

Paying with Cards

Enter a store in the United States. Any store. You will find logos on the products sold in the store. Some logos will be familiar and others will not. The brands will be appropriate to the store: you will find a Nike swoosh in a shoe store but not in a bookshop, and the Kellogg tiger will beckon to you in a grocery but not in a hardware store. There are, however, two logos that will show up in all of these outlets. One will be a four-letter word written in blue italics on a white background, the first letter sporting an orange splash: *VISA*. The other will feature a Venn diagram of two overlapping circles—one fire-truck red, the other mustard yellow—across which is written, as you might have guessed by now, a compound word with an uppercase *C* in the middle: *MasterCard*.

Now go to a foreign country. Any country. You will find the same two logos almost everywhere, from Shanghai to St. Petersburg, Sofia, Szczecin, and Székesfehérvár. The further you stray from the beaten path of globalization, the fewer of these two logos you will encounter, but you will be sur-

prised to find them occasionally even in small, rural villages in the poorest regions of the world. Though far from everyone in countries like Hungary or Ukraine will use those two logos, almost everyone will recognize them.

Today, Visa and MasterCard, together with smaller brands such as Diners Club, American Express and Discover, stand with Coke, McDonald's, Microsoft and others as universally recognized brands. Credit cards are the epitome and a protagonist of globalization. As a new form of payment, they embody the effortless and instantaneous flow of money, in the form of information, from anywhere to anywhere else in the world. Cards tear down national boundaries by allowing travelers to pay easily, without the burden of having to carry wads of cash and to exchange one kind of currency for another. Today, traveling without a credit card turns simple transactions such as plane and hotel reservations into unduly cumbersome chores. Cards also make long-distance purchases possible. Without cards, the Internet, the most global of institutions, would never have been able to turn into a global retail marketplace. The global nature of commerce demanded a global payment system, and the large credit card companies built their own worldwide web of authorization and processing, linking souvenir shops and banks all over the world.

It is not just Western cardholders whose convenience is served by the way the credit card weaves the world into a global bazaar. Lives in the rest of the world are also profoundly affected. Globalization expands the reach of credit card markets to the less affluent parts of the world, to places where those markets had not existed earlier—in the process transforming local populations into card-carrying consumers. In this book, we trace the course of this transformation and the paths that emerging card markets carved in Bulgaria, China, the Czech Republic, Hungary, Poland, Russia, Ukraine and Vietnam. Our story is not, however, a straightforward account of globalization. We demonstrate that despite the overwhelming similarities around the world in the appearance of credit cards (small rectangular pieces of plastic proportioned according to the golden ratio,¹ with a magnetic stripe on the back exactly 0.223 inches from the upper edge, and sometimes a small embedded computer chip), and despite the undeniable ambitions of multinational card companies to present cards as a standard, “McDonaldized” product, postcommunist card markets neither developed according to a single “Western” blueprint nor proceeded in identical “postcommunist” ways in all of the eight countries.

*Credit Card's Dual Role:
Both Payment Mechanism and Instrument of Credit*

The credit card stands at the intersection of two momentous changes in the world economy. As a means of payment, the card is replacing cash as well as checks (where they previously existed) with a piece of plastic and the digital flow of information. The most recent step in a long historical progression from beads and shells to gold coins and paper money, the payment card makes the link between value and its material vessel even more attenuated.² At the same time, the credit card is also an instrument of accessing consumer credit. As such, it allows people to use money they do not yet have to buy goods now and pay for them later, and it is a major force in the rapid expansion of consumer credit and consumer culture. Thus, to understand credit card markets, we must recognize that the credit card is not one but a combination of two products: the payment card and the consumer loan.

As a means of payment, the credit card helps displace cash from day-to-day expenditures, making payments more convenient, transparent and traceable. As an instrument of credit, the card provides access to small-scale renewable loans, enabling cardholders to enjoy purchases they would not otherwise be able to afford. Historically, the two products were seamlessly fused into one in the form of a piece of plastic that fueled the twentieth-century credit card revolution in the United States. Conceptually, they are different, however. Credit can exist without cards: in the United States, retail credit has been around for much longer than cards, and examples abound of economies where installment purchases, home mortgages and personal loans flourish but no cards exist, with payments being made exclusively in cash or by check. Cards can also exist without credit: when a debit card is used, the money is immediately deducted from one's bank account, and the issuers of pre-paid cards do not extend any credit to cardholders; the card serves only as an instrument of payment. In fact, as we show, the majority of the Visas and MasterCard in circulation in transitional countries are debit cards, so cards extend little or no credit to customers in these countries.

Each of the two products that the credit card represents—a personal loan and a payment tool—offers its own set of puzzles. For instance, as a means of payment issued to individual holders and used in a variety of retail locations, the credit card has to be peddled simultaneously to consumers and merchants, giving rise to the chicken-and-egg problem (or as we call it, the

two-sided market problem). As an instrument of borrowing, the credit card necessitates solving another problem: the card issuers' uncertainty regarding the future repayment of the loan.

*Market Creation Versus Market Operation:
Generative and Functional Rules*

Today in the developed world, the payment card is a natural part of everyday life. We take it for granted. It works effortlessly, quickly, conveniently and innocuously. It can fulfill its functions precisely because it appears ordinary, reasonable and almost inevitable. When we pull out this piece of plastic, we know what to expect. When a cashier or waiter takes our card, they know what comes next. When a bank gives us a card, it can be fairly certain what we will do with it. Things can go wrong, such as when a card is declined at the point of sale, or stolen and used fraudulently, running up a huge tab in several countries within days. But we expect these mishaps to be the exception and develop routines to deal with them.

To appear natural, markets such as the ones that allow us to pay using plastic cards instead of coins or banknotes must have an explanation that captures the way the market works. For instance, if we ask people why they use payment cards instead of cash or checks, we may be told that it is a more convenient way to purchase things. This explanation makes sense, but it would be the right one only under several conditions. Paying with cards should not be much more costly than using cash, and card use should be secure enough to defend the cardholder from fraud. Another condition is that the electronic record of card transactions may not be used against the cardholder later, say, by the tax authorities. Still another condition is that there must be enough shops where the card is accepted so that it is worthwhile to carry the card around. And the list goes on.

Generating the conditions under which this simple explanation makes sense is what we refer to as *market creation*. Creating a market means constructing circumstances that allow people to conduct business by voluntarily following rational *functional rules*.³ We call the principles that describe market creation *generative rules*. The discipline of economics is interested in the rational, functional rules that drive the behavior of market actors. These rules reproduce markets, but they only work within the margins set

by *generative rules*. Economists focus particularly on one set of powerful functional rules: those based on self-interested competition that is driven by price signals and rational calculation. As economists move away from generalized notions of the market and toward particular markets, they build more complex functional models to capture the specific features of those markets.

Reproducing a market is not the same as creating it anew, just as building roads follows a different logic than driving on them. The first logic involves the tricks of moving earth, laying concrete, mixing asphalt, painting center lines and surface markings, cutting troughs for rumble strips and gluing down Botts' dots. The second logic involves the rules of traffic and some basic knowledge of how to operate vehicles. Once the road is built, the generative rules fade into existing circumstances and the functional rules take over. The road will still need maintenance—the filling of potholes, the repainting of markings—but we would not be able to drive from San Diego to Boston if we had to consider each and every engineering feat, past or present, that made our journey possible. This is why getting a driver's license does not include a test on road construction.

Traditional economics dispenses with this distinction between generative and functional rules, in two ways. First, it assumes that the circumstances that serve as preconditions of markets are so general and universal that they do not merit separate study. Any surface can serve as a highway: a rocky mountainside, a sandy beach and a snow-covered tundra can all be driven on; drivers just need to make some minor adjustments. Whether one is driving on rock, sand or snow, there is traction, albeit to varying degrees. The fact that people are rational optimizers who act independently on the best information available under some very general constraints, such as scarcity of resources and available technology, will be sufficient to account for the existence of any market. Constraints, like slippery roads, will be accommodated.

Second, economists may acknowledge that conditions can vary considerably, and some necessary conditions may be absent or certain adverse conditions may be present, but they posit that evolutionary forces will propel circumstances to align with rational functional rules.⁴ The traffic will create its own pathway and will maintain it. Its needs will force the existence of proper roads. If this is true, we can always explain road design by understanding the needs of traffic. We can account for the final characteristics of the road by keeping in mind that the engineers wanted the traffic to flow

properly. It is not just that we can provide an explanation *ex post*, but we can also confidently predict *ex ante* that the right circumstances will materialize. If markets work by people competitively reacting to price signals, then markets *will emerge* as people competitively respond to *shifting* price signals.⁵ In the first instance, generative rules are irrelevant; in the second, they can simply be deduced from functional rules.⁶

In the road example, the separation between generative and functional rules is clear. Road construction and driving are two different activities, done by different people with different credentials, at different times. In markets, this distinction is more blurred. The same actors who lay the foundations of the card market—card-issuing banks and credit card companies—are the ones who “drive” in that market (together with merchants and cardholders). The building of markets and the operating of markets are harder to separate, and markets are often constructed on the go. If markets create the conditions of their own operation, which amounts to building roads by driving, there is no need for outside intervention. Deregulation, the removal of outside interference, is the most we can do. As we show in this book, card markets do not spring up simply as a result of banks issuing cards to consumers; instead they require a lot of concerted market-building effort on the part of banks and the state, as well as multinational corporations and institutions.

There are stable markets in which the conditions are, at least for a time, relatively settled. To understand what happens in these markets, the researcher can fall back on functional rules. One can often create a rational model, beginning with laying out the market’s assumptions, inevitably followed by making some additional ones along the way, and proceeding to produce an explanation of high logical consistency. The rationalization of a market serves multiple purposes. It provides a simplified model of how it works and sometimes even allows for limited prediction. It advises actors how to behave, and makes the market legitimate by demonstrating that it functions in a reasonable and optimal manner given the circumstances. Moreover, a rational theory itself contributes to the stability of a market by providing a common language and understanding of how things ought to work. Because of their emphasis on analytic clarity and consistency, rational theories are often quite effective in coordinating people from different cultures and cognitive worlds. By justifying markets, rational theories also protect them from destabilizing moral or political criticism. But markets are rarely as frozen

as economic theories portray them. When conditions shift or entirely new markets emerge, the researcher needs to look for generative rules. Besides, entrepreneurs who engage in innovation must also consider generative rules because entrepreneurship often revamps old markets or gives birth to new ones, setting up new conditions and requiring new assumptions.

Our distinction between market creation and operation, between generative and functional rules, is not new at all. This contrast is recognized by both economists and sociologists. The incongruity of generative rules and functional rules will appear to economists as market failure. One of the key functional rules of the market is that the price signal drives supply and demand. One way economists understand market failure is that the price fails to include all important existing information about the product or service. Externalities are the costs and benefits that price does not capture.⁷ An example of possible market failure is food safety.⁸ Restaurants that cook under unsanitary conditions may save money by doing so and thus outcompete clean restaurants on cost, but only if they do not have to pay for the discomfort and sickness of their customers. Yet unclean cooking not only damages the cook's reputation but also dampens people's overall enthusiasm for eating out and thus harms all other restaurants. For this market to work properly, food safety regulations and inspections must be in place; these conditions, which are not generated by the rules of price-guided, self-interested competition, may make the market flourish once they are installed. Then a story of rational market competition, *assuming* working food safety regulations and inspections, can be constructed. As long as the food safety problem is solved, these functional rules can have predictive power.

Sociologists are even more aware than economists that generative rules are not necessarily those that can describe the operation of a rational market. One of the central ideas of economic sociology is that markets are embedded—that they depend on a series of social arrangements unacknowledged by economists.⁹ This idea can be recast as the realization that the conditions of rational economic action are generated by a different set of logics. When we argue that economic transactions are embedded in social ties or institutions or cultural understandings, we essentially argue that the circumstances that make economics function are generated outside the transaction, that functional and generative rules are different. For instance, the classic example of Orthodox Jewish diamond traders in New York observes that the selling and buying of expensive gems require trust among the traders.¹⁰ This

condition, however, is not produced by the functional logic of the transaction that strives for maximum profit and thus abets opportunistic behavior. The trust is generated by a separate logic, that of the religious community with its power of socialization and sanctions. Yet once the puzzle of trust is solved—thanks to religion—a rational story of supply and demand, profit maximization, and so forth can arise.

All economic sociologists agree that the market is socially constructed,¹¹ but when they go about demonstrating how markets depend on their social context, they often engage in an interpretative exercise to show how different elements of an already existing rational market are linked to the social world. This linkage is then offered as evidence that the social world does something to markets that allows them to operate: Orthodox Judaism makes the diamond trade possible, or health inspections are necessary for a restaurant business to exist. Skeptical economists, however, may point out that the causation may run in the opposite direction. It is not, they may say, that trust makes the diamond trade possible but that the trade gives people a strong incentive to be trustworthy. Religion is just an incidental form that trust takes. Precious stones are traded by people other than Orthodox Jews and even by people with no religion whatsoever. By the same token, they could argue that health regulation in the restaurant industry is unnecessary as long as eateries can be sanctioned after the fact to deter unclean cooking. Proper standards of hygiene can and will be achieved one way or another. The social conditions of the market are produced by the overriding logic of supply, demand, price and rationality.

We contend that these questions can be answered only if we take a historical, comparative approach, to see how things have unfolded in time, what came first and what came later, and to observe various ways in which markets have emerged or failed to do so.

Social Order

Markets are a particular way of coordinating economic exchange. Building a market means building this particular form of coordination.¹² There are alternative ways of organizing economic exchange, including centralized redistribution, a form of which was the centrally planned economy under communism, and reciprocity, the kind often found within families or