Real and Virtual
From e-commerce to m-commerce to f-commerce

by

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Payments are being changed forever as we go online. Games and social networks are giving us some clues as to what the future holds, but it helps to understand history too.

I said a few years ago that not only were virtual worlds going to be big business, but that they would have an impact on the payments market. I used to put things like World of Warcraft into discussions with our financial services clients and I'm sure they thought I was doing it just for fun, just to get some discussion going. But having played around in the space, I could see it would lead to some new thinking. When you're sending World of Warcraft gold to a friend in Asia via an elven intermediary (quicker and cheaper than banks, by the way) you can't help but wonder at the "real world" instruments to hand. It's been clear for some time that such instruments are not perfectly suited to virtual commerce[1]. A typical virtual goods store probably saw a completion rate of less than 1% on payment cards.

You can see why. People playing at being virtual farmers want to buy some virtual cows, so they click to buy, but when they see a credit card payment screen, they can't be bothered. So there was a demand for a new kind of payment instrument that was not being met by the banks. Look how much things have changed since then, with the incredible boom in app store and in-game payments. There's no doubt that the retail payments roadmap is indeed being affected by the world of games.

Now I'm not implying that it's only payments that will be impacted, because in the longer run it will be many kinds of financial service, including banking. Here we have already seen early experiments, starting when the publisher of the online science-fiction game *Entropia Universe*, set on the planet *Calypso*, received a banking license from the Swedish Financial Supervisory Authority. Their players were already exchanging real money for a virtual currency. And virtual money they make in the game, through hunting, mining, trading or other activities, can be cashed out into real money. Why bother? Well, it's a selling point to customers: by setting

[1] http://blog.zong.com/2008/10/25/virtual-goods-currency-and-mobile-payments-the-business-model-for-social-apps/

up a real-world bank, Sweden-based publisher MindArk PE AB gained the protection of the Swedish government's deposit insurance for these accounts, up to about $60,000 for each customer.

Of course, you don't need to be a bank to create electronic money and handle payments because the rules have changed (in Europe at least). There are more than a hundred organisations (such as mobile operators) who have already obtained Payment Institution (PI) licences or Electronic Money Institution (ELMI) licences to run new payment systems for themselves. In the UK, Telefonica is to obtain such licences for it's new "O2 Money" service and I wonder how long it will be before games and virtual world developers go down the same route.

If they don't, what will happen? Facebook and Google and others have already begun to develop micropayments, virtual currencies and marketplaces and people have already begun to wonder if there might be something big going on. US Banker[2] asked whether Facebook and Google were poised to challenge the banking industry in online payments. I said at the time that I couldn't see any reason why Facebook or Google would want to be a bank, unless it was to get some sort of government handout, but I could see why they might want to get involved in payments.

Crucially, this was not in order to make money from the payments, where profit margins are thin, but from new products and services that have payments integral to them. Since then we have seen Facebook Credits for sale in shops, a billion dollar virtual goods market on top of them (the so-called "f-commerce") and a multi-billion dollar valuation[3] for Zynga, the company behind Farmville and Mafia Wars. We are seeing some fascinating interchanges across the ever-more-fuzzy boundary between real and virtual, such as the canned vegetable company Green Giant offering FarmVille currency as reward points[4].

So will Facebook Credits take over from dollars one day? No less a journal of record than *The Economist* noted[5] that Facebook has tried to guide the development of its online economy almost in the way that governments seek to influence economic activity in the real world, through fiscal and monetary policy. Earlier this year the firm said it wanted applications running on its platform to accept its virtual currency, known as Facebook Credits. It argued that this was in the interests of Facebook users, who would no longer have to use different online currencies for different applications.

This comes from the Great Khan's playbook for monetary and fiscal policy. In 1260, Kublai Khan became Emporer of China. He decided, much as Mark Zuckerberg has,

[2] http://www.americanbanker.com/magazine/121_5/facebook-and-google-encroach-on-banks-turf-1036012-1.html
[3] http://www.cnbc.com/id/43564083/Zynga_IPO_Implies_a_15_20_Billion_Valuation
[4] http://www.businessinsider.com/zynga-is-giving-away-free-farmville-cash-with-purchases-of-real-life-vegetables-2010-5
[5] http://www.economist.com/research/articlesBySubject/PrinterFriendly.cfm?story_id=16646000

that it was a burden to commerce and taxation to have all sorts of currencies in use, ranging from copper "cash" to iron bars, to pearls to salt to specie, so he decided to implement a paper currency.

His monetary policy was refreshingly straightforward and more robust, even, than Mr. Zuckerberg's: if you didn't accept his money, he would kill you. Naturally, in a short time, the new single currency was established and paper money began to circulate instead of gold, jewels, copper coins and metal bars. If you think talking about a new currency is crazy, take a look at "Facebook Deals". According to Facebook, at launch, you will not be able to buy physical goods with Facebook Credits. Rather you will be able to get things like vouchers that you can redeem at events, which seems to me a paper-thin distinction. I can't use Facebook Credits to pay for, say, a Coke at a pop concert but I can use them to pay for a voucher for a Coke at a pop concert... I am not an economist, but[6]... "when beloved national retailers start offering goods and lower prices to customers who pay with a new, virtual currency... Somebody call Congress and the Federal Reserve, it's time to start having some serious conversations."

There's a warning from history here! The Khan's paper money ended in disaster because the money supply was not managed: it collapsed in hyperinflation, because the temptation to print money was just too great for the monetary authorities too resist! Just as China turned in on itself and stagnated, leaving technological and commercial progress to other people, maybe Facebook will become an inward-looking economy while others take up the torch!

We need competition in money and payment to keep commerce vital and evolving and games are a great place for competition and experiment. Let's start taking them seriously.

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[6] http://www.readwriteweb.com/archives/facebook_deals_launches_tonight_groupon_doesnt_sta.php