What Does the Future of Checks Look Like?

WHITE PAPER
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Paper check volumes have been declining for the past two decades. The number of paper checks written has fallen by more than half since 2001. None of this is news, and no one is predicting a reversal of the trend. However, that’s largely where the consensus ends. Opinions differ on both the forward trajectory and the likely endgame.

Through this report, we hope to address frequently asked questions about ongoing check usage through an objective, data-driven approach.

The 20 Billion Checks of 2015 – and the People that Still Write Them

The authoritative source for US payments data is the Federal Reserve Payments Study, which was initiated in 2000 and has since been conducted every three years. The Federal Reserve’s quantitative research provides a dispassionate, detailed snapshot of historical industry trends.

The Federal Reserve’s research disproves the notion that “the check is no longer relevant in 2015.” Roughly 20 billion checks continue to be written each year, conveying over $22 trillion in value – second only to the ACH network among all payment instruments. By comparison, credit and debit cards support $3 trillion and $2 trillion of value, respectively. Despite ongoing declines, checks remain an integral component in the overall US payments mix.
Breaking Down Checks by Payment Type

Another common view that bears closer scrutiny is that the decline of checks is accelerating. Based on Federal Reserve data, check volumes have been falling at a steady rate of 2 billion items per year for at least a decade. If viewed in percentage terms, this can appear to be an accelerating pace given the shrinking denominator.

McKinsey & Company projects that the rate of check decline will slow slightly in the coming years. In order to appreciate the logic behind such a stance, it’s important to disaggregate the drivers of US check usage, each of which carries its own set of dynamics.

Consumer to Business Payments.

Payments from consumers to businesses (C2B) remain the most common use case for checks, comprising over 40 percent of checks written. This is also the segment that has experienced the most rapid rate of check decline.

Delving further into the numbers, one sees a dramatic reduction in check use at the point of sale (POS) from 4.4 billion items in 2006 to 1.0 billion in 2012. This drop coincides with the widespread availability and adoption of debit/credit cards at grocery stores, those businesses whose low margins were once thought unable to absorb interchange fees. Excluding POS payments, C2B declines averaged 7.3 percent from 2006-2012, well below the 10.0 percent overall C2B rate.
Business to Business Payments

The rate of decline for Business to Business (B2B) checks is notably lower than C2B, for a series of logical reasons. In both groups, check use at the point of sale declined at a higher rate. POS transactions comprise a greater share of C2B activity, however. And on the bill/invoice payment side, B2B migration from paper has been slow, averaging only 2.2 percent annually since 2006.

B2B payees have a stronger motivation to avoid cards – average transaction values are larger, translating to higher interchange levies for card payments. ACH payments can be problematic given the need to convey more complex information (e.g., discounts taken, invoices covered, line item deductions) along with the payment.

Finally, legacy accounting systems and the desire to maintain audit trails often favor check use among both business payors as well as payees. As the second largest check category (nearly one-third of checks written), B2B’s overall sub-four percent decline continues to dampen overall check reductions.

Business to Consumer Payments

Business to Consumer (B2C) payments were the first to experience wholesale migration to electronic form. Payroll direct deposit was the foundation for the 1970s rollout of the ACH network, and the vast majority of these paper paychecks were eliminated decades ago.
Recently the B2C category has undergone another drop in volume (15 percent annually between 2009 and 2012), as payroll cards made a dent in the remaining base of non-direct deposit payroll transactions. More importantly, during this time consumer incentive rebates migrated from paper checks to prepaid cards. The B2C category, comprising 3 billion annual items (15 percent of check volume), appears poised for further double-digit declines as businesses continue to promote the use of payroll and incentive gift cards.

**Consumer to Consumer Payments**

The smallest of the four categories, Consumer to Consumer (C2C) payments have proven the slowest to migrate to electronic channels. The 2.1 billion transactions measured by the Federal Reserve in 2012 (10 percent of checks written) were essentially unchanged from six years earlier.

Well publicized electronic alternatives have existed for some time (PayPal, Venmo, PopMoney) and have achieved varying degrees of success. However, there appears to be a steady base of consumers who, when faced with certain types of events – a birthday gift or paying a neighborhood teen for yard work – continue to regard paper checks as an effective solution.

It’s worth noting that recent advancements by Apple Pay and digital wallets are better suited to displace existing card (and to a lesser extent, cash) payments, rather than checks.
External Forces Aren’t Affecting Checks As Much As Expected

It’s important to note that technologies have existed to supplant check usage for some time. Yet checks have endured and actually exceeded the expectations of many analysts. History has shown that no one solution or group of solutions is going to completely eliminate the demand for checks. Clearly customer segmentation and perceived benefits play a role. A 2009 working paper by the Federal Reserve Bank of Boston concluded that while demographic characteristics, such as age, factor into payment decisions, more highly correlated factors include the acceptance and appeal of features for alternative payment products. In other words, while younger consumers write fewer checks they will still use them for some form of payments including C2C and C2B when they feel its expedient.

Likewise, we are highly unlikely to see a groundswell of merchants refusing to accept checks – particularly in the bill payment arena. Empirical evidence has demonstrated that despite a desire to reduce payment acceptance costs, merchants prioritize the ability to transact in whatever fashion a consumer wishes to pay, rather than risk alienating customers. And notably, the merchant cost of check acceptance remains well below that of cards.

So what is the enduring appeal of paper checks? Payment alternatives rising in dominance are not likely to poach any more activity from checks.
1. Accepted almost everywhere - Checks’ ubiquity remains a core advantage. While retailers have demonstrated a willingness to support new payment forms which generate far lower volumes than checks, absent an industry-wide mandate, financial institutions are highly unlikely to disadvantage themselves competitively by ceasing check support. Banks’ recent investment in marketing remote deposit capture is evidence of this.

2. Minimal cost to merchant to accept or cash - Given the ongoing merchant battles to minimize cost of acceptance, it’s important to note that checks carry no merchant discount. The limited remaining back office processing cost will be difficult to eliminate until all check AND cash volume is fully eradicated - an unlikely proposition.

3. Proof of payment/receipt - The value consumers place on this feature is validated by the increasing demand for “duplicate” check stock. It remains easier to retrieve an image of a paid check to confirm both receipt and purpose of payment than it is to accomplish the same task for a card or ACH payment. This benefit is even more powerful for business checks, as noted below.

4. Audit trail/records - A key reason that business check volumes have proven more resilient than consumer checks. Business payors continue to prefer the approval documentation and detailed remittance explanations (which are often more complex than for consumers) provided by a paper trail. Automated workflow alternatives have existed for years, but behavior indicates that businesses do not perceive sufficient value to justify the effort to switch.
Checks Remain in the Mix Through 2030 and Beyond

As any savvy investor knows, past history does not guarantee future performance. The Federal Reserve does not offer forward projections of payment trends. By extrapolating current trends at a detailed level (assessing each of eight payment categories separately, e.g., C2B point of sale vs. B2B bill payment) Deluxe has created its own estimates of future check volumes.

Our analysis foresees nearly 12 billion checks being written in 2020, and over 6 billion in 2030. Although developed entirely independently, Deluxe’s projections are quite similar to two other known sources. McKinsey & Company’s Payments Map forecast extends through 2019, showing slightly lower check volume than Deluxe. A 2015 white paper issued by Digital Check Corp. (a leading manufacturer of check scanners) offers three check scenarios through 2030 – two of them tracking closely to Deluxe’s.

One interesting side note is that we see B2B check volumes matching C2B by 2020-2021 due to the steeper decline of C2B payments. Overall, consumers will continue to write nominally more checks than businesses, however, thanks to relatively stable C2C volumes.

While such forecasts are an inexact science, a few predictions seem safe. The number of check writers will decline at a slower pace than the number of checks written. While many have blamed the decline on new checking accounts being opened without checkbooks, the Federal Reserve Bank of Boston’s research indicates that the greater impact is from a decline in the number of checks written per active household.
Attempts to Fully Retire Checks Rarely End Well

Absent some major unforeseen event, the volume of US checks written will remain non-zero, as there is no precedent for a country fully retiring checks without a firm government mandate. The only literal examples of complete retirement are Sweden and the Netherlands, where checks had always played a secondary role in the payments system. Yet banks, even in these countries, remain capable of processing checks and there is still some limited usage even in these countries.

More relevant is the UK experience, where in 2009 the British government issued a mandate to eliminate checks by 2018. As deadlines for the first tangible actions approached, however, consumer groups registered strong opposition and the mandate was rescinded – while check elimination remains a policy goal, there is no longer a target date attached.

EXTERNAL FORCES THAT DROVE REDUCTIONS IN CHECK USAGE

- Payroll direct deposit (1983-1988)
- Cards at grocery stores (1995-2000)
- Cash back at the point of sale (2003-2006)
Conclusions

Hopefully our analysis has helped demystify the underlying drivers of US check trends. Some key takeaways:

• There are still roughly 20 billion checks written in the US each year, conveying over $22 trillion in value - more than any payment instrument other than the ACH

• Trends vary by usage (C2B, B2B, POS, bill payment, etc.) and must be evaluated separately to gain a firm understanding of check trends

• Alternatives have existed for some time to eliminate all remaining check usage - it’s customer preference/demand that drives their persistence

• The number of checks written will decline more rapidly than the number of check writers

• The only countries to have fully retired checks 1) never relied on them to the same extent as the US, and 2) issued some form of governmental mandate to complete the process

• Projections developed independently by Deluxe and other industry experts estimate roughly 12 billion checks remaining in 2020, and 6 billion by 2030
About Deluxe

Since 1915, Deluxe has been working hard as a partner for financial institutions to drive deeper customer engagement and more profitable revenue. As the financial services industry has evolved, Deluxe has been an active participant in shaping it—with the calm assurance of a company that has done it before.

Today, thanks to collaboration, innovation, and acquisition, Deluxe has an ever-growing portfolio of retail and commercial banking FinTech solutions focused on helping our clients manage the customer lifecycle—acquire, onboard, engage, and operate. Our growing array of inventive, client-inspired solutions are designed to help our clients grow in a changing, competitive landscape:

• Data and Analytics
• Digital Channels
• Marketing Services
• Performance Management
• Rewards and Loyalty
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