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Heard on the Street

Payments Firms Don't Get Enough Credit --- Stocks have been pressed while lenders have jumped, but investors might be missing a larger picture

By Telis Demos

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[Financial Analysis and Commentary]

Consumers use cards for two major purposes: Spending and borrowing. Investors right now seem more worried about the future for spending. But they might have it a bit backward.

Shares of companies that facilitate the spending side of cards -- networks like Visa and Mastercard, merchant acquirers like Fiserv and FIS and digital payments companies like PayPal and Square -- have widely fallen or underperformed the broader S&P 500 financial sector. PayPal has fallen 17% since lowering its expected full-year revenue growth earlier this month. Square is down 15% since it reported slowing revenue growth for its Cash App. Meanwhile, shares of major credit-card lenders, like Capital One Financial and Synchrony Financial, have widely outperformed financials or seen solid gains.

During the pandemic, many categories of spending surged, while borrowing fell off as households were flush with cash from stimulus checks and other sources. Investors may be expecting a natural reversion to the mean, with things cooling in payment volume while eventually picking up in borrowing. But there are reasons to continue to be relatively more optimistic about payment volume than lending volume.

A big source of concern for payment volume, as well as borrowing, has been cross-border travel. The return of this major spending category has been tough to predict precisely, and depends a lot on things like political decisions about when to open borders. But there is little yet to indicate that the overall desire to travel has diminished.

Already, the indication from borders that have been opened is positive: Visa has said that its spend volume for U.S.-Mexico travel in the most recent quarter was more than 60% above the 2019 level. Visa also recently said that if intra-European is included, then its planning assumption is that its overall cross-border travel will return to its 2019 level by the end of its next fiscal year. So as barriers in places like the Asia-Pacific region continue to loosen, and people become more willing to move around, travel spending could potentially surprise to the upside in the near term.

It also may be the case that future spending is more digital and card-heavy than in the past. Digital payments have grown as things like hand-held card readers become more commonplace in U.S. restaurants, and as more businesses shift to an e-commerce or "omnichannel" model.

Bernstein analyst Harshita Rawat has estimated that in the U.S. cards in 2021 may end up accounting for about 75% of consumer-to-business payments, up from about 70% in 2020. Cards' share usually grows each year, but this would be roughly twice the typical annual jump. Likewise, cards and card networks are being deployed in new realms, like in business payments, and when businesses pay out to consumers.

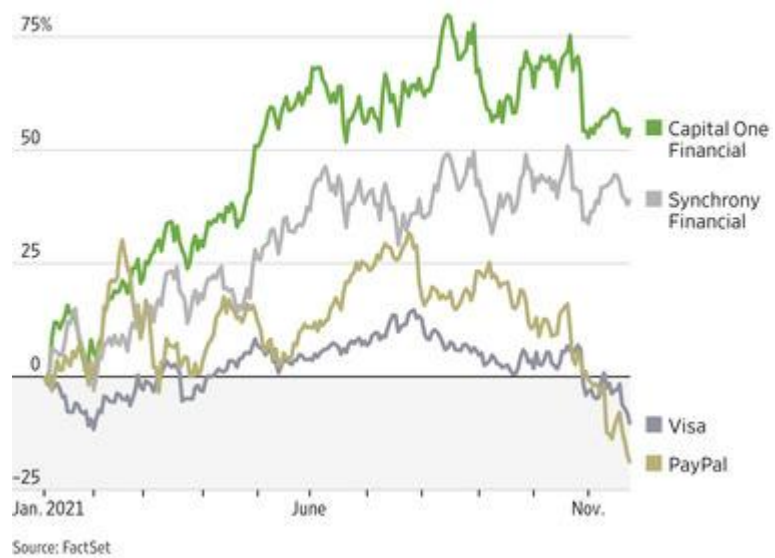
Then there is the case of "buy now, pay later" installment payments. Although shoppers often aren't entering a card number into an online cart when they click a button for Afterpay or another split-payment service, they are nonetheless frequently paying off those installments with a card -- or might use a card firm's infrastructure to facilitate the transaction. But consumers may be shifting their borrowing away from credit cards, even if they are still using a debit card to make payments.

Inflation also might be a positive for payment volume, versus something of a headwind to card borrowing. Higher prices can mean more payment volume. But while the conventional wisdom is that inflation favors borrowers, that isn't necessarily the case for floating-rate debt like credit cards if rates are also rising.

In general, consumer card borrowing balances will almost certainly pick up, while some spending volume growth has been pulled forward due to the pandemic. But the near-term opportunity set for card lending still might not be as good as the one for card payments.

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Share-price performance, year to date



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Lenders Find Dental Niche

By Orla McCaffrey

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Linda Stultz learned last fall that she needed a \$1,100 dental crown, but she didn't have the money.

So Ms. Stultz instead financed the treatment with CareCredit, a credit card offered by Synchrony Financial for healthcare and pet expenses. She first learned about the card from her veterinarian's office during a visit for her cat, Tinky.

Ms. Stultz, a 72-year-old retired social worker, has dental insurance through Medicare Advantage, but she can't find a local dentist who accepts it. She paid off the cost of the crown but used the card again this year for about \$700 of fillings. She has a balance of about \$580; if she doesn't pay it off by February, the bank will start charging about 27% interest.

Millions of Americans, including many who have dental insurance, have to take out personal loans or dig into slim savings to pay for dental care. Many forgo treatment altogether. A previous version of President Biden's proposed economic package would have given dental benefits to people on Medicare, but that measure was dropped from the pared-back version of the legislation.

Covid-19 turbocharged investors' interest in medicine broadly, and some lenders are betting that rising out-of-pocket costs for dental work will create a niche but lucrative financing market. CareCredit is a major player in the fractured field, but it accounts for about 2% of an estimated \$500 billion U.S. market for personal-health and pet-industry expenditures, according to Wolfe Research.

Some companies are tapping into the market with **buy-now-pay-later** offerings. Those plans let people pay for specific items in installment loans; lenders are often willing to approve borrowers who wouldn't qualify for credit cards.

One **buy-now-pay-later** lender, Sunbit, began by teaming up with auto-repair shops, giving customers the option to pay for brake repairs or new batteries in installments. The company says the dental-finance offering it added this year is its fastest-growing segment.

"There is a big difference between if you go to the dentist and need a loan or you go to the jewelry store in the mall and need a loan," Sunbit Chief Executive Officer Arad Levertov said. "One is nice to have, and one is something that you need."

That is another draw for lenders: People are less likely to default on healthcare purchases compared with travel or consumer goods, in part because they tend to have established relationships with their dentists or doctors, said Brian Shniderman, CEO of **buy-now-pay-later** lender Opy USA Inc. Opy started offering financing at healthcare providers and veterinary offices this year.

In July, Citizens Financial Group Inc. joined with patient-financing platform PrimaHealth Credit to offer **buy-now-pay-later** financing for dental work. The bank said it plans to expand into other healthcare offerings, including eye care.

Many patients first hear about the financing options through their doctor's or dentist's office and can apply on the spot.

Synchrony, a consumer lender based in Stamford, Conn., says CareCredit enables people to get treatment they might have skipped. CareCredit is offered at more than 250,000 locations, including nearly 116,000 dental offices.

Some dentists, vets and doctors prefer steering patients to CareCredit over setting up a payment plan directly with the office. That way, if a person stops paying, Synchrony is on the hook.

Most purchases are eligible for six to 24 months of interest-free payments. Synchrony says nearly 80% of customers pay off their balances in full before the interest-free period ends.

Ms. Stultz, who lives outside Chico, Calif., considered using CareCredit again when her dentist told her this summer that she needed another \$1,100 crown. But her card has a credit limit of \$1,500, and she used it to pay for the \$700 in fillings.

She opted for a cheaper filling that her dentist says is only a temporary fix. To make it last, she avoids sticky foods and chewing on her left side.

Ms. Stultz said she thought CareCredit was a miracle when she first heard about it, but now she is just worried about the bills coming due. She doesn't believe she will be able to pay off the card by February, when interest from the previous six months will be added to her unpaid balance.

Dental insurance typically covers far less than traditional medical insurance. Many plans will pay for only \$1,000 or \$2,000 of dental work in a year.

"Dental insurance is not true insurance in the sense that it protects you from catastrophic costs," said Marko Vujicic, chief economist of the American Dental Association's Health Policy Institute. "It's more of a prepaid benefit."

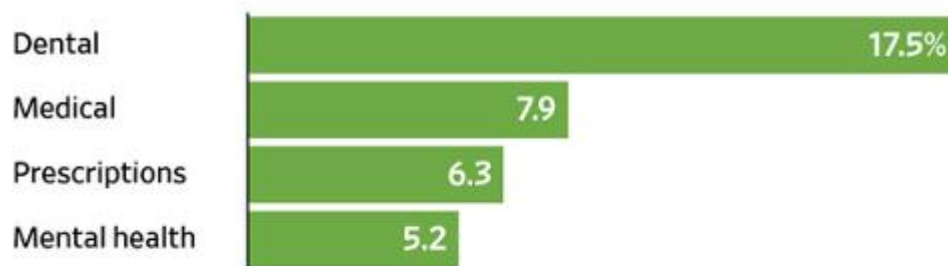
Last month, nearly 1,000 people filed through Pittsburgh's convention center for Mission of Mercy Pittsburgh, a free, two-day dental clinic. Organizers said in past years, about a third of attendees had dental insurance.

When Jerry Stephens needed major dental work last year, he and his wife, Carolyn, pulled \$6,000 from their IRA to pay for it.

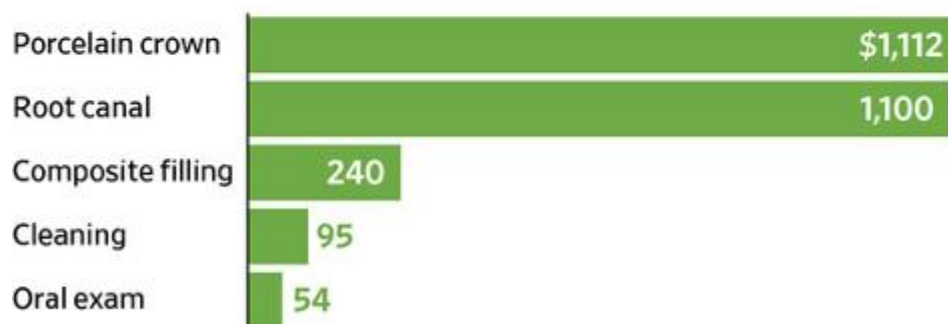
The couple, who live outside Las Vegas, have dental insurance, but it covered only a small portion. This year, the dentist told Ms. Stephens, 77, that she needed \$3,000 of work. For now, it isn't in the couple's budget.

"At my age," she said, "I have to get a good return on investment on this money."

Share of adults skipping care because of cost within the previous 12 months, 2020



Median cost of dental treatments, 2020*



*Figures represent full procedure cost before insurance is applied.

Procedure fees can vary based on the tooth, number of surfaces and materials used.

Sources: American Dental Association Health Policy Institute analysis of the National Health Interview Survey (share of adults); American Dental Association (treatment cost)

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