Surviving the global financial crisis by adopting a unified payments hub approach

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Abstract Corporates are coming under increasing pressure to cut costs and become more agile in order to survive the difficult financial climate. The author explains why a payments hub solution is exactly what corporate treasurers need to tackle the challenges of the current market. Technology becomes an enabler to help corporates to stay one step ahead of the competition by providing increased efficiency along with reduced overheads and a single overview of liquidity for better risk management. Furthermore, being able to see overall cash position in a more timely and consolidated manner allows faster reaction to market events, which is vital in these volatile times. A suitable payments hub solution also allows corporates to benefit from technological and market improvements, such as SWIFT connectivity and SEPA and later on with e-invoicing.

KEYWORDS: payments, payments hub, SEPA, e-invoicing, SWIFT, cash management, rule-based, end-to-end STP

INTRODUCTION

The times are volatile and challenging. The ongoing financial crisis is posing a significant threat to businesses as they are faced with the economic imperative to cut costs and become more agile in order to survive. The last 12 months have seen the collapse of a surprisingly large number of established corporates, caught out by the global liquidity crisis. To avoid the same fate, firms are focusing on their finances and the role of the corporate treasurer has grown in importance.

Corporate treasurers are being asked to do more with less by their senior management, and headcounts and budgets have been drastically cut. Cost containment is therefore at the forefront of these corporates' minds, as is the spectre of risk in the form of increased liquidity risk and supply-chain risk. Couple these financial pressures with the impact of globalisation and the requirement to deal with more firms across a wider geographic footprint, and one has a significant challenge on one's hands.

WHAT CORPORATE TREASURERS WANT

According to recent research by analyst firm Celent,[1] corporate treasurers are looking to their providers for a range of areas for improvement, including data consolidation, standardisation, global solutions, integration, analysis and timeliness. This necessitates consolidation across geographic regions and

across banking relationships. The holy grail of liquidity management in this market is a single consolidated view of all funds available, and the ability to act on the data in a timely manner.

The competitive environment is tough and getting tougher. Corporates need to stay ahead of the game and, as well as dealing with short-term issues such as immediate cost-cutting measures, they also need to focus on their long-term strategic goals. Accordingly, corporates that successfully manage the new formats and standards in the payments world will increase efficiency and reduce costs, while those that do not will see increased bank charges and processing overheads.

Many corporate treasurers are adopting a back-to-basics approach and focusing on getting core treasury functions correct via investment in a centralised solution. The ultimate payments goal for corporates should be a centralised, flexible and scalable platform that handles invoices and payments for all suppliers, banks and accounts. This may be a complex undertaking, but the rewards will be worth the effort.

SEPA: AN OPPORTUNITY TO BE TAKEN

In terms of consolidation across geographies, the introduction of the Single Euro Payments Area (SEPA) also promises to bring substantial benefits to corporates. At a basic level, SEPA will benefit corporates by ensuring that euro payments, both domestic and cross-border, are handled with the same level of service and at the same price.

It is still early days for the bank-led initiative — SEPA credit transfers (SCTs) went live on 28th January, 2008. SEPA direct debits (SDDs) are scheduled for implementation by November 2009, by which time the European Commission's Payment Services Directive (PSD), which provides a legal framework for SDDs and SEPA card payments, must have been transposed into national law in all EU member states.

Those that do not take notice of SEPA, however, could potentially face added costs, not least because banks can charge more for a non-SEPA message than for a SEPA message. Unsurprisingly, such added cost cannot be supported in the current climate.

Furthermore, SEPA is an infrastructural investment that sets the stage for future gains. A study by Cap Gemini,[2] commissioned by the European Central Bank and published on the day SEPA went live, estimates that there is ¤123bn of 'market potential' in SEPA. The study, called 'SEPA: Potential Benefits at Stake', points out that electronic invoicing (e-invoicing) could create potential extra revenues of between ¤0.4bn and ¤3.4bn per year.

SEPA therefore standardises and harmonises payments processing across borders, thus reducing the complexity of implementing e-invoicing solutions that has existed until now. E-invoicing solutions can be integrated into the back offices of sellers and buyers. Moreover, the PSD harmonises regulation and legislation, further lowering the barriers to e-invoicing.

TECHNOLOGY AS AN ENABLER

In such a challenging market environment, technology becomes both a method of cost and risk reduction and an enabler to cope with future requirements. As cost-cutting measures must be balanced by the fact that areas such as payments must still be managed to a high level of quality in order to avoid costly errors, technology seems the most obvious solution. After all, cutting costs is all very well, but cutting corners is not.

Corporates need to leverage technology-based solutions in order to be better able to adapt to changing market conditions. A key factor in this is getting the basics right, in the form of automated payments processing and liquidity management. Being able to see one's cash position in a more timely and consolidated manner allows faster reaction to market events, something which is now high on the radar of corporates that may have been caught out by fast-moving events in recent times. There is also a regulatory imperative to comply with

regulations such as Sarbanes-Oxley and Basel II, which specify levels of control and risk management.

The fundamental issue is also avoiding errors, which can be introduced by manual processing at the start of payments lifecycle. Getting it right first time reduces the likelihood of errors further down the line. The regulatory and public focus on better risk management has increased the impetus to obtain a true consolidated picture of a firm's liquidity position, current holdings and risk exposure. This necessarily entails more data and analytics in order to provide better and increased visibility.

The corporate focus on cost-cutting indicates that very few companies will have the budgets to maintain costly in-house systems and large headcounts to deal with the basics of payments processing. Moreover, the increase in volumes and the complexity within the market will heighten the need for specialist knowledge and a partnership approach to processing. By employing a technology-based solution for payments processing, these corporates can be freed to deal with other more complex areas in partnership with a specialist vendor.

THE PAYMENTS HUB

The argument for the introduction of a centralised payments hub is compelling. It involves significant cost reduction via the centralisation of payments processing onto a single integrated platform and payment routing across multiple banks with statements reconciliation. The elimination of point-to-point linkages (Figure 1) results in a reduction in required headcount and duplicative technology. Through such specialisation, corporates can dispense with a large number of country-specific accounts and the associated costs and complexity.

After all, in the current market environment, corporates will not want to put all their risks in one basket by routing their payments via a single bank. They must consider the potential collapse of financial institutions and the threat this poses to their business. This risk can be

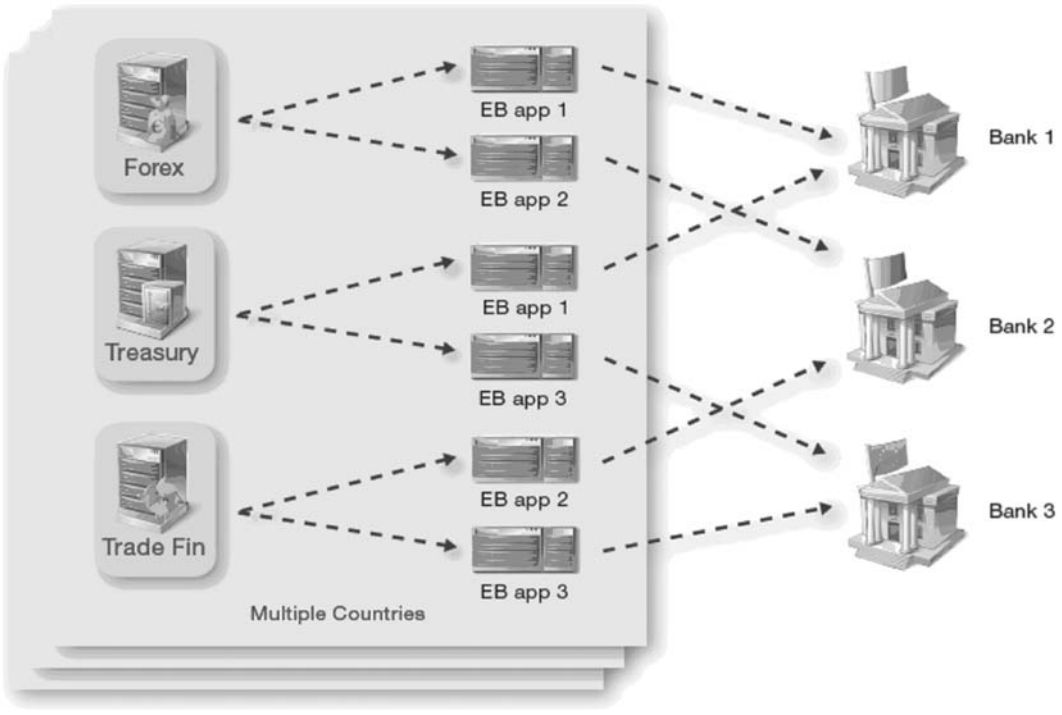

Figure 1: The typical situation for connectivity via multiple electronic banking applications

easily reduced by connecting to several banks via a single payments hub.

A centralised system also provides increased control and transparency of financial and operational risk by holding the data in a single harmonised system. Corporates must learn from the mistakes made by others in the financial services industry and move away from inefficient silo systems. There must also be clear separation of business and back-office applications from their network connectivity application, and this must be taken into consideration when selecting a vendor partner.

Solutions should include unified high-value/urgent and low-value/non-urgent payments messaging across a system with a high level of service and security. The solution should also incorporate industry best practices as standard.

To realise the full benefits of their investments, corporates need to take a holistic view, taking into account their banking relationships, financial supply-chain optimisation, compliance requirements and cash flow/liquidity/credit management.

A payment hub system should support the following key functionalities:

- *Payment message processing*: The messages and files received from ERP and back-office systems must be validated, enhanced, transformed and then routed to the respective banks.
- *Bank statement processing:* The statements received from banks must be validated, matched and routed to the respective back-office and ERP systems.
- *File processing*: Several file formats should be supported to ensure easy connectivity, such as Clieop3, BACS, BAI2, EDIFACT, SEPA, GMU, BTL91 and back-office specific formats.
- *Manual payment capture*: PELICAN provides a user-friendly web-based graphical user interface to capture payments manually. The interface should support four-eye (ie maker and checker) principles for added security.
- *Multi-institution and multi-branch:* The solution should support a multi-entity and multi-country processing environment.
- *Exception processing:* In addition to automated straight-through processing (STP), the system should also support secure exception processing. Multiple workflows and queues should be available, with qualified access for exception scenarios like duplicates, cut-offs and holidays, future date warehousing, rejects, returns etc.
- *Cash and balance management:* The statements received from banks should be automatically matched to the payment receivable and payable items in the cash ladders. The system should then calculate the real balance, actual balances for the same day, and forecasted balance for various user-designated accounts.
- *Connectivity to back-office systems:* Connectivity to ERP and back-office systems should be possible via multiple options such as files, MQ Series or databases.
- *Connectivity to SWIFT:* Connectivity to SWIFT should be established through SWIFT Alliance Access, SWIFTNET InterAct and FileAct. PELICAN transmits payments files and messages to the banks and, in turn, receives statements from banks via this connection.

Moreover, to benefit fully from SEPA, corporates need to make investments and changes. The key issue here is information exchange — by linking payments and invoicing, corporates can gain greater visibility and control over their liquidity. At a time when credit is hard to find, this capability is paramount.

BANK CONNECTIVITY VIA A PAYMENTS HUB

Systems exist for managing under the new market environment, and when properly conceived and implemented (Figure 2), they can accelerate the evolution of information flow and transaction handling. The features of such a system should include:

- *End-to-end STP:* Corporates can gain competitive edge by taking advantage of

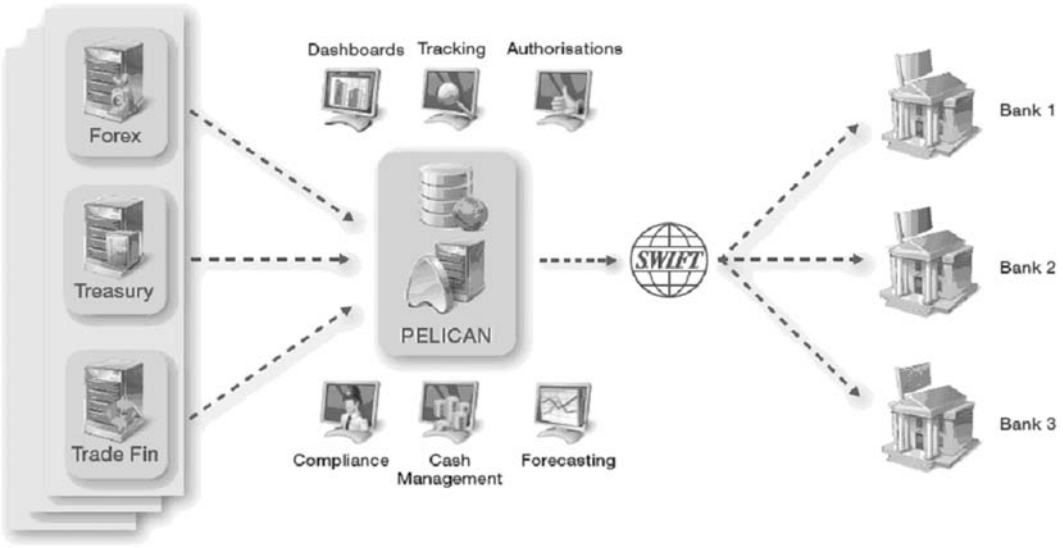

Figure 2: Bank connectivity via a payments hub

initiatives for complete end-to-end STP, the elimination of manual processing, and the integration of financial and physical supply-chain transactions.

- *Measures for SEPA compliance:* This includes ensuring that BIC and IBAN information is available in payment instructions and moving to new ISO20022 messaging formats.
- *Global vision and control:* There is a need to oversee, control and manage all financial transactions worldwide for optimal cash management.
- *Extensible component-based architecture:* IT spend has been cut and corporates can start in their particular area of pain and move to other areas gradually, resulting in reduced development risk and increased implementation speed
- *Single window access to financial institutions:* To reduce risk, manual processes, errors and connectivity overheads, a secure multi-FI (financial institution) platform is desired. This facilitates flexibility in choice of banks via the standardisation of all current proprietary connectivity to these institutions.
- *Agile, rules-based functionality:* The system should provide corporates with the ability to adapt to changes in the global environment quickly and painlessly and, most importantly, stay ahead of the competition.
- *Flexibility, scalability and reliability:* In the world of continuous change and improvements, a system should be flexible and scalable to accommodate new requirements and function in a reliable manner.

SWIFT CAPABILITIES WITHIN A PAYMENTS HUB

Access to SWIFT allows corporates better visibility over their funds via the use of standardised messages and protocols. The network allows corporates to communicate directly and immediately with the growing community of banks connected to SWIFT. The decision by SWIFT to extend its corporate access offering in 2007, with the addition of the Standardised Corporate Environment (SCORE) model, has made connectivity to the network even more worthwhile.

A corporate can manage its own private infrastructure whereby the connectivity infrastructure is owned and operated by the company, or it can engage a service bureau, which owns and operates the connectivity infrastructure. In both scenarios, the corporation is responsible for its own

applications (ERP, treasury workstations) and is best served by facilitating integration and STP to each whenever possible. A service bureau may serve as member concentrator, which also manages the administration (eg applications, onboarding and invoicing) of the SWIFT membership on behalf of its corporate client, thereby increasing the level of service the corporate can enjoy.

Unsurprisingly, as it is used by as a communication by the financial services community, SWIFT's reliability and resiliency as a network is remarkable: it has a 99.995 per cent availability history. It also has a follow-the-sun support model which allows for round-the-clock network availability, in keeping with the global nature of today's markets. SWIFT's cash management and exceptions and investigations services can also help corporates to achieve the same levels of STP in their treasury that banks enjoy in their back offices.

At the end of 2008, SWIFT also facilitated the exchange of trade data over the network to complement the treasury and cash management offering already in place. Moreover, moves by SWIFT, Twist and ISO20022, as well as other initiatives in e-invoicing, e-billing and e-reconciliations can be of immense value to the corporates connected to SWIFT via a central infrastructure.

Corporates seeking to take advantage of access to SWIFTNet will need to make some technology decisions. They must avoid a situation whereby they are managing multiple interfaces to SWIFT. To extract the maximum benefit from SWIFT access, corporates will want to enable communication with banks by a number of different departments — accounts payable and receivable, treasury and foreign exchange. Corporates therefore need to choose systems that enable a single SWIFT hub to handle all these connectivity needs.

SWIFT changes its messages frequently and, as banks have learned to their cost over the years, if SWIFT connectivity is embedded in numerous systems, the burden of keeping up with those changes becomes unbearable. Solutions that keep SWIFT activity separate from back-office processing systems and ERP solutions, while at the same time enabling ease of integration with those systems, help to alleviate this burden as changes that need to be made to SWIFT messages can be implemented without disruption to the core infrastructure.

The implementation of an intelligent and flexible solution also supports corporates' ongoing requirement to manage SWIFT connectivity for corporate-to-bank communication and internet-based messaging for communication with other corporates. The most efficient way to handle this dual requirement is to implement one system with the intelligence to manage both connectivity with the banks via SWIFT while automatically routing messages related to invoicing, for example, to other corporates. This takes the form of a payments hub that can quickly meet all corporates' payment-related requirements.

The solution must therefore be able to act as a hub for both SWIFT messaging and payments (Figure 3). As most SWIFT messages are payments-related, this functionality is merged in many cases. However, this option to act as a hub for both, whether separately or in combination, allows those wanting to use SWIFT messaging to do so and thus benefit from this connectivity.

E-INVOICING: THE FINAL STEP

E-invoicing is a crucial final step in automating the financial supply chain and a number of activities fall under the umbrella of e-invoicing, including all of the steps in purchase-to-pay and the order-to-receive cycle (Figure 4). Sending and receiving invoices, dispute handling, acceptance, payment and collection, reconciliation and archiving are all tasks that can be automated and streamlined. E-invoicing improves efficiency by eliminating manual tasks, achieving higher reconciliation rates, shortening processing cycle times, and reducing penalty interest.

Corporates have made substantial investments in automating the physical supply chain — at any time, a corporate can track the whereabouts of goods, but it cannot track the

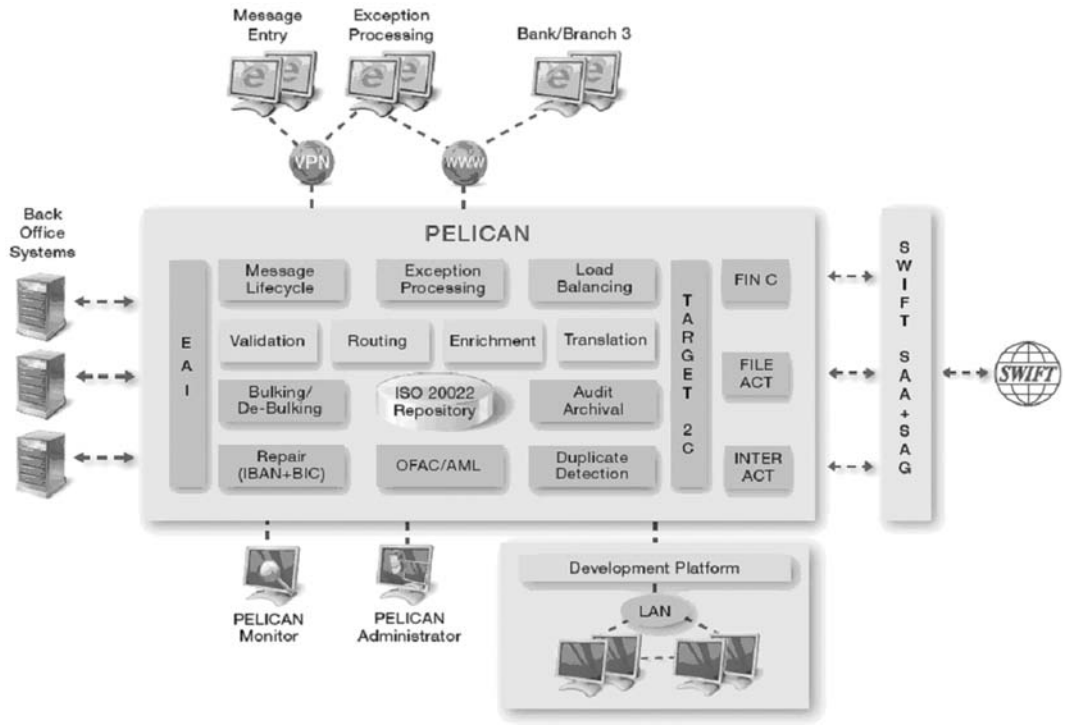

Figure 3: SWIFT capabilities within a payments hub

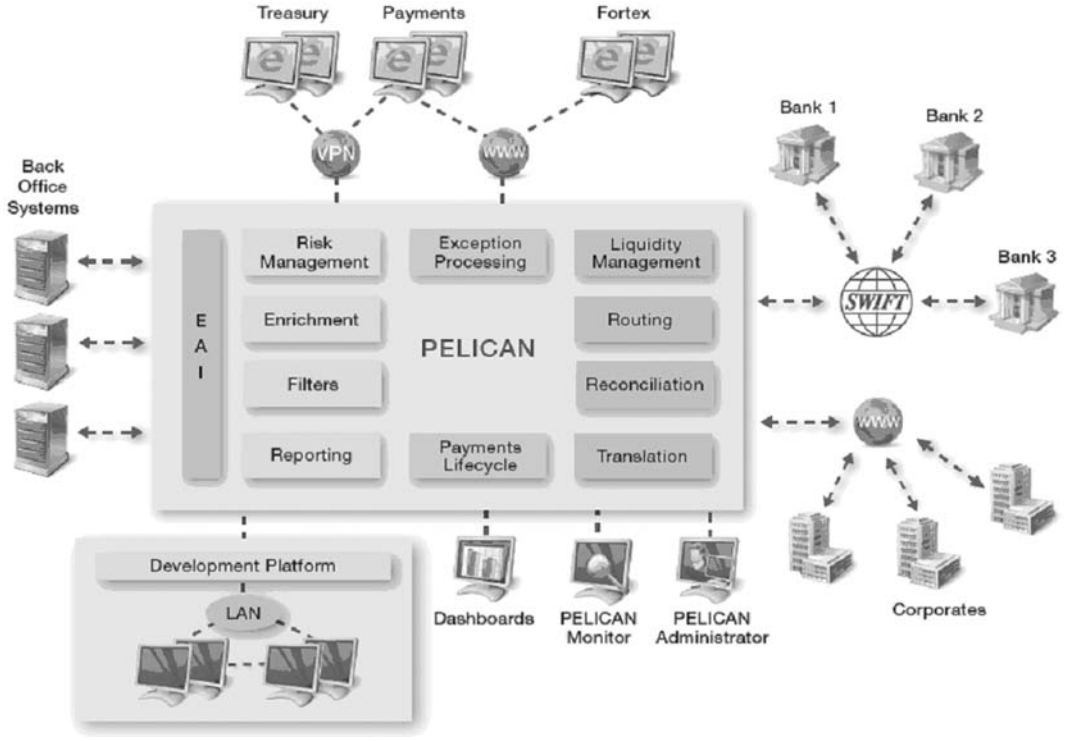

Figure 4: E-invoicing — the final step

payment associated with those items. Goods can be delivered within hours, but the associated payment cannot. Yet there is no reason for this — the standards and the technology exist to enable information to be sent automatically to back-office systems for reconciliation. With a combination of standards and best practice, the financial supply chain can be as efficient as the physical supply chain.

This lack of automation in the financial supply chain means that corporates spend a huge amount of time managing their accounts receivable and accounts payable activities. Paper-based invoicing is cumbersome and prone to error given the high level of manual handling required. The majority of corporates do not know the exact status of payments and have great difficulty in matching payments with their invoices.

In Europe, the average cost of manually processing a paper invoice is about ¤30. By leveraging infrastructure and standards that are being promoted by SEPA, such as ISO20022, the potential cost savings are in the order of 80 per cent. European corporates could in total save about ¤243bn in processing costs. Now is the time to focus on the financial supply chain, automating it so that the financial information can flow freely and payments can be made within hours, if not minutes.

THE FUTURE

Although there are many issues to address in the short term due to the current market environment, corporates cannot forget about the challenges that are likely in the longer term. For example, financial supply-chain automation will be a key element for both banks and corporates to succeed in an increasingly competitive business environment. In the future, it will be increasingly difficult to compete without a consolidated approach to payments, SWIFT and the financial supply chain. If corporates do not invest in a centralised approach, costs will be very high and they will be unable to dynamically monitor performance, risks and revenue streams.

To cope with future market challenges, corporates' systems must also support, or be committed to supporting, initiatives including:

- matching and reconciliations — artificial intelligence-based matching of the invoice numbers on invoices with those mentioned in the bank statements;
- least-cost routing/advanced global payments routing for all payments — back-office systems should not have to worry about this as it should be handled by the payment gateway;
- e-invoicing, e-billing and e-reconciliations;
- integrated credit transfers, direct debits and cards processing;
- integrated SWIFTNet business solutions;
- real-time cash reporting, exceptions and investigations;
- workflow with business process management and business activity monitoring.

However, to benefit from the advantages of these new initiatives, including new forms of SWIFT connectivity and integrated business processes, corporates must start planning and implementing a solution now. They cannot afford to wait and allow themselves to be overcome by cost and complexity when the economic environment is so challenging. Instead, they must make the choice now to centralise onto a single integrated platform for all their payment processing requirements and benefit from greater efficiency and cost reduction. They must adapt to survive.

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