Why We Find Digital Payments Compelling

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As a consumer, you may not spend much time thinking about the series of connections and interactions that take place within a few seconds after you swipe your credit card, click “complete purchase” on a screen, or tap your smartphone on a sensor.

But what goes on behind the scenes is changing the world, and is even more important as individuals further embrace all things digital in the wake of the COVID-19 pandemic.

But as investors who are focused on finding opportunities for sustainable value creation for our clients, we believe that what goes on behind the scenes comprises a compelling opportunity that deserves attention.

When we find an industry that is experiencing double-digit growth driven by clear, long-term secular trends, with high profit margins and a potential market size of $30 trillion (or more), our interest is piqued, to put it mildly.

The shift from cash to noncash payments around the world—while occurring at different rates and in different forms—is indisputable. And it underpins what we believe is a unique growth opportunity.

This trend is supported by secular shifts that include the growth in e-commerce, as well as services, such as ridesharing and buying tickets to a concert on the secondary market, that are made possible by the ubiquity of cellphones.

Although earnings multiples for many global payments companies are high, we believe those multiples are warranted based on the exceptional outlook for growth that we feel is durable and still underappreciated. We also believe that concerns about “disruption risk” in the industry are largely overstated.

We think the total potential market for the payments industry is more than $30 trillion in volume,[1] and that is a conservative estimate based only on the business-to-consumer (B2C) market. If the untapped potential of the business-to-business (B2B) market is viewed as a “free” option for investors, the growth opportunity is nothing short of staggering.

Moreover, the global payments industry is both highly complex and highly attractive, with growth opportunities and risks that differ by segments within the industry and by geography.

This complexity creates opportunities for us as disciplined, fundamental managers to identify the aspects of the value chain that are best positioned to capitalize on the growing and shifting pools of profitability across payments.

Within each segment, our rigorous, bottom-up approach—which focuses on aspects such as return on invested capital and a company’s ability to use its excess cash flow to drive growth and strengthen its competitive advantage—can help us to identify the companies with the potential to outperform over the long term.

We created this blog series to explain why we believe that opportunities in the payments industry are so compelling. After reading it, we think you will have a new appreciation for how much value and investment opportunity is being created each time you—and billions of fellow consumers around the world—make a purchase in the rapidly expanding noncash economy.

In our next post, we will discuss one aspect of the payments industry that makes the investment opportunity particularly compelling for fundamental managers: the fact that the industry represents a truly enormous addressable market that continues to expand due to strong, durable secular tailwinds.

Digital Payments Series

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Part 2: 5 Factors Driving Digital Payments Growth
Part 3: Disruption and Growth in Digital Payments
Part 4: Follow the Money in Digital Payments
Part 5: More Competition for Merchant Acquirers
Part 6: Digital Payments Issuers Face Regulatory Risk
Part 7: Networks: The Rails That Connect Digital Payments

[1] PayPal. 2018.

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