Low-income consumers in the United States and Canada pay the highest net transaction costs as a percentage of their purchases.

Using data from the United States and Canada, we quantify consumers’ net pecuniary cost of using cash, credit cards, and debit cards for purchases across income cohorts. The net cost includes fees paid to financial institutions, rewards received from credit or debit card issuers, and the higher retail prices passed on to consumers to cover merchants’ payment processing costs. Even though credit cards are more expensive for merchants to accept compared with other payment methods, merchants typically do not differentiate prices at checkout but instead pass through their costs to all consumers. As a result, credit card transactions are cross-subsidized by cheaper debit and cash payments. Card rewards and consumer fees paid to financial institutions are additional sources of cross-subsidies. We find that consumers in the lowest-income cohort pay the highest net pecuniary cost as a percentage of transaction value, while consumers in the highest-income cohort pay the lowest net cost. This result is robust under various scenarios and assumptions, suggesting payment card pricing and merchant cost pass-through have regressive distributional effects in the United States and Canada.

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Article Citations

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