Plug into Paysafe:

Embedded Finance: What's behind fintech's hottest trend?

Embedded finance has become the fintech buzzword of the last 12 months. In this four-part series we look deeper into the opportunity and applications for this mega trend and what brands should consider when they embark on their embedded finance journey.

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The consumer take on embedded payments

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It might be a hot topic for merchants, payments providers, banks, and a plethora of other financial services players, but what do consumers think — and know — about embedded payments?

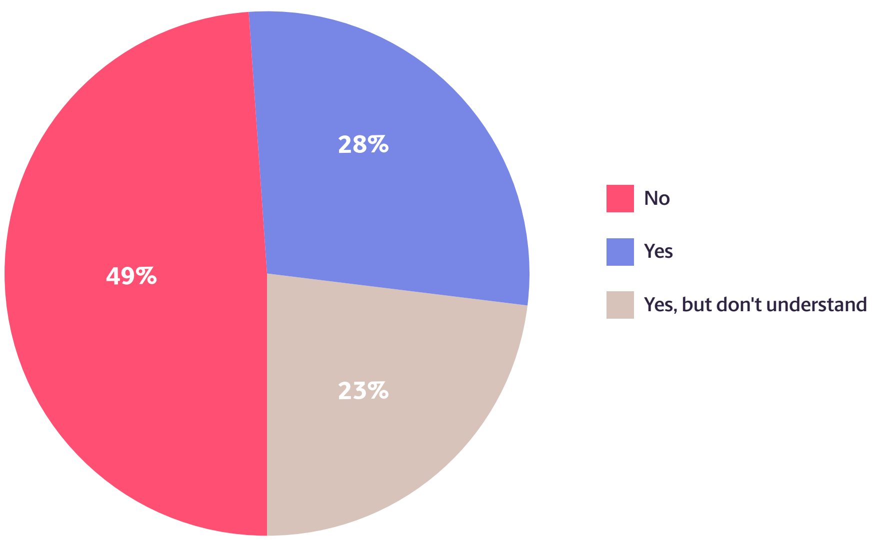
A trend that's rarely been out of the spotlight and continues to drive billions in investments yet seems to be more mystery concept than transaction revolution for the average consumer: in Paysafe's 2022 Lost in Transaction survey of 11,000 respondents in Europe, North America, and Latin America, we asked consumers about their perception of embedded finance. Before we share more detailed thoughts about embedded finance from a business perspective, we explore some of the perceptions among consumer audiences and see what the results mean for merchants.

"Embedded what?"

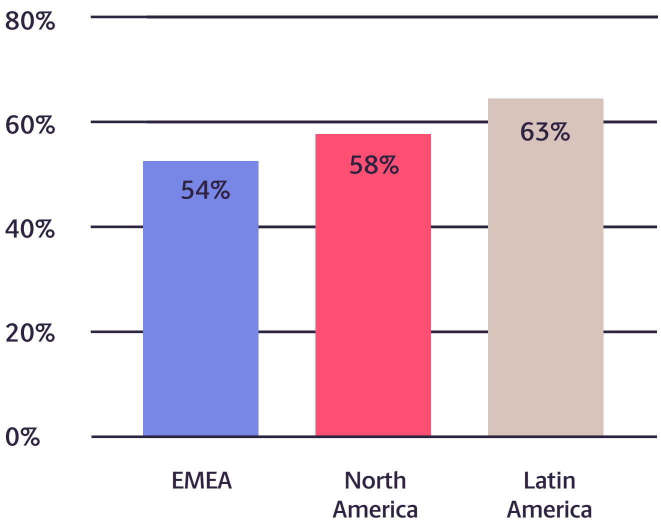
Nearly half of those who took part in the survey — 49% — have never heard of the term embedded payments. And of the 51% who have heard of the term, 23% don't understand what it means. This shows us that while there may be much fanfare across the industry, consumer awareness of embedded payments is generally low.

There's a noteworthy difference between responses to this question in Latin America compared to EMEA and North America, with only 39% in Latin America having never heard of the term versus 53% in EMEA and North America combined. Latin American consumers' keen adoption of alternative payment methods in the last couple of years might explain this more extensive understanding of the digital payments options available, as well as knowledge of how they work.

Have you heard of the term embedded payments? | North America



% of respondents who agree they don't know enough about embedded payments (by region)



Back to the worldwide picture, and of those who have heard of the term embedded payments, 58% of respondents agree with the statement that they don't know enough about embedded payments. Here, in contrast, we see minimal variation between EMEA, North American, and Latin America — 54%, 58% and 63% respectively.

So one of the strong messages coming out of Paysafe's research is that there is a clear opportunity for more education around embedded payments. This means there's huge scope for the role of merchants in not only highlighting their embedded payments capabilities, but also helping the consumer base understand the benefits and thereby encouraging greater uptake.

Already the ultimate frictionless experience?

While the survey results expose a big knowledge gap and demonstrates a need for more education around embedded payments, there's also a clear willingness to get to grips with the concept. This suggests people would be more open to using the option when paying for services online and on their smartphones.

Another key point is that a fair number of consumers who responded that they don't know (or don't know enough) have probably used embedded payments, but not necessarily realised they had. Or perhaps they've just not known this is what we call it in the fintech world. How easy is it to book a cab on an app, order a takeaway? And how many of us when we do this, think — "that was a seamless embedded payments transaction"?

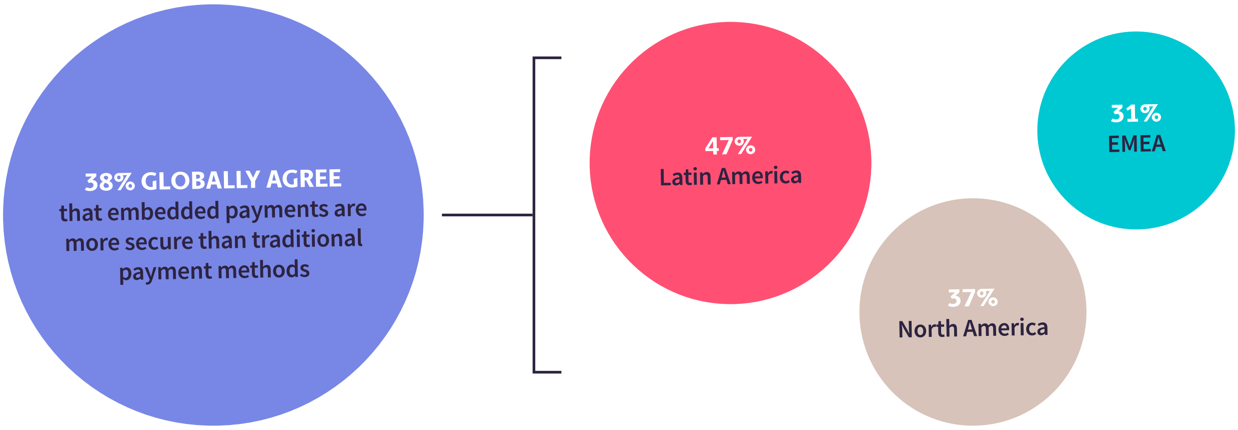
The thing is, consumers know when they've had a substandard experience. They know when there's friction. And the whole idea around embedded payments is that the payment aspect becomes so seamless that the consumer doesn't need to expend any of the usual effort of locating their wallet or purse, entering card details, organising a transfer. Nor do they encounter any of the potential problems, such as dropped or declined transactions or long wait times as authentication processes take place. So these figures might, in part, reflect the fact that the embedded payments transactions consumers are having are so seamless as to be entirely unnoteworthy — they just work.

Embedding the experience and building trust

That being said, broadening consumers' knowledge around embedded payments and its benefits is no bad thing. Especially addressing the security concerns that some respondents have expressed.

Like with many emerging tech trends, consumers may be taking time to get used to the concept. Currently, only 38% of those who have heard of embedded payments globally agree that they're more secure than traditional methods of payment. When broken down into region, the responses highlight another interesting geographic difference, with 47% of Latin American consumers reckoning embedded payments are more secure than traditional payments, compared to 31% in EMEA and 37% in North America.

Respondents who have heard of embedded payments



Another significant callout on security is that of those that have heard of embedded payments, 59% worry that they might be charged the wrong amount when using embedded payments. This is a fundamental concern that needs to be addressed before we can expect more widespread adoption of embedded payments.

So for merchants and payments providers, getting the word out there is a top priority. Highlighting not only the speed, ease, and convenience benefits, but also showing that security — and consumer control — are bolstered rather than compromised with embedded payments. Build trust, and they will come.

Maybe, also, we need a better moniker. One that sticks more comprehensively in the consumer mind and says more about their experience — which is what matters — than how we think of it as merchants and payments providers. Answers on a postcard, please.

In the next three articles, we'll be looking at the embedded finance ecosystem, strategies and questions for merchants, and what three critical elements successful use cases have in common.

Evolution and opportunity in the embedded finance ecosystem

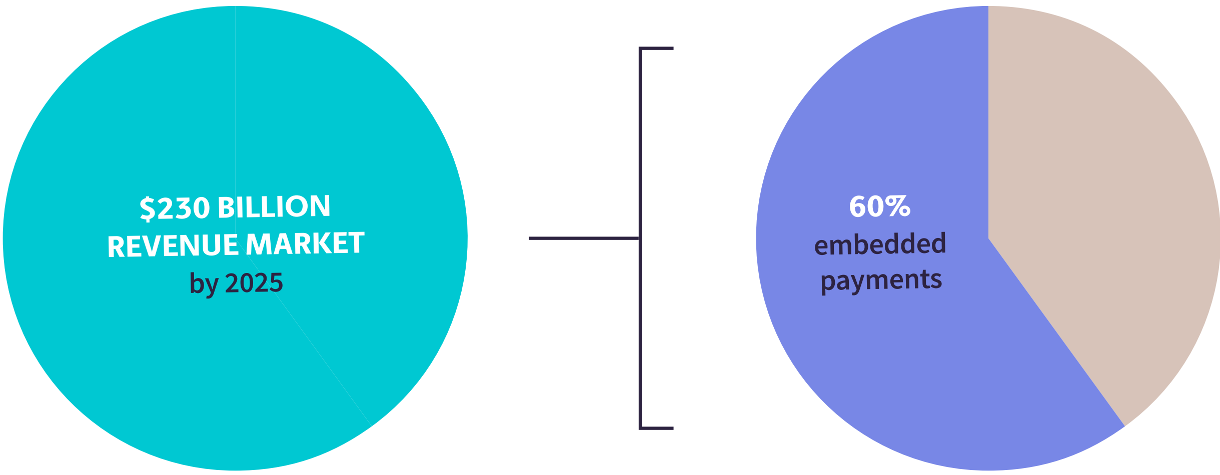
2

In this article, we're exploring the embedded finance environment today. How and why we've got to where we are, and what embedded finance means for consumers, merchants, and other key players.

Towards more agile payments functionality

Open banking has been the enabler of many aspects of disruption in financial services and payments. And as the disruption has played out, embedded finance has become increasingly relevant. This, along with the shift to online in the wake of the pandemic and greater customer expectations of the payment experience, has accelerated the speed with which we've arrived at where we are. And that, in a nutshell, is lots more embedded finance use cases. It's also what's fuelling forecasts of growth over the next few years — a $230 billion revenue market by 2025, according to Lightyear Capital, with embedded payments making up around 60% of that.

Forecast of growth for embedded finance



The rapid changes happening at the checkout — for example, the rise in both cryptocurrency payment methods (63% growth in the year ending October 2021, as we saw in our survey) and digital wallets (67%) — is a clear signal to all companies that they need an agile way to provide new payment capabilities. Because while the landscape looks different today compared to 12 months ago, it's a given that we'll be saying the same thing in another 12 months' time. This is why building financial functionality into their offerings — and by that we mean functionality that can change as demands do — is going to be essential for the vast majority of brands.

The road to embedded finance: from opening gateways, to open banking and open ecosystems

We can look at payments innovation as an evolution in three stages. Back in the day — before we lived in a world of pandemics and lockdowns — we watched the payment gateway come to the fore: both dedicated gateway services provided by the payment provider and those which are directed by a gateway vendor to the processor. The aim was to remove friction from the payments process. Simply, ecommerce firms and merchants operating online could use a payment gateway of whatever flavour to make it easier for their customers to pay.

With open banking on the scene, payments evolved. A frictionless experience when paying by debit card online was one thing. Customers wanted more choice. Open banking provided this — the ability to offer alternative payment methods like digital wallets as well as allow consumers to pay for services from their bank accounts. So from more seamless experiences we started seeing optionality of payment and a proliferation of alternative payment providers to service this need.

As consumers and merchants — and all the providers (financial, tech or fintech) in between — have become more savvy, the platform economy has started to emerge. We have different ways to pay, but we also have a host of associated services within our reach in this same space. And we don't have to leave the environment we're in to access the products we require. This is where embedded finance is finding its feet, enabling the fulfilment of a variety of financial needs as part of a highly integrated services experience.

What's driving the trend?

The embedded finance phenomenon has been both customer- and merchant-led. Customers get fast, seamless experiences. They get convenience. They get to pay how they want within an environment and through a brand they trust.

The merchant reaps numerous benefits too. Reduced transaction costs, increased revenue opportunities, better control over what services it can deliver, and a keener level of insight into its consumers' spending and habits. And, as a result of being able to target appropriate products at the point of need, the value the brand delivers to the customer grows, with a corresponding hike in satisfaction and loyalty.

When done right, it's a win-win situation.

Perception around financial services, and who dispenses these services, is also changing. Consumers are becoming more used to sharing their data, especially if they get something in return. So, with the right incentives, they're more likely to be comfortable signing up to financial products through non-financial companies. Especially if that company is a brand they know and have had good experiences with in the past.

So, all-in, there are quite a few forces at work making embedded finance a perfect solution to both consumer and merchant needs.

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The shift to a platform economy

There are many embedded finance use cases that have been about for a while. As online shoppers, we've all come across the option to pay in instalments for a product or service. This type of embedded lending at the checkout — buy now, pay later — is often faster and more seamless than getting your credit card out, punching in the details and waiting for authorisation. And the merchant gains advantage by keeping the customer on its site and opening up a new revenue stream.

Other classic embedded finance use cases include financial service add-ons to a primary product, such as integrating insurance when you buy a fridge freezer. Or the financing of larger purchases through loans enabled by the merchant. These payments methods are being embedded by companies in every sector. Car retailers offer not just leasing, but their own insurance products. Airlines provide you with a loan for your annual family holiday.

The transition now is towards greater integration. Platform companies like Uber, Grab and Toast, are successfully embedding entire portfolios of financial services into their businesses and creating significant new revenue streams as a result. In these examples, it's almost not about the payment at all. It's about the experience.

Getting a piece of the action

There's opportunity at both ends of the spectrum. But to hit the mark with consumers, organisations need to ask some key questions about their business models, and consider not just the tech they'll require, but, more critically, what issue they're trying to solve. In our next article, we'll explore what some of those questions are.

Making embedded finance work:

3 questions to secure success

3

While the hype is enough to make any and every company think it's easy to unleash a raft of payment options, is that true in practice? In this article, we're looking at some key considerations for creating a successful embedded finance strategy. The questions merchants need to ask about their businesses and their customers. And what a good embedded finance partner looks like.

Clarity of strategy

As history has taught us, jumping on the latest tech bandwagon just because it's there and you can, is a recipe for disaster. Not falling foul of this basic tenet of business is even more vital when you're dealing with payments and financial functionality. A great brand adding finance capabilities that either don't hit the mark or don't work as they should, is at best a waste of time and at worst a sure-fire way of losing customers. As with any change to business strategy, adopting embedded finance should be driven by customer need. Closely followed by an assessment of your ability to cater for that need.

1. Where's the friction?

Whether in the customer's journey or in the way you're able to deliver what you want to deliver to them — what are the sticking points? Any successful idea is essentially a solution to a problem, and with embedded finance this involves not just the individual's interaction with your brand, but areas of friction or need after they leave your environment. Can you solve one of those challenges by bolting on functionality and keeping customers within your ecosystem?

There's also the issue of operational friction. In a highly regulated industry such as gaming, for instance, there are additional pressures that might affect the type of services you're able to provide customers.

2. What's your hook?

The benefits are great for those who find the right recipe. Companies have a significant amount of transactional data on their customers. This means being in a good position not only to target the right products at point of need, but also to create completely new revenue streams. An opportunity not lost on Tesla owner Elon Musk, who reckons the company's foray into the insurance market could represent 30–40% of Tesla's business in future.

Here are some questions it's worth thinking about to frame your approach.

If you're adding something on to existing services, what is it you currently provide that can be enhanced through embedding payments?

Will it lend depth or diversity to your customer interactions and your brand?

Can you provide a financial service that's better and more convenient than your customers can get elsewhere?

If you're launching with a new idea or platform, who are your customers and why will they use your business?

The likelihood is it's not a net new idea (few are), but you may well be providing a novel experience because of the combination of product and/or service plus payments options.

3. What's your commercial strategy?

Understand the solution you're providing — whether that's to consumers or suppliers, or both. Putting in place the right operational constructs is a more time-consuming part of the journey than the technology piece of the puzzle. For example, in terms of compliance, knowing your responsibilities and establishing good practices. And in the case of security, deciding the appropriate layers and levels of checks. Again, the answers to these questions will be specific to your market.

Embedding your advantage

Embedding capabilities such as digital wallets into your service can give customers choice and solve some of the points of friction around transactions. Our recent Lost in Transaction survey shows that digital wallets are the third most used payment method after debit cards and credit cards, with a quarter of respondents saying they use digital wallets more than they did a year ago. This reflects the convenience and security they provide, which is why they're attractive to consumers. But they're also a win for merchants. With an embedded digital wallet, customers are more likely to complete their purchases because of the fact the process is so easy and overcomes the common frustrations of some other payment methods.

Digital wallets have additional advantages for merchants. They can be branded and therefore work to strengthen customer loyalty and brand awareness. And with access to consumer payment data, they give businesses a better understanding of customer preferences so they can hone their offerings and provide a more personalised experience.

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A fit-for-purpose partner

Finding the right partner is going to be most merchants' quickest route to embedding payments into their offerings. A provider that both understands the nuances of your industry and is able to complement your internal skill sets will be valuable in more ways than one. Not just in helping to overcome hurdles of tech and operational implementation, but in identifying potential embedded finance use cases and helping answer some of the critical questions that we've covered.

It's worth considering how much help you'll require overall. It can be as simple as getting the API keys and running with it — 5 minutes to operational payments provision is entirely achievable — but usually there's more to it, especially in the longer term. No solution, embedded finance or otherwise, works truly out of the box, so a no-contact provider should be a no-go. But a good provider will make integration as easy as possible, with technical documentation, support, and integration guides to help your team. And remember your payments needs, along with your integration requirements, will change. You may start out happy with a low-touch provider, but then favour a more consultative approach further down the line.

Connections matter

On a basic level, you need to choose a payment provider that will be able to help you access the markets and geographies you're targeting. So that means holding the correct licences, but also having robust relationships with regulators and strong connections with local partners.

You'll also want a range of options when it comes to products. A wide selection of alternative payments methods that you can mix and match according to need. Look at the wider ecosystem that your provider can connect you with, too. Integration to specialist third-party financial services might not be something you think about straight away, but as your financial services proposition to consumers becomes more sophisticated, this type of integration could be important to your commercial strategy.

Also ensure you're working with a partner that's able to scale as you need it to. One with a responsive, agile infrastructure that can handle spiky workloads, which could be anything from high-volumes of transactions in response to a sales promotion, or the general seasonal cycles of a business.

Getting on the road

It's clear that companies adopting embedded finance need to understand not just the nature of their offerings and shifting demands of their customers, but the expertise and tech stack of the providers they choose to work with. As with most new ways of operating, embedded finance involves both technical and strategic challenges, as well as expertise in bringing those elements together.

In reality, as we've seen, the tech is probably the easiest and fastest part to put in place. And that, essentially, is the beauty of embedded finance and where it stands today. It's the simple bit. Bolt it on and you're good to go. Just make sure you get the rest of your house in order first.

In our final piece, we'll be looking at how embedded finance is playing out in different sectors — and where the greatest opportunities lie.

Embedded finance applications and opportunities:

Right product, right time, right place

4

We're seeing both tried-and-tested and more novel applications of embedded finance from players in all industries. Here we take a look at some use cases — and highlight the three critical elements that successful approaches have in common.

Bridging a gap

In exploring use cases across different sectors, we see common themes emerging. What's central to them all is that they create a more fluid experience. But, more than that, they get one step closer to their customers, reinforcing brand trust and the subsequent loyalty this generates.

How close depends on market-specific factors. Regulation hoops. How high or low risk the sector is. The levels of security — not just the layers that are necessary, but those that make consumers feel comfortable (as we'll see, sometimes friction can be a good thing).

Fly, fly away?

Opportunities tend to arise from not-so-ideal situations. A recent example of this that will resonate with many, was the considerable friction caused by the lockdown rules at various stages of the pandemic, which required would-be travellers to cancel flights and accommodation bookings. Hundreds of thousands of people in the UK alone having to claw back their money from airlines, hotels, car hire companies, and the rest. In the clamour, we expect more people than not had pretty poor experiences trying to get the various travel-related agencies to settle up.

But the frustration wasn't just felt consumer side. Airlines, online booking agencies, and other travel merchants were plunged into an administrative nightmare. For a major airline, for instance, something like an airline voucher system is a huge operation involving departments of people and necessitating the shifting of money and vouchers from one place to another. Such a complex and time-consuming undertaking costing into the millions if not billions could have been entirely avoided with a simple embedded finance solution: an escrow account, by which a third party holds the funds until the service is delivered. In this case, when the traveller takes the flight. Indeed, a whole new type of service offering has emerged from this, with companies like Fly Now Pay Later taking a single use case and making a brand out of it.

Keeping them in your world

Some of the time, it's not necessarily about solving a pressing or particularly acute problem. It's about achieving seamlessness, making your customer happier — and keeping them in your ecosystem for a greater part of their journey.

The iGaming sector is a good example of this. A service based on immersive experiences, it's obvious that anything that can make it more so is better for players. So in the case of the onboarding process, embedding a financial product can make this slicker by minimising the administration required to sign up new players. The player submits their details once and simultaneously registers with the iGaming merchant to get access to its services, as well as fulfilling the requirements for signing up to the digital wallet or other payment method that'll then be linked to their account.

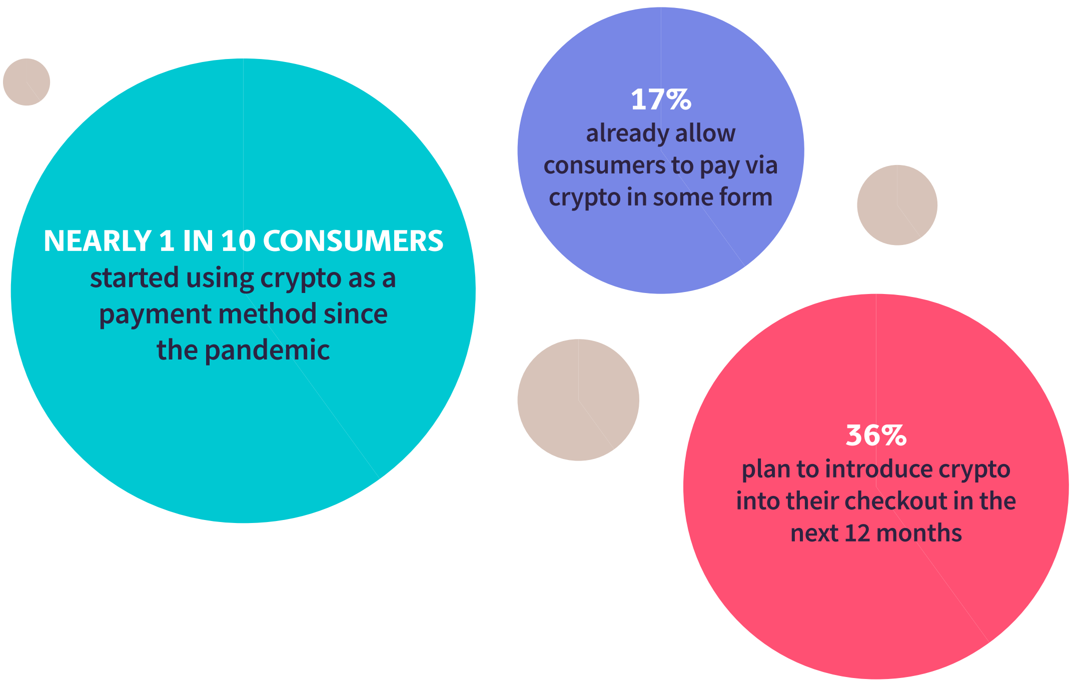
Crucially, this also means one set of Know Your Customer (KYC) processes and less chance of fraud. After all, the merchant already knows — and has a significant amount of transactional data on — the customer, so the relationship is established. On top of that, the insight that the merchant has through that customer data can then be used to anticipate their needs further down the line.

The crypto factor

No review of the drivers of embedded finance and changes in consumer appetite for alternative payment methods is complete without a look at cryptocurrency. Crypto has been an area of huge growth in the last couple of years, driven largely by consumer demand. According to Paysafe research — which surveyed 1,100 businesses across the UK, North America, Italy, Bulgaria, Germany, Austria, and Brazil, — nearly one in ten consumers have started using crypto as a payment method since the pandemic. While 17% of businesses say they already allow consumers to pay via crypto in some form, and a further 36% plan to introduce crypto into their checkout the next 12 months.

The call for crypto at checkout is going to be higher in some markets — for example, gaming and tech-related products and services — than others. But we're currently seeing an increase across the board, so building it into the checkout experience is no longer a lookout for niche merchants and services providers. However, it's a more complicated process than, say, adding a digital wallet. You need to understand the anti-money laundering, KYC, and regulation issues around crypto. Here, a specialised embedded payments provider can help, giving insight into these needs — outlining what your responsibilities are and providing a range of alternative payment methods. Acceptance rates when buying crypto are typically higher when they are made through digital wallets as many banks reject them, which is also why it's important to have choice and choose an embedded payments partner that has a good relationship with crypto-friendly banks.

1,100 businesses surveyed



Right-sizing security

This also highlights an important point about the role of security and embedded finance. We've touched on the differences of operating in markets with varying risk factors. And while we're always saying that customers want less friction, sometimes it pays to have some well-placed friction to reassure them that their data and funds are being protected. Which means applying appropriate layers of security relative to what consumers are buying or doing in that ecosystem. If they're trading in Ethereum, they might be pleased to go through two-factor authentication, type in the name of their first pet, school, and girlfriend's name, and recite a pass phrase backwards. If they're just booking an Uber, maybe they'd prefer to bypass some of those security steps.

Essentially, it's about getting the right balance of security and usability.

#1 Enable integration. #2 Build trust. #3 Make it speedy

The three takeaways from our brief look at applications of embedded finance aren't anything new. Broadly speaking, they have three things in common.

First, they provide integrated experiences. This is as much about making things work seamlessly as it is about creating an environment that consumers don't want to leave.

Second, they work transparently, and the services they offer are transparent. Plus, they communicate that transparency to their customers. This is what generates trust within their ecosystem.

Third, when it comes to transactions, they know that real-time is key. Fast transactions are a must. Mess around with this aspect of consumer interaction, and you've lost them.

So, success is simply getting all of these factors spot on.

Great CX pivots on payments

As ever, all roads lead back to the customer experience — and payments functionality very much sits at the heart of that. Regardless of sector, target market, or type of offering, it's just about making it easier for customers to pay for services.

The nature of online consumer interactions continues to shift. The key for merchants is having the flexibility to adopt the services they need to deliver the best experience, with the least friction, and the most appropriate level of security. Killer idea, perfectly executed. With the right business model and embedded payment solutions, that's more possible than ever.

So, does every company need to be a fintech company? Probably not. But they do have to be 100% customer- and solution-driven. And whether they build, buy, lease — partner or go it alone — getting payments right should be a priority.

About Paysafe Group

Paysafe Limited (“Paysafe”) (NYSE: PSFE) (PSFE.WS) is a leading specialized payments platform. Its core purpose is to enable businesses and consumers to connect and transact seamlessly through industry-leading capabilities in payment processing, digital wallet, and online cash solutions. With over 20 years of online payment experience, an annualized transactional volume of over US $120 billion in 2021, and approximately 3,500 employees located in 10+ countries, Paysafe connects businesses and consumers across 100 payment types in over 40 currencies around the world. Delivered through an integrated platform, Paysafe solutions are geared toward mobile-initiated transactions, real-time analytics and the convergence between brick-and-mortar and online payments.

Further information is available at
www.paysafe.com

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