announced plans to combine their efforts in a bid to crack down on online

child pornography. We have committed to give financial support to the work of the IWF until 2006.

7 The future – key trends

Debit card volumes and real values: 1997-2013



The next few years will see a number of important developments in card usage trends.

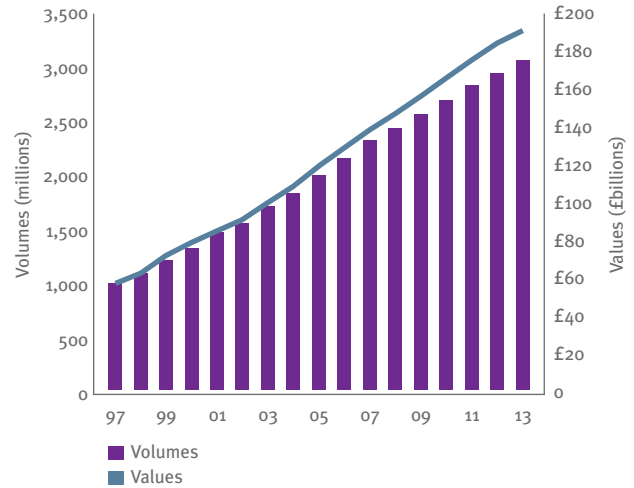
Key amongst these is cards' development into our most popular payment tool.

2004 is expected to be the first ever year in which spending on cards rises above cash spending.

By 2005, personal plastic card expenditure alone is expected to move ahead of cash expenditure and from then on, we will see an increasing gap between cash and card expenditure.

Debit cards will lead this growth. Over the next 10 years, we expect a growth in debit card spending of more than £100 billion (at 2003 levels). In 2013, we predict there will be 32.7 million regular debit card users holding a total of 80 million cards, each making an average of more than three payments a week on their cards.

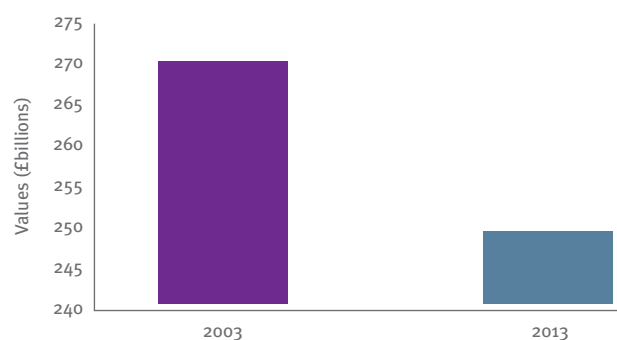
Personal credit card volumes and real values: 1997-2013



Credit cards are also expected to continue their growth, with a rise from 30.2 million cardholders in 2003 to 34.5 million in 2013. E-commerce is expected to give a substantial boost to credit card usage. In 2003, 69 per cent of the 200 million on-line transactions was on credit cards, reflecting awareness of the fraud prevention and purchase protection benefits provided by credit cards.

These trends do not mean the end of paper; cash will account for £251 billion of spending in 2013 (against £272 billion in 2003) and there will be an estimated 1.3 billion cheque transactions (against 2.3 billion in 2003). But the trends clearly point towards a significantly increased role for plastic cards.

Cash in society (£billions)



The other major development will be the full adoption of chip and PIN across the country. When chip and PIN has been fully rolled out, 130 million cards, 850,000 tills and 45,000 cash machines will have been upgraded, affecting 42 million cardholders and 2.7 million retail staff. It will be the biggest change to the way we pay since decimalisation.

The impact on fraud is expected to be significant, particularly on counterfeit and lost or stolen card fraud. But it is also expected to act as an additional spur to card usage, as making payments becomes quicker, safer and easier by using PIN.

The industry will continue to develop its policies on transparency and on responsible lending, and will work with regulators on the finalisation and introduction of the new Consumer Credit Act in the UK and the European Consumer Credit Directive.

In working with regulators, we hope to ensure new legislation does not impact adversely upon consumers or the industry. An APACS study found, for example, that if implemented as originally proposed, the Consumer Credit Directive would make UK consumers worse off by as much as £950 million, with up to two million people finding it difficult or impossible to obtain credit on the high street. This runs counter to the current debate which encourages the availability of low-cost credit to all sectors of the population.

Our aim is to ensure that the UK industry retains its position as a truly world-class industry, continuing to offer consumers highly competitive levels of choice, as the scale of card usage continues to grow.

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