

## Comparison and Choice of Mainstream Payment Methods for Small Amount Cross-border Trade

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**Abstract:** The rise of Internet+ has brought a revolution to China's traditional cross-border transactions under which we can witness more and more cross-border micropayments. Small amount cross-border trades have gradually become a new economic engine for China. However, payment methods commonly used in traditional foreign trade like collection and letter of credit has many inelasticity with micropayment transactions due to complex procedures and long money collection periods etc. This article introduces three current mainstream methods for cross-border micropayments by comparing them from operation procedures, costs and risks including Western Union, PayPal and T/T, aiming to provide implications for our small amount cross-border transactions in the choice and application of payment methods.

### Mainstream Payment Methods for Small Amount Cross-border Trade

**Paypal.** Paypal, born in America in 1998, now is frequently used in cross-border online transaction. Either corporates or individuals can register as Paypal members through emails so that the buyer can make instant payment and the seller can receive the payment without any delay. As a global payment platform, Paypal now has more than 270 million active accounts which distributes in more than 200 countries in the world. Paypal clients can use more than 100 kinds of currencies. Almost 70% online cross-border buyers prefer to pay by Paypal. It usually is much more applicable for small orders or sample orders.

PayPal uses e-mail to realize online payment, which effectively reduces the insecurity and inconvenience brought by traditional mail or remittance. At the same time, PayPal guarantees the interests of both buyers and sellers to the greatest extent. For example, for buyers, PayPal will compensate for losses in case an accident occurs, as long as the transaction meets the conditions of Buyer Protection provided by PayPal. Also the seller no longer has to worry about receiving "unauthorized payment" or the buyer claims "never received the item". The advanced management functions integrated in PayPal account can help clients track the details of each transaction easily and protect the rights and interests of buyers and sellers. Because of its good reputation, PayPal has a very high usage rate in Europe and the United States. It can even be said to be the representative of online payment companies worldwide. In China, PayPal has started business cooperation with UnionPay and AliExpress.

**Western Union.** As a financial service company with a history of more than 150 years, Western Union provides express money transfer services through digital, mobile, and retail channels, with an array of convenient pay-out options to meet business and consumer needs. By now, it has over 550 thousand agent locations around the globe in over 200 countries and territories. Its consumers and business clients can transact in nearly 130 currencies.

Thanks to its extensive powerful online network, global remitters and recipients can manage international payments simply, effectively and efficiently by using western union's 24/7 global financial network to transact, often on a same-day basis[4]. ALL withdrawals are free but Western Union may charge processing fees. Its security is mainly reflected in the seller receiving money before delivery, which is most beneficial to the seller and relatively acceptable to customers in Europe and the United States.

**T/T (telegraphic transfer).** T/T is widely used in traditional foreign trade because of its fast speed and easy operations. Under T/T, the remitter first submits the application to the bank for remittance and pays the fee to the bank. Then the bank sends money through telegram or telex. After receiving T/T notice from the remitting bank, the payee shall go to the bank and get the payments. Telegraphic transfer is the fastest way of remittance. Usually banks handle the remittance business on a same day basis without occupying remitter's funds. However, additional charges for telegraphic might need to be collected on remitter's account. Telegraphic transfer can be divided into pre-T/T (prepayment) and post-T/T (payment after delivery of goods). Transaction risk is higher than letter of credit, but the handling fees paid to the bank is far lower than the cost of using letter of credit. There is no minimum limit for money transfer however a ceiling is set for each transfer. Therefore, telegraphic transfer is much more suitable for small amount of remittance[5].

### **A Comprehensive Comparison among Mainstream Payment Methods for Small Amount Cross-border Trade**

The choice of cross-border payment methods generally follows the principle of "easy to operate, fast to transfer with low cost". In the next paragraphs, costs, Risk and conveniences of three main payment methods for small amount cross border transaction are described and compared.

**Costs.** Service fees, transaction fees, and cash fees are a bit much for small amount Cross-border orders. Transfer through PayPal requires no service fees. If payment is made in other currencies, only small exchange fees are required. If merchants often collect money through PayPal, they can also get more tools and discount prices from PayPal[6]. Transaction only needs to be charged when the order ends. The higher the monthly sales, the lower the payment rate (3.4%-4.4%).

In addition, PayPal customers also have to pay a fee if they need to withdraw money, which are affected by different withdrawal methods and currencies. It also affects handling fees. For example, each telegraphic transfer to a bank account in mainland China would require 35 US dollars service fees. 5 US dollars service fees are needed for each transaction paid by cheque. Therefore, small multiple withdrawals for PayPal customers are uneconomic.

In the case of Western Union remittance, the handling fees shall be borne by the buyer, while the Seller shall not have to pay any additional fees. Western Union fees vary according to the amount of money. The higher the amount of remittance, the higher the handling fees. For each remittance less than 500 US dollars, the handling fees are 15 US dollars; for transaction of 500 US dollars, it is 20 US dollars. Additional 20 US dollars are required for every increase of 500 US dollars if the overall payment is over 10,000 US dollars. Clients with transactions below 10,000 US dollars can choose either PayPal or Western Union. Western Union makes it ever more cheap for remittance over 10,000 US dollars. The use of telegraphic remittance will result in handling fees, which vary according to the rates charged by different banks. Buyers and sellers can decide which party will bear the handling fee on their own, which is more flexible. In addition to handling fees, telegraphic transfer may also require a certain amount of telegraphic fees.

**Risks.** Network security and credit issues have always been an unavoidable pain point in the development of e-commerce. Fraud widely exists in international trade micro-payment, and the withdrawal rate and dispute rate are very high [7]. At the same time, compared with traditional stores, the quality of goods traded online is difficult to be guaranteed, and a perfect credit system is needed to ensure the normal conduct of transactions. As the third-party payment platform with the highest application rate in the world, PayPal provides users with anti-fraud checklist and buyer and seller

protection. PayPal guarantees sellers against unauthorized payments, withdrawal of payments due to fraud and non-receipt of compensation applications for items as long as the transaction meets the requirements. For the buyer, if the order has not been delivered or does not conform to the description, a compensation application can be filed within 180 days. But using PayPal is still risky. If PayPal supports the buyer to withdraw within six months after using the platform for payment, it will increase the risk that the seller's account will be frozen. As the world's leading remittance company, its global secure electronic system ensures the security of each remittance and has operating passwords for customers to verify, so that remittances can be safely delivered to designated recipients. Western Union adopts the mode of payment before delivery, and the payment time is very short, which belongs to a payment method to protect sellers. On the contrary, its shortcomings are also very obvious. Because of its requirement of payment before delivery and its fast arrival time, the buyer usually finds that the money has been withdrawn when he is cheated. And the bank is not responsible for any responsibility, and is not responsible for verifying the authenticity of the certificate. As a result, many buyers do not trust this trading model, which is very detrimental to the development of new customers.

Telegraphic T/T refers to the way in which the remitting bank pays a certain amount of money to the remittee by sending a pressurized telegram, telex or SWIFT. As a common method of payment in international trade, telegraphic transfer has the advantages of fast speed, high safety factor and much lower cost than letter of credit. But risks still exist. There are three kinds of applications for telegraphic transfer in actual business: advance payment, cash on delivery and pre-Telegraphic plus post-Telegraphic transfer. Advance payment, also known as pre-T/T, means that the seller arranges the production of goods only after receiving full payment, which is much favorable for the seller. However, this settlement method bases whether the seller would dispatch the goods or not totally on the seller's own credibility, which might cause great loss for the buyer. So it is difficult for the buyer to accept this practice, usually only suitable for small trade. Payment on delivery, also known as post-T/T, means that the seller first arranges the production and delivery of the goods, and then receives the payment after the arrival of the goods. Obviously, this practice is quite unfavorable to the seller. It is better to stipulate in the contract the time for the customer to raise quality disputes or to make the latest payment, usually suitable for regular customers. Whether advance payment or on-livery, these two methods will completely put the risk on one side, which is obviously not conducive to the conclusion of the transaction. Therefore, a method of discount is derived, that is, before T + after T. Usually, the buyer pays a certain proportion of deposit first, the seller arranges production and delivery, and the buyer pays the balance time and conditions as follows. The buyer can pay the balance within a few days after the delivery of the goods. In this way, the seller still faces the risk that the customer will only take delivery of the goods without paying the balance. Therefore, the seller should use this method carefully. The risk of the seller's payment can also be reduced by stipulating in the contract that the buyer pays the balance against a copy of the seller's bill of lading.

Although there are risks, pre-T/T is already an international trade practice which is quite common for small orders. No matter what payment method is adopted, it is hard to avoid all risks. Effective risk avoidance can be achieved through adequate communication and understanding before order. Clients can choose a payment method suitable for them according to their own needs and risk assessments.

**Convenience.** Convenience is also one of the important factors affecting merchants' choice of payment methods. Convenience not only refers to the rapid arrival of transfer, but also has certain requirements for the simplicity of the procedures for collecting remittances. Small cross-border merchants usually require high liquidity of funds, and a slightly slow settlement rate may affect their overall operation. PayPal accounts can be used to collect money in a timely manner, but it takes some time to withdraw it from PayPal accounts. For example, you can withdraw dollars from PayPal accounts by wire transfer checks. It takes about three to seven working days for a wire transfer to a domestic bank, and about six weeks for a check[8]. In addition, withdrawal from PayPal accounts is limited to \$50,000 a year, and there is a risk that the accounts will be temporarily frozen. Among the three payment modes, remittance through Western Union is the fastest. It can usually receive the

remittance in a few minutes, which is conducive to the turnover of funds. However, the single amount of the Western Union remittance in US dollars can be up to US\$20,000 . Among the three payment modes, PayPal is an online payment mode. Both parties need to register their accounts by e-mail. It is easy to operate, but the withdrawal needs certain operation and time. Western Union remittances and wire transfers are offline payment methods. Among them, the Western Union remittance requires both parties to provide personal information. Remitters need to fill in the application for remittance, and recipients need to bring personal documents to the bank to collect money. China's major commercial banks provide Western Union remittance services, requiring remitters to use debit card account. For the first operation, it is necessary to register personal information, maintain the receipt and loan information and fill in the remittance information. If the transfer information is correct, the other party will receive the remittance within 1 to 3 working days.

### **Suggestions on the Choice of Mainstream Cross-border Trade Payment**

Since entering the Internet + era, the trend of fragmentation of foreign trade business orders is obvious [9]. Many cross-border e-commerce enterprises in China are mainly small and medium-sized enterprises, which deal with small orders frequently. However, due to the lack of experience, limited funds and low risk resistance, they have higher requirements for cross-border payment methods. Choosing an appropriate payment method is directly related to their vital interests. Cross-border businesses should choose their own cross-border payment methods according to their own business practices.

**Choose Mainstream Cross-border Payment Methods.** Nowadays, the cross-border payment market provides a variety of payment methods with uneven quality. Cross-border enterprises should focus on the choice of mainstream payment methods, such as PayPal, Western Union and T/T. These payment methods occupy the vast majority of the market, and after a long period of market baptism, their security and reliability are strong. Each payment method has its own advantages and disadvantages. According to the above comparative analysis, enterprises can choose from several aspects such as cost, convenience and risk according to the actual situation.

**Be Familiar with Operations of Cross-border Payment and Clauses.** Different cross-border payment methods have different operation processes. Understanding the platform rules and continually learning the safety payment terms can effectively avoid payment disputes caused by improper operation and intellectual property rights. In the use of payment methods, especially online payment methods, it is easy for businesses to ignore the rules and protocols of the platform, thus resulting in losses. For example, the massive freezing of Chinese sellers' accounts by PayPal in 2015 has left many cross-border businesses still shocked. At that time, PayPal accounts of a large number of Chinese merchants were frozen or even liquidated because customers in the United States sued products for infringement of intellectual property rights of American companies. However, due to the lack of legal awareness and the high cost of litigation in the United States, these merchants chose to remain silent, and Chinese merchants suffered heavy losses. The incident has also sounded an alarm for Chinese businesses. The solution to avoid such risks is to establish legal awareness, understand the rules of payment platform and focus on improving product quality.

**Choose payment method according to customer preference.** Business and personals in different parts of the world have different payment preferences and habits. In order to expand sales and facilitate transactions, cross-border merchants should choose payment methods suitable for customers according to the consumption habits of different regions, and use various payment tools when necessary with an aim to reduce the risk of cross-border payment [11]. This requires either business or personals to know the customer's background and payment preferences in the country or region where the customer is located. For example, customers in Europe and America prefer PayPal as a payment method. At the same time, due to the perfect credit system in Europe and the United States, online payment by credit card is also very common. For less developed areas such as Africa, the overall development of cross-border e-commerce is backward, and the development of cross-border payment is also limited, so they prefer to use traditional payment methods such as T/T.

## Conclusion

In today's complex global economic situation and foreign trade and export environment, small and medium-sized cross-border e-commerce enterprises need to choose their own cross-border payment methods according to their own business practices. Each payment method has its advantages and disadvantages. Only through comprehensive consideration, skilled operation process and effective risk avoidance can we better promote the completion of the transaction. With the further improvement of cross-border e-commerce market rules, payment methods will become more mature and standardized.

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