CHAPTER– 11

THE LACK OF STRONG COMPETITION IN THE MARKET FOR CREDIT CARDS

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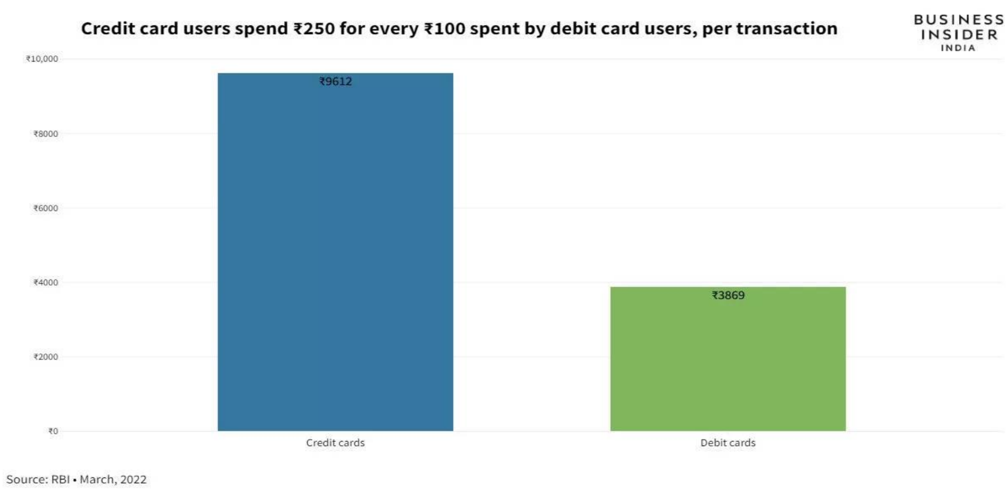
ABSTRACT

According to new research published by India's national bank, the Reserve Bank of India, the use of credit cards in India is no longer considered to be in its infant stages. Although they remain out of reach for a sizable portion of the population due to the requirement of a credit score, credit cards are already more valued than debit cards. There is only one credit card out there for every twelve debit cards, yet the number of something does not always indicate its value. Most of the requirements for a completely competitive market are mostly met by the credit card industry. The lack of consideration by consumers for the extremely high likelihood that they will pay interest on their outstanding accounts appears to be a contributing factor in the competitive model's failure.

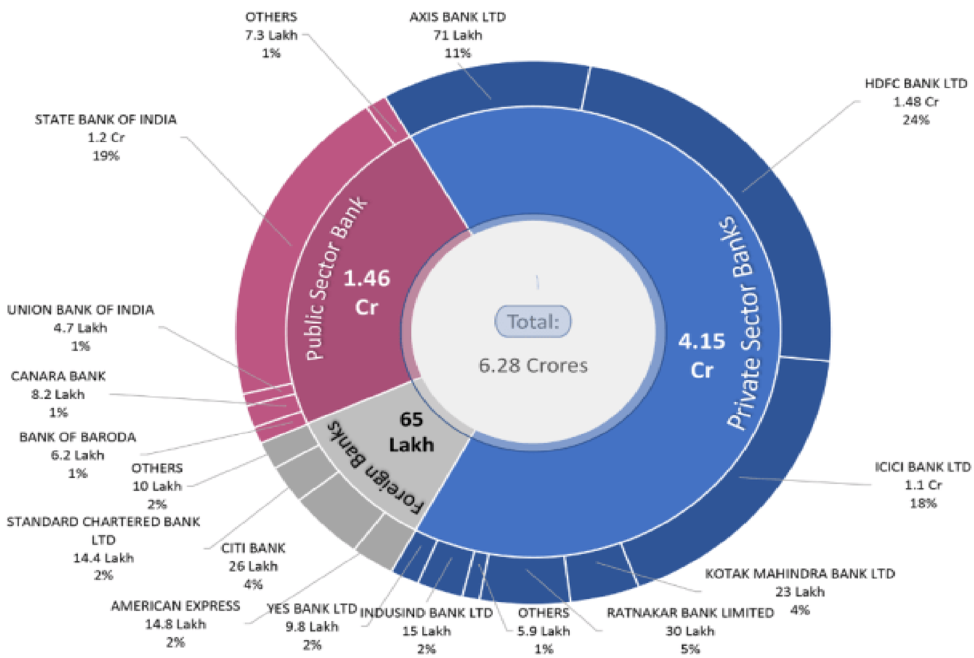
THE PROBLEM

"The bank credit card market of the 21st century is uniquely pathological, or can one identify other markets whose structures seem equally conducive to the competitive model"

According to the Reserve Bank of India's most recent statistics, there were almost 77 million active credit cards in India in May 2022. This represents a significant increase of 23% over May 2021 and an increase of over 100% over May 2018 data.

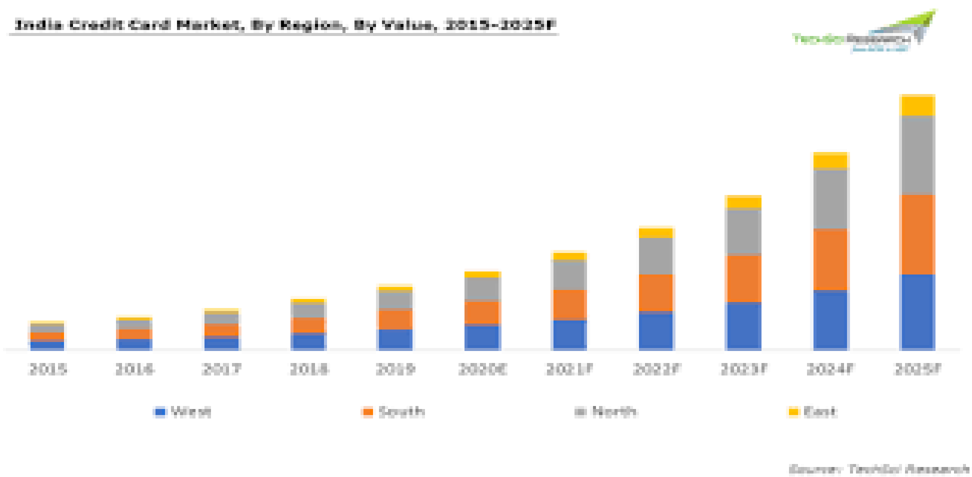


The credit card business initially appears to be a very consolidated sector of the economy. The three credit cards with the most recognisable names—Visa, MasterCard, and American Express—are used for more than 60% of all transactions. But upon closer inspection, the sector appears to demonstrate most of the traits of ideal competition. First, consider the quantity and dispersion of customers and vendors. Although most users choose Visa, Mastercard, and American Express, these cards are issued by more than just those three companies. Currently, out of every 100 people in India, only three of them have a credit card. This shows that there is great scope for development in this industry. There are actually over 77 million credit card customers in India, and these cardholders can choose from among the dozens of businesses (mostly banks and credit unions) that issue credit cards in the country. A neighbour in Delhi may have gotten her Visa from ICICI, while someone in Haryana may have gotten theirs from HDFC, where they both work.



As you can see in the donut chart that is located above, we segmented market share into three sections: 1. Public Sector Banks, 2. Private Sector Banks, and 3. Foreign Banks due to the fact that they have a greater exposure. These days, there are a lot of fintech businesses that provide credit cards, but most of them have partnerships with card issuing companies, thus some of these facts are also provided by such companies. One could say that credit cards are a rather uniform product. The majority of Visa cards look identical and have the same functionalities. The merchant is unlikely to notice who issued the card when the charge is made. The banks that already issue credit cards are proof that entering and leaving the credit card market is simple. A new company may have trouble breaking into the market, but a financially strong bank, even one of modest size, might easily get the licence to provide a MasterCard or a Visa card from the existing corporations. There would be a ready market to sell the bank's accounts to other credit card providers if it decided to exit the business. Therefore, it appears that the credit card market possesses the majority of the traits of a completely competitive market.

The bank credit card market, which has a large number of businesses and no regulatory restrictions, might seem like an ideal setting for the perfect competition model. But according to this article, relative to the cost of funds, credit card interest rates have been particularly sticky. Major credit card companies have also consistently earned three to five times the standard rate of return in the banking industry. The lack of consideration by consumers for the extremely high likelihood that they will pay interest on their outstanding accounts appears to be a contributing factor in the competitive model's failure. Visa, MasterCard appear to control an apparent oligopoly in the credit card sector. However, a closer examination reveals that behind the surface, Visa and MasterCard are basically associations of financial institutions that issue cards and "acquire" businesses that consent to take the cards as payment. Many of the thousands of members of Visa and MasterCard are banks. Indicating monopolistic competition, this. However, a closer inspection reveals that the card-issuing market has gotten more and more consolidated. The top ten companies hold about 90% of the market in terms of cardholder receivables, or the money that cardholders owe their issuing financial institutions.



The market data seems to contradict the idea that most buyers are educated people looking to cut their borrowing expenses as much as possible. Neither that consumers are often provided competitive interest rates on credit card balances nor that most consumers take advantage of lower interest rates when offered is supported by the available data.

The empirical results of this article raise a bigger question: is it true that the bank credit card market of the 21st century is the only one with a problem, or can other markets be found whose structures seem just as good for the competitive model but whose results are also not competitive? This appears to be ripe for additional exploration.

QUESTIONS

1. The credit card business seems to exhibit between five of the criteria of perfect competition. What are these traits?
2. Explain the perfect competition's output and pricing assumptions.
3. What is the obligation of business towards society? Support your answer with reliable sources.

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