State of the Industry: Changing but Unbroken

"Innovation is even more important but may be incremental and more focused on the business model and more efficient operations as opposed to paradigm-shifting ideas that pose unknown risks and regulatory threats," Hanson says.

Why Are We Still Talking about Awareness?

The industry also continues to face an awareness and perception problem, despite high satisfaction among consumers who've used prepaid products. Sixty percent of U.S. consumers have used a prepaid card in the last 12 months, with gift cards leading usage (44 percent), followed by rewards/incentives (15 percent) and GPR/payroll (12 percent), according to GfK research. With plenty of room to further penetrate the market—40 percent of respondents hadn't used a prepaid card—results around willingness (or not) to recommend prepaid to a friend, suggest the industry may be suffering from a lingering image problem, according to study author and GfK Executive Vice President Tom Neri.

GfK surveyed 1,000 online consumers representative of the U.S. population from May 30-June 2, 2014; and again Feb. 13-17, 2015. After narrowing the field to 609 prepaid users, GfK found that 65 percent or more consumers across income brackets were satisfied with prepaid cards. Yet, when prepaid users were asked if they'd recommend prepaid to a friend, the responses were more mixed.

M&A GURU ON WHAT'S DRIVING DEALS

M&A expert Robert P. (Bob) Zinn, partner at K&L Gates LLP, talks to Paybefore about what's fueling today's deals.

What are the drivers behind M&A in the payments industry broadly and in the prepaid sector specifically?

First, the drivers are totally different.

These days, prepaid is—if not quite old-school—a mainstream or even mature segment of payments. In a mature market, prepaid included, you see M&A to support very specific goals—like building scale, product diversification and vertical integration to achieve operational and economic efficiencies. If you look at two prominent acquirers in this space, Blackhawk Network and Green Dot, you'll see a combination of these objectives driving their decision making. And, of course, there are pure ecosystem drivers—such as margin compression, which is a function of the increased cost of doing business due, in part, to regulatory pressures and competitive limitations on pricing.

Consolidation is what you'd expect for a payments product approaching 20 years in market, like prepaid. And the greatest area of consolidation is in the most easily replicated part of the value chain—the program manager—where propositions for market entry are readily attainable but cost-effective scaling can be hard to sustain.

If you look at payments more broadly, the M&A hotspot is technology, especially fintech that quickly enables businesses to execute digital and mobile strategies that dovetail with the evolution of commerce as an omnichannel experience. PayPal's Paydiant acquisition and Samsung buying LoopPay are examples. As the traditional payments ecosystem broadens, cross-industry plays also can bolster M&A activity, as in the case of Google's acquisition of Softcard.

No one—not even the biggest names—fully understands what the endgame in the next age of payments looks like or how to get there. What they understand is the potential. And, this is precisely why M&A in this area is so active. The tech players are positioning themselves with the tools to try new approaches, experiment and gain consumer experience with new payments propositions. So, they're hungry to buy innovative businesses with potential, which is why valuations are so high and the investment community is all over the space—looking for the next big idea.

Prepaid M&A today is surgical. It's done with precision and specific goals. Payments technology M&A is making sure a company is positioned to win as the new payments market gains structure—even at the expense of buying and discarding a few companies or technologies along the way.