

Study | Treasury

Payment Processing and Cash Management Study Trends and Opportunities



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1. Introduction and purpose of the study

In recent years companies worldwide have had to face challenges due to changes in global economics, in market stability, in Cash Management and liquidity assurance, as well as due to new techniques and standards in Payment Processing. Some of those challenges have been mastered, while others are still in progress.

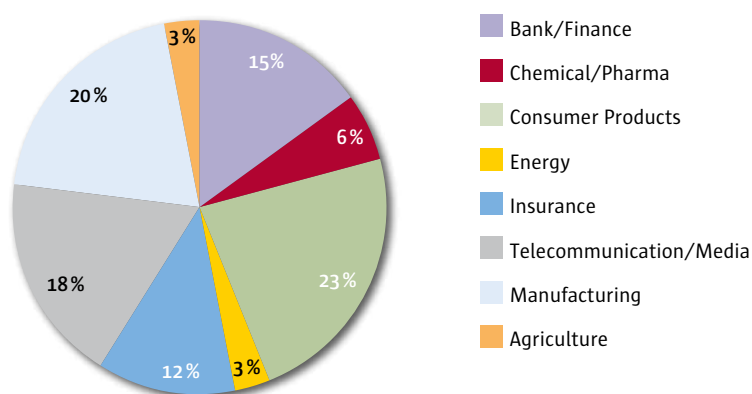
With this study, BearingPoint investigated how European companies have been facing these challenges and how they are preparing for the future. It includes an analysis of current developments in the area of Payment Processing and Cash Management. Special emphasis was placed on the progress of the Single Euro Payments Area, as SEPA is bound to permanently change the European payments landscape. The goal of SEPA introduction is to bring about savings in costs and complexity through harmonized and renewed Payment Processing for every company. BearingPoint specifically emphasised the progress of both SEPA Credit Transfer and SEPA Direct Debits adoption.

The questionnaire was divided into sections dealing with SEPA Credit Transfer and Direct Debits, Corporate Payment Processing and Shared Service Centre Organization as well as Cash Management.

The questionnaires, which were presented to the participants both as an online survey and in print form, were filled out between the middle of 2010 and the beginning of 2011.

The industries of the respondents participating in this survey are shown in the following figure.

Figure 1: Participants of the study by industry sector



The following chapters show the key findings of the survey including interpretation and conclusions which can be used to analyse the position of your company compared to the other survey participants. This study offers the opportunity to identify fields for further improvements of the daily Payment Processing and Cash Management operations. To some extent the results can also facilitate a strategic decision regarding the centralization of payment processes and implementation of an In-house Bank.

2. Management Summary

The banking industry already started to harmonize interbank communication in the 1970s by founding the Society for Worldwide Interbank Financial Telecommunication (SWIFT), but the majority of the corporate world was excluded from that network for another 30 years. After decades of isolated national payment formats and communication standards for electronic data interchange between corporates and banks, we are today witnessing a major shift towards harmonization and standardization in Payment Processing.

Many new aspects of corporate Payment Processing solutions have arisen in recent years, revealing both chances and challenges. In Europe, ambitious efforts are driving a major technical change in the payments landscape affecting the whole payment process chain, called SEPA.

The study confirms that the European Union and the European Payment Council are on the way to reaching their goals in setting up SEPA. The implementation of innovative and efficient SEPA payment services based on global ISO standards leads to efficiency gains for corporate businesses as well as public institutions. Common standards, faster settlement and simplified processing, without compromising on security, improve cash flow, reduce costs and facilitate access to new markets on a domestic and cross-border basis.

New formats, legal requirements and changes in the local and global markets under tough economic constraints within a changing banking landscape caused the adoption of SEPA payment processes and functionality to be quite a daunting task. An interesting result shows that it is the medium-sized companies from 1,000 to 10,000 employees that struggle the most to adopt SEPA payment formats and services. Both small and large companies are more advanced in the adoption. Most implementations have been made in using SEPA Credit Transfer for cross-border payments. The abolition of national methods and formats can significantly motivate the remaining companies to switch from domestic payment formats to SEPA payments.

The results show that the implementation of SEPA Credit Transfer is much more advanced than the corresponding SEPA Direct Debit. This is not surprising in itself as the process for SEPA Direct Debits started later and is more complex to implement, but in combination with rather low information level in those corporates regarding additional services provided by banks, two major points can be derived for SEPA Direct Debits:

- As soon as a final date for local formats has been set up, a lot of companies will be under time pressure to find a solution to quickly adopt SEPA Direct Debits.
- There is still significant potential for banks to offer products and additional optional services to their customers, and there is still room for improvement for corporates to end up with a high-performance payment infrastructure as a combination of both internal services and selected external services.

The study shows that the trend of payment process centralization and harmonization is still ongoing due to the setting up of Shared Service Centres. The optimization and internalization of group internal and external payment processes is, among other reasons, a result of optimization of working capital as well as reduced trust in the stability of the banking industry.

Both, In-house Bank and so-called Payment Factory functions are widely used. And even those companies with more than 5,000 employees that do not yet have a shared service function in place mostly plan to implement one in the future to streamline and harmonize their Payment Processing. For companies with less than 5,000 employees, a careful cost/benefits and process analysis that identifies whether the implementation of an In-house Bank for group internal Payment Processing is useful needs to be undertaken. The study shows that the centralization of external payments is made regardless of the size of the company. Larger companies will organize this in a Payment Factory.

Companies have been restructuring their Cash Management and Payment Processing over the past few years in order to obtain a better overview and control over the group-wide liquidity and exposure situation. The results of this study confirm that the trend towards centralization of Cash Management from local to regional or global units is now reaching an optimum level in many companies. Further centralization could lead to a reduction in efficiency and effectiveness as the distance to local or regional markets would get too big.

Cross-border Cash Management activities are usually not performed as often as domestic payments, but especially with the SEPA instruments Credit Transfer and Direct Debit they will become much more attractive. Even smaller companies not yet using Cash Pooling or Cash Concentration will be in a comfortable position to implement those functionalities at reasonable costs.

Finally, in terms of business process outsourcing, only one-third of the responding companies use external bank services to support their internal treasury functions such as FX Exposure and Hedge Management, Cash Pooling, Risk Management and Payment Processing. The majority of the companies perform these tasks with internal resources and systems only.

3. Topic introduction and survey results

The questionnaire addressed three areas starting with SEPA Credit Transfer and Direct Debits followed by Corporate Payment Processing and Shared Service Centre Organization and closing with Cash Management topics. Each area is split into a chapter introducing the topic and a chapter presenting the survey results and conclusions.

3.1. Introduction to SEPA Credit Transfer and Direct Debit

Since the establishment of the Single Euro Payments Area (SEPA), there has been a standardized way to perform domestic and cross-border payments via SEPA Credit Transfer (SCT) and SEPA Direct Debit (SDD) without a limit to the amount, in contrast to the former limit of 50,000 EUR.

The objective of SEPA introduction is the Europe-wide standardization of payment transactions as well as its corresponding infrastructure, resulting in a further step towards European integration. Besides the 27 EU nations, Iceland, Liechtenstein, Norway, Monaco and Switzerland are also current SEPA members.

Domestic and cross-border Euro payments between any country in SEPA are processed quicker and at lower or at least the same cost as domestic payments before SEPA introduction. First big milestones were the implementation of SEPA Credit Transfer in January 2008 and SEPA Direct Debit in November 2009. The adoption of the Payment Services Directive (PSD) into national legislation forms a Europe-wide standardized framework for payments.

Since November 2010 all banks have been obliged to be able to execute all kinds of SEPA payment requests sent to them. With the implementation of SEPA instruments, banks also offer Additional Optional Services (AOS), e. g. supporting electronic invoicing. Clients thereby have the possibility to perform and optimize further business processes via SEPA services and can thus realize economies of scale. SEPA makes products and services in the area of payment transactions more comparable. With the implementation of SEPA formats, the banks in the end also get the chance to reduce the number of national formats step by step and, in so doing, reduce the number of interfaces, the complexity and the costs.

3.1.1. SEPA Key Design Elements

All bank accounts within the SEPA are uniformly accessible via IBAN (International Bank Account Number) and BIC (Bank Identifier Code, also known as SWIFT code) through the introduction of the SEPA payment transactions instruments.

The new SEPA format is based on the ISO 20022 standard and will replace existing national standards such as DTAUS (DE), CFONB (FR), CLIEOP (NL), etc. This change has a direct impact on banking communication, which necessitates changes in the existing communication systems. It also impacts the timing for payment execution.

The settlement time between sender and recipient will be reduced by SEPA Credit Transfers from three bank working days to D+1 day, starting in 2012.

3.1.2. SEPA Payment Types

The SEPA Credit Transfer allows credit transfers to be processed under the same conditions as existing domestic ones, regardless of the transferred amount and whether it is a domestic or cross-border payment.

The SEPA Direct Debit process for the first time allows the standardized processing of cross-border direct debits. Direct debits can only be processed on the basis of mandates. As with the still-existing domestic direct debits using direct debit mandates and debit orders, there is a B2C (business to customer) as well as a B2B (business to business) process in SEPA. This is described by the European Payment Council in the Rulebooks for SEPA Direct Debit B2B and Core. The existing direct debit authorizations have to be transferred into direct debit mandates.

In addition to the payment methods mentioned above, the SEPA Card Framework (SCF) allows the use of SEPA cards in all terminals across the SEPA. The SCF will not be further detailed in this study.

3.1.3. Strategic Positioning and Payment Factory Impact

A single European legal framework enables companies to use a single bank strategy within the SEPA area. The single bank model will remain an exception in order to avoid strong dependencies. But companies should consider that a reduction of bank relationships facilitates a reduction of interfaces.

In centralizing and concentrating payment transactions execution, additional synergies in the area of Cash Management, e. g. in implementing an In-house Bank as well as a Payment Factory, can be achieved and complexity reduced. Beyond centralizing all payment processes, companies can also think about outsourcing the processes to an external service provider in order to reduce costs and increase efficiency.

Even when the adoption of SEPA Credit Transfer reaches 100 %, the payment scheme is still for euro payments only. There is still a need for further payment procedures to settle non-euro payments. Therefore SEPA Credit Transfer will not be the only format for companies making outgoing payments in non-euro currencies or via banks outside SEPA.

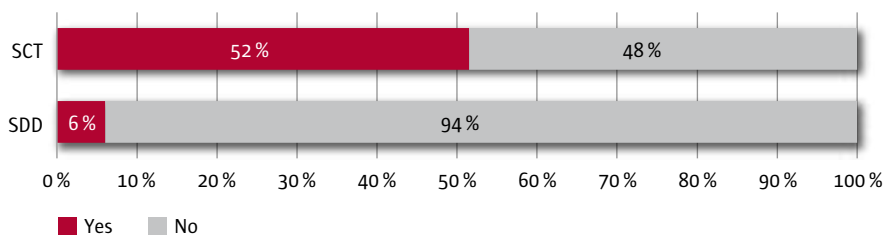
The SEPA payment format is based on the ISO 20022 standard, which also includes a field for payment currency. Therefore many banks with international reach already offer the processing of payments in the ISO format in any currency. So it is worth negotiating for acceptance of further currencies when discussing the implementation of SEPA with banks. After the investment to implement SEPA based on the ISO 20022 format, foreign currency payments (if accepted by the bank) can be executed using SEPA Credit Transfer and SEPA Direct Debit payment formats.

3.2. Survey results on SEPA Credit Transfer and Direct Debit

3.2.1. Usage of SEPA

Since the introduction of SEPA in January 2008, a transition phase has been taking place in the corporate world. New payment formats are being adopted in order to reduce or replace existing proprietary payment formats. As the country-specific formats for credit transfer and direct debits will disappear, this is a change that all companies have to face sooner or later. Therefore, it is interesting to see how many companies participating in this study have succeeded in the transition to SEPA payments usage.

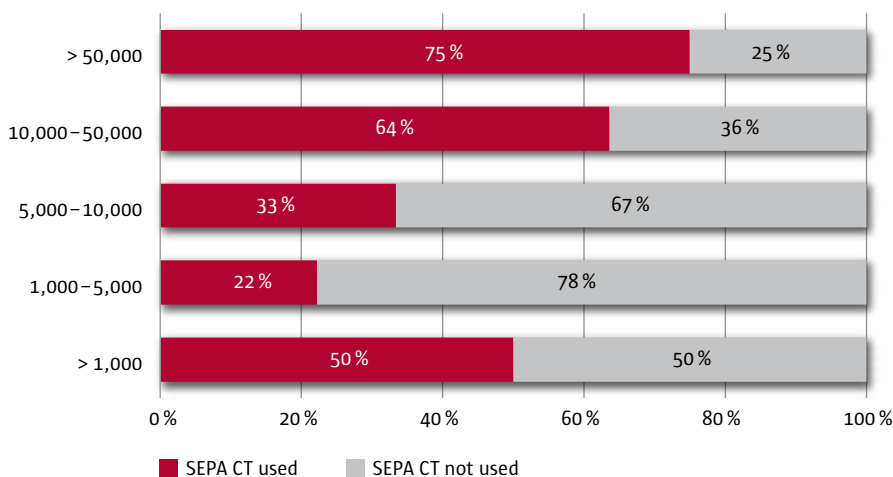
Figure 2: Companies using SEPA payments



The results above show that SEPA adoption is only completed halfway for credit transfers and just starting for direct debits. The study also shows that SEPA Direct Debit is so far only used by companies that already use SEPA Credit Transfer.

Breaking down the adoption of SEPA Credit Transfer by the size of the companies (measured by number of employees) leads to the following figure.

Figure 3: SEPA Credit Transfer usage by number of employees

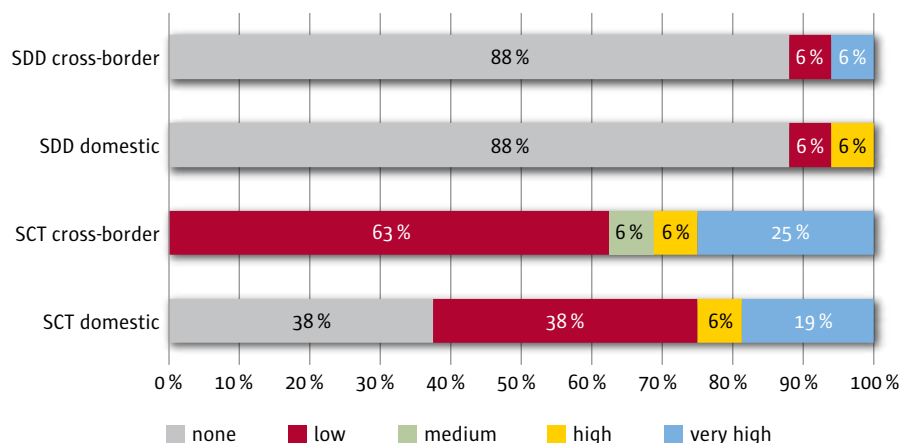


The study shows that companies with more than 10,000 employees and smaller companies with less than 1,000 employees are more advanced in the SEPA Credit Transfer adoption process than companies in the middle range of 1,000 to 10,000 employees. The possible reason is that smaller companies have less complexity when changing their payment processes and large companies already have more standardized processes and more resources to manage the change, while the companies in the middle range have to deal with higher complexity of heterogeneous systems, processes and master data, often with insufficient available capabilities.

3.2.2. Extent of usage of SEPA Format for Domestic and Cross Border Payments

Looking at those companies that in general use SEPA payments, the figure below shows that there is a huge discrepancy in the extent to which SEPA products are used for domestic and cross-border payments. Far more companies use SEPA Credit Transfer for cross-border payments than for domestic payments.

Figure 4: Usage of SEPA for domestic and cross-border payments



This leads to the conclusion that companies tend to keep the domestic payment process unchanged while taking advantage of the lower costs for cross-border payments by using SEPA Credit Transfer.

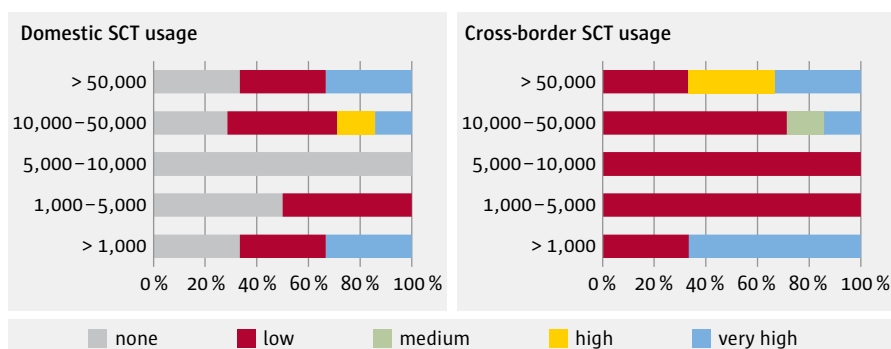
When the SEPA Credit Transfer format is set up in the payment infrastructure, it can be used for domestic and cross-border payments in the same way. An obstacle is that the master data of the payee (payment recipient) needs to include IBAN and BIC and that the transition phase of collection and maintenance of master data for domestic payments is still ongoing due to larger data volume. From a SEPA introduction project perspective, the lower volume of master data and number of payment transactions make it easier to start with and then to roll out the solution for domestic payments in a second step.

In summary, while the trigger for SEPA in the area of cross-border payments is the reduction in charges as well as value dates (settlement within D+1 day beginning of 2012), the use of SEPA for domestic payments is stimulated by the harmonization of payment processes and avoidance of country-specific formats and interfaces.

3.2.3. Split of usage by Company Size (number of employees)

For SEPA Credit Transfer payments, a split by number of employees and usage of SEPA payments on a domestic and cross-border basis as a percentage of the total number of payments showed interesting results. For SEPA Direct Debit there were as yet too few users to make a reasonable split based on company size (number of employees).

Figure 5: Domestic and cross-border SEPA Credit Transfer usage by company size (number of employees)



Taking a closer look at the companies that use SEPA payments, large companies with more than 10,000 employees and small companies with less than 1,000 employees are consistently faster in the process of SEPA adoption for domestic payments as well as for cross-border payments.

Even though larger companies have more vendor and customer master data to harmonize and maintain before SEPA payments can be implemented, they are at the forefront of SEPA adopters. The internal processes for master data maintenance are either already more harmonized and standardized or they have proportionally more resources and know how to manage the change from country-specific bank data to international IBAN and BIC within the customer and vendor payment details.

As the adoption is more advanced for cross-border payments than for domestic payments, this can be seen as an indicator of a consolidation process in the area of bank communication. Companies often use the cross-border reach of SEPA to reduce their external bank connections from banks in all countries where business is done to selected core or master banks that cover regions or sub-regions (e.g. Nordics, Iberia, etc.). This is a general trend seen in several industries and SEPA is a promoter of this bundling process.

3.2.4. SEPA Payment Format Creation

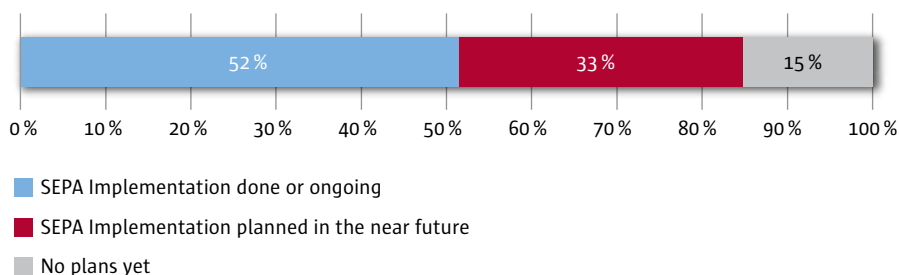
Regarding the question how those SEPA payments are carried out, two-thirds of the participating companies answered that they send SEPA payments in xml-format to the bank (message type pain.001.00x....) while the remaining one-third is using a conversion service at the bank's site (e. g. sending SWIFT MT101 or local format files to the bank, which the bank then carries out as a SEPA payment).

This fact gives banks the opportunity to offer payment-related services such as format conversion while companies can benefit from an accelerated adoption of SEPA. The usage of a format conversion can be a way to adopt SEPA in a phased approach, starting with a soft adoption where only the master data of IBAN and BIC needs to be aligned with the bank's mapping services. Like every additional process step, the conversion bears some disadvantages: the risk of failure, mismatch in mapping and increased complexity of returned payments. For direct debits, this is not just a pure conversion topic as mandates also need to be collected and administrated.

3.2.5. SEPA Adoption Outlook

The SEPA adoption process is running at full speed as 85 % of companies participating in this study have already implemented SEPA or will do so in the near future.

Figure 6: SEPA adoption progress



Assuming that SEPA adoption will be mainly carried out for SEPA Credit Transfer payments, this is in line with ideas at the European legislative level on abolishing national credit transfer payment formats by the beginning of 2013. Plans to set the beginning of 2014 as the end of national direct debit formats seem rather optimistic, considering the level of SEPA Direct Debit adoption described above.

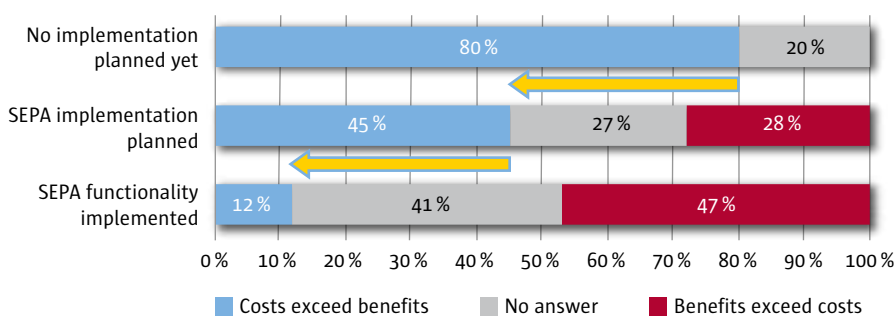
The remaining 15 % of companies not planning to adopt SEPA in the near future are predominantly companies with less than 5,000 employees and more than 1,000 employees. Political discussions are ongoing to set an end date which will compel the remaining companies to adopt SEPA.

When asked for the reasons for not implementing SEPA payments, the major argument was an unsatisfactory cost-benefit ratio while only a few participants wanted to wait for higher acceptance or did not yet have the payment infrastructure available to manage the new formats.

3.2.6. Perception of Costs and Benefits for SEPA Adoption

The costs for SEPA adoption are estimated differently by companies that have already carried out the implementation and those who have not yet started the adoption process.

Figure 7: Perception of SEPA adoption costs and benefits by adoption progress



Companies that do not plan to implement SEPA in the near future for the most part expect higher costs than benefits while this estimation is shared by less than half of the companies (45 %) that plan to implement SEPA. After the successful implementation of SEPA, only a minority of 12 % share the opinion that costs related to SEPA would exceed the benefits. This leads to the conclusion that adoption has been started or even completed by companies that see a clear benefit in using SEPA. Additionally, there can also be a shift in the perception of the costs and benefits after adoption that the implementation of SEPA is rather beneficial.

Those companies that have already implemented SEPA with benefits exceeding the costs expect a return on investment in a time range of between half a year and three years.

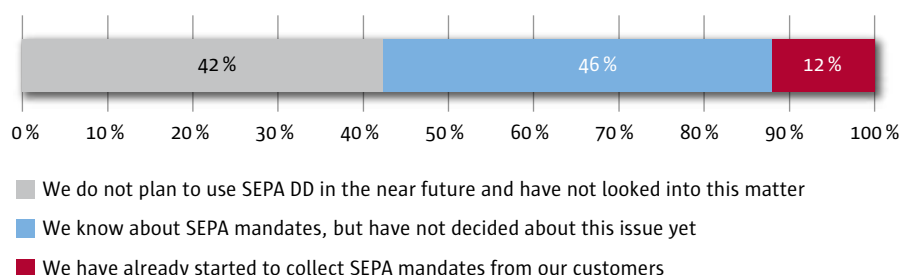
The study shows that the companies are split in two groups: the SEPA adopters and those companies that see no, or not enough, benefits in implementing SEPA. The adoption process will probably slow down as companies that do not plan to implement SEPA in the near future will complete the adoption based on external pressure from banks no longer accepting national formats. Therefore, an official deadline for the acceptance of national formats will be important for finalizing the SEPA adoption process as soon as a critical mass of users has been reached. The question is not if an end date will come but whether it will be a firm deadline or a transition phase. In the end the remaining companies will be forced to switch to the new payment formats.

Another interesting result is that a significant number of the companies that had implemented SEPA did not perform a business case and cost/benefit analysis before starting the project. It means 41 % of the responding companies, which have already implemented SEPA, made the decision strategically as a 'must-have project'. Those companies that have not started to migrate to SEPA yet are potentially losing the chance to deliver additional value to their business.

3.2.7. Adoption of SEPA Direct Debit and Mandate Management

The SEPA Direct Debit Core Scheme was launched in November 2009 and therefore started almost two years later than the SEPA Credit Transfer. Alignment for the scheme between the SEPA countries was more challenging from a regulatory and process-harmonization perspective as local law for direct debits needed to be changed or established in all SEPA countries. With SEPA Direct Debit it is mandatory to own a valid mandate for each SEPA Direct Debit transaction. The customer needs to be informed and the payment file needs to be sent to the bank, both within a predefined timeframe. Administration of the mandate makes the SEPA Direct Debit adoption more complex than SEPA Credit Transfer and the participating companies deal with this requirement in different ways.

Figure 8: SEPA Direct Debit adoption and mandate management



As shown earlier, SEPA Direct Debit adoption is lagging behind SEPA Credit Transfer adoption as only 12 % of the companies have started the process of collection of mandates.

The effort required for SEPA mandate management was mostly rated as 'high' in the survey and seen as the major reason for not using SEPA Direct Debit at present. Mandate management requires much more than just creating a payment file with correct bank identifier and account and is therefore organized as a separate work stream in many SEPA implementations.

The finance industry is of course more advanced than other industries in SEPA Direct Debit adoption as the banks had to be ready with SEPA Direct Debit adoption by November 2010. In other industries, even if mandate collection had not already started, SEPA Direct Debit was, at the very least, being investigated and considered.

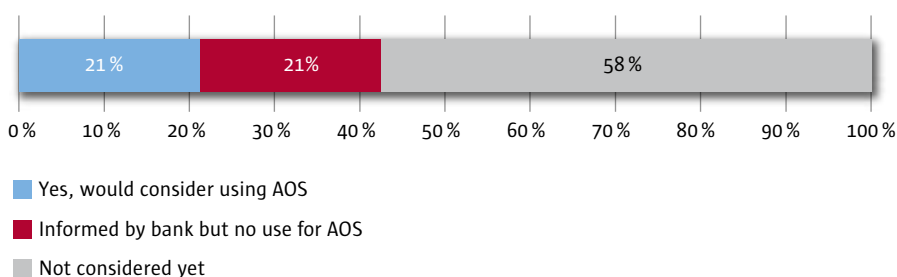
3.2.8. Additional Optional Services for SEPA Direct Debits

The European Payment Council states in the SEPA Direct Debit B2B and Core Rulebook that the scheme recognizes that individual SEPA Direct Debit participants and communities of SEPA Direct Debit participants will provide complementary services, based on the scheme, so as to meet further specific customer expectations. These are described as Additional Optional Services ('AOS'). The following two types of AOS were identified:

- Additional Optional Services provided by participants to their customers as value-added services which are nevertheless based on the core payment schemes. These AOS are purely a matter for participants and their customers in the competitive space.
- Additional Optional Services provided by local, national and pan-European communities of participants, such as the use of additional data elements in the ISO 20022 XML Standards. Any community usage rules for the use of the SEPA core mandatory subset of the ISO 20022 XML Standards should also be mentioned in this context, although they are not AOS per se. Other AOS may be defined, for example relating to community-provided delivery channels for customers.

These AOS can be used as a competitive advantage by banks when offering value-added services to customers. Therefore, one question in this survey was if companies would consider using Additional Optional Services provided by their bank, for example reversals when implementing SEPA Direct Debit.

Figure 9: Readiness to using Additional Optional Services for SEPA Direct Debits



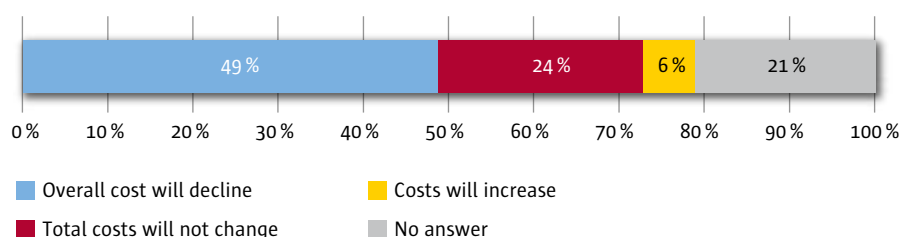
Every second company that received some information from their banks would consider using AOS for SEPA Direct Debit while 58% of the interviewed companies had not been offered AOS or were indecisive about the use of these services. Considering that SEPA Direct Debit adoption is significantly lagging behind SEPA Credit Transfer adoption, it seems to be too early for the majority of the companies to answer the question on the possible use of AOS for SEPA Direct Debit.

For banks there is great potential to sell their services as 21% are open to AOS and 'only' need to be convinced of the added value of the services offered.

3.2.9. Long-term Cost Perspective for SEPA Credit Transfer and Direct Debit Payments

While SEPA adoption is continuing and progressing despite all discussions about costs and benefits, it is interesting to see that the vast majority of the companies have a neutral or positive outlook regarding payment costs in the course of time.

Figure 10: SEPA payments long-term cost perspective



In the long run only 6% of all companies expect that costs for SEPA Payment Processing will increase markedly while almost half of the companies expect even a decline in cost. This is in line with the goal of the European Payment Council to reduce costs for Payment Processing.

3.3. Introduction to Corporate Payment Processing and Management

In the area of corporate Payment Processing, harmonization and centralization has been taking place for a decade. These processes can be split into two areas – group internal payments between subsidiaries and group external payments where either one party is a company not belonging to the group or where there is an external cash transfer between group companies (e. g. for cash concentration purposes).

The location of payment execution can be completely decentralized in each subsidiary, grouped by regions or completely centralized. Which organizational setup is best depends on the business model and global reach of the company.

When implementing an In-house Bank or Payment Factory the usual objectives are:

- Group-wide unified and standardized payment processes
- Standardization of payment formats and centralization of bank interfaces
- Increased level of automation
- Harmonization of the bank structure
- Optimization of Working Capital
- Centralization in a Shared Service Centre

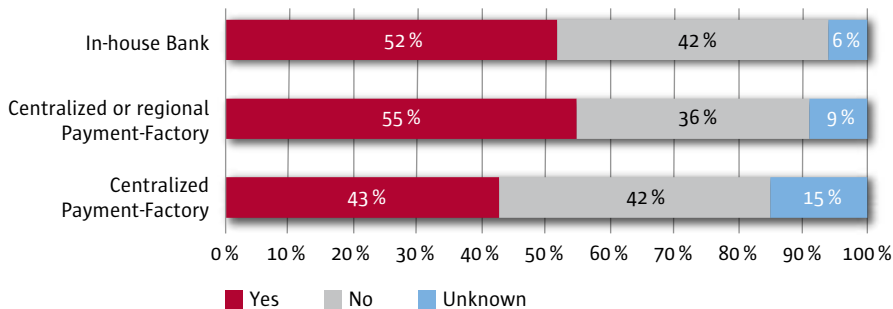
The benefits that can be leveraged by that in general are:

- Reduction of process costs and complexity by improved and harmonized processes
- Stronger governance and compliance
- Group-wide increase in efficiency, transparency, quality and security
- Reduced number of bank accounts, minimizing bank charges and transaction costs
- Improved management of group liquidity and group internal financial allocation
- Support of centralized risk and hedge management
- Better conditions with master banks (economies of scale)

3.4. Survey results on Corporate Payment Processing and Management

In the survey, the organizational status for processing of group internal and external payments has been explored.

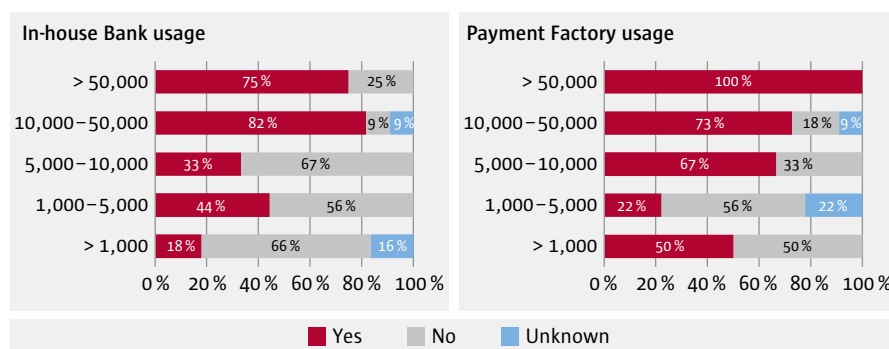
Figure 11: Organization of internal and external Payment Processing



The results show that more than half of all companies use a regional or even centralized (global) organization for internal or external Payment Processing.

Smaller companies often have a centralized unit executing all external payments for the whole company. This can be seen in the following figures where the use of an In-house Bank and Payment Factory is split by company size represented by the number of employees.

Figure 12: In-house Bank and Payment Factory usage by company size (number of employees)



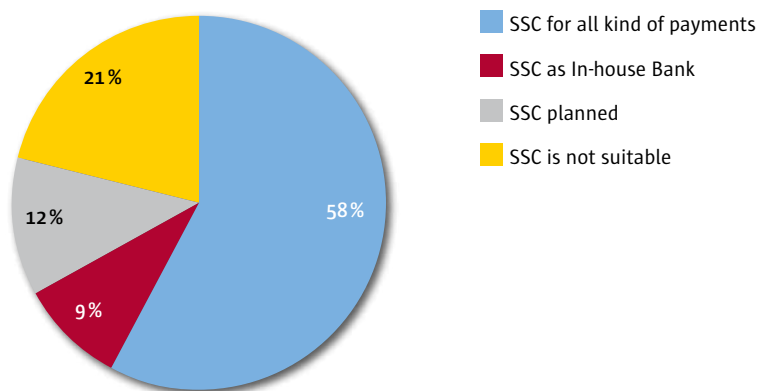
The results clearly indicate that the bigger the company, the higher the probability that it uses an In-house Bank and Payment Factory. For smaller companies without or with only a few subsidiaries, an In-house Bank is not suitable, as there is not much to centralize.

The processing of external payments is a centralized function at half of the small companies, partly decentralized in medium-sized companies and again bundled in regional or central Payment Factories for large companies.

3.4.1. Shared Service Centre Usage

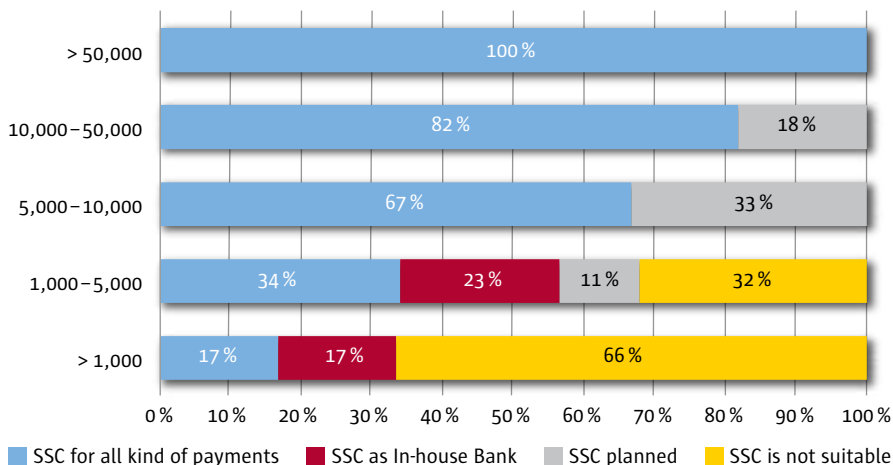
Using a Shared Service Centre (SSC) for Payment Processing and Cash Management means centralizing and streamlining these processes and thus realizing economies of scale. This is also often an indicator for the progress on other issues in the payment area, such as SEPA implementation.

Figure 13: Shared Service Centre for Payment Processing



Deciding in favour of running a Shared Service Centre for payment transactions depends on the structure and size of a company. The results of the study show that two thirds of the companies use a Shared Service Centre (SSC) and even more plan to establish such a centralized service while less than a quarter of the companies are of the opinion that there is no use in centralizing Payment Processing in a SSC. The reason for not setting up a SSC is strongly related to the size of the company, as can be seen by splitting the statistics above based on company size represented by the number of employees.

Figure 14: Shared Service Centre by company size



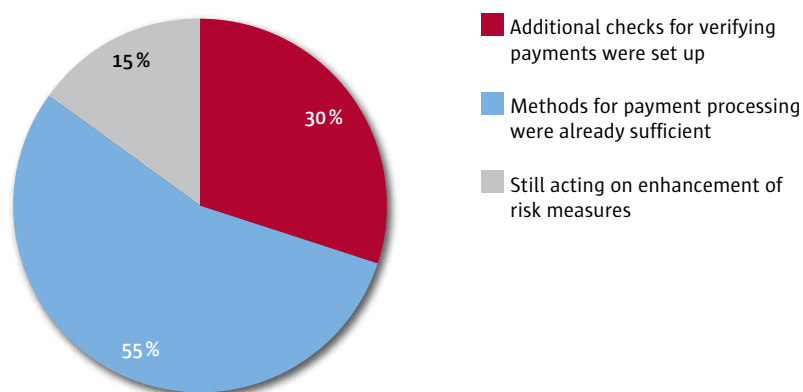
For companies with more than 5,000 employees there is a clear preference to centralize payment functions in a SSC. By now many of these bigger companies have centralized their processes and the necessary infrastructure in the area of payments, or they will do so in the near future. There is such a high volume of payments of several kinds taking place in these larger companies that it pays off to run a SSC for realizing economies of scale by centralization and specialization.

According to the results of the study, companies that streamline their payment processes by using a Payment Factory or In-house Bank mostly run that department as a Shared Service Centre. Nevertheless, there are limitations with regard to the company size as two-thirds of the companies with 1,000 employees and still one-third of the companies with 1,000 to 5,000 employees state that the implementation of a SSC would not be suitable for their company. This is in line with the results of this study above, where a significant size dependency for setting up an In-house Bank or Payment Factory was identified. For smaller companies these functions are often performed by a centralized unit at the company headquarters.

3.4.2. Risk Management Measures for Payment Execution

Due to the global financial crisis, Cash Management, Liquidity Management and Financial Risk Management have become even more important than they already were. The sub-prime mortgage crisis and the subsequent governmental euro crisis had a significant impact on banks, asset management companies and other corporations, as the write-off of holdings of sub-prime-related securities led to a massive reduction in bank capital, which in turn reduced the liquidity available to companies for credit and loans to fund their business. In many companies this led to a reassessment of internal Risk Management and risk control measures. The following figure shows if and how the participating companies have extended Risk Management measures in Payment Processing.

Figure 15: Risk Management measures in Payment Processing due to the global financial crisis



More than half of all companies did not revise their internal controls despite the financial risk. This is surprising as the discussion about potential bankruptcy of system-relevant

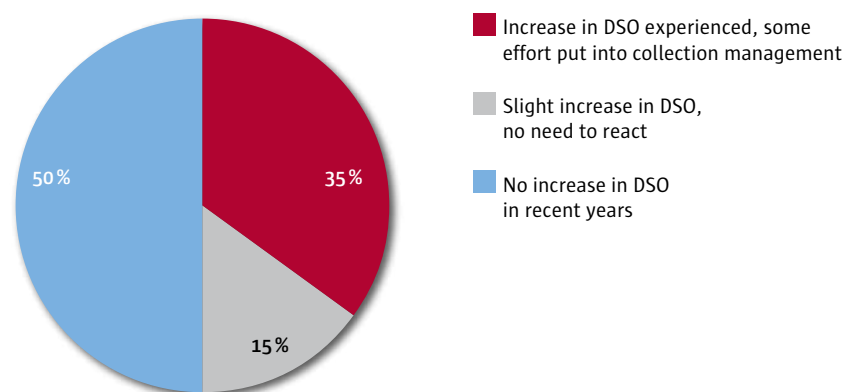
banks has not come to an end yet and the stability of house banks (or master banks) is always critical for all companies. Less than one-third of the responding companies extended Risk Management measures due to the financial crisis.

Even if payment execution and counterparty risk is just one issue, sufficient liquidity needs to be secured at all times, especially in financial crunch times. Liquidity risk is managed with bank lines, (syndicated) facilities, loans or corporate bond placements. In all these processes, banks are involved and internal controls need to match the market situation as well as regulatory requirements.

3.4.3. Working Capital Management and Days Sales Outstanding (DSO)

An important factor to Working Capital Management is the monitoring and steering of Days Sales Outstanding (DSO) and Days Payable Outstanding (DPO). Against the background of the financial crisis many companies optimized their working capital by paying invoices after due date. The participants of the study were asked to share their views on whether they had experienced an increase in DSOs with their customers over the period of two years and whether they had applied additional counter-measures or functionalities to react to that.

Figure 16: Changes in Days Sales Outstanding (DSO) and measures taken



Half of the companies that answered this question recognized an increase in DSOs over the last two years. Despite putting some additional effort into improving their Collection Management for incoming payments, 57% of these companies did not extend their Risk Management measures during the financial crisis.

3.5. Introduction to Cash Management

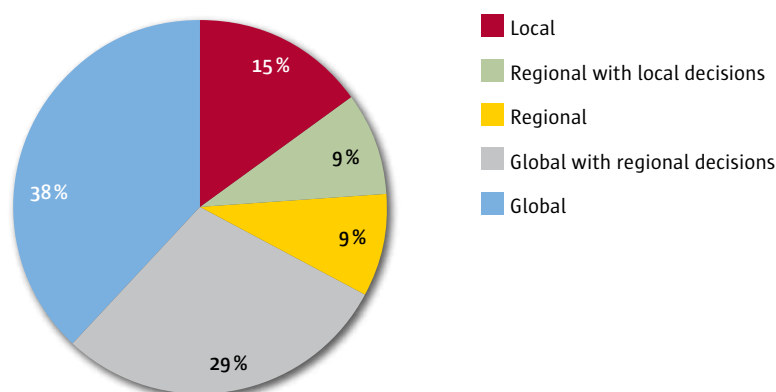
Cash Management gives an overview over a company's short-term liquidity situation. It can also provide information on the development of the company's mid-term liquidity in the near future. Having an up-to-date and exact view over bank account balances and short-term payables and receivables is essential for getting an accurate overview of available liquidity for carrying out payments as well as funding or investment activities. Performing external payments that are not only processed within the In-house Bank is one of the reasons why there is a strong need for considering the liquidity situation on different kinds of accounts. Treasurers are aiming at arranging the right amounts in accordant currencies at the right time on their bank accounts. These account balances are volatile throughout the day, not only because of payments initiated by a company of the group but also because of incoming payments from their customers.

3.6. Survey results on Cash Management

3.6.1. Degree of Centralization of Cash Management

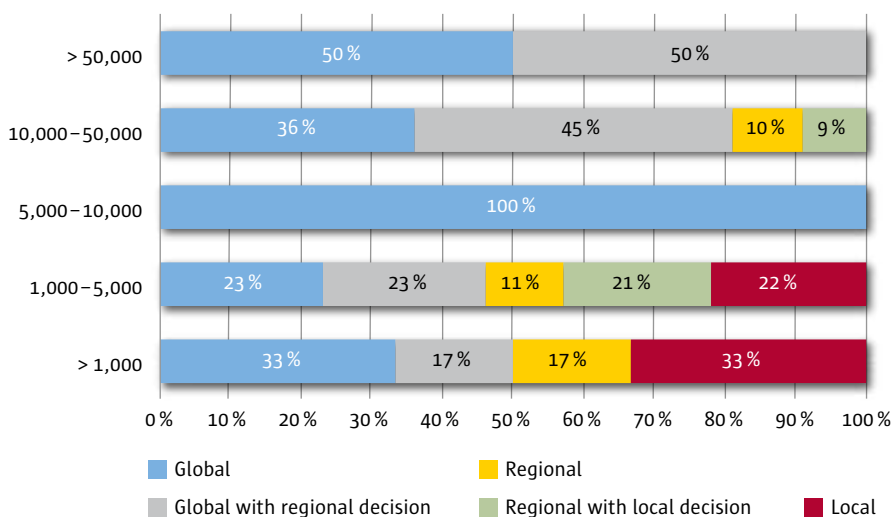
Companies always have to decide whether they operate their Cash Management locally, regionally or even globally on a fully centralized basis. This means that a balance needs to be found between on-site Cash Management activities with deep knowledge of local requirements and bank practices on the one hand, and centralized Cash Management on a global basis with a group-wide management of liquidity and financial risks on the other hand.

Figure 17: Degree of centralization of Cash Management



Regarding Cash Management centralization, the study shows that more than two-thirds of the responding companies operate a global Cash Management. More than half of the remaining companies run a decentralized regional Cash Management organization and only 15 % operate a local Cash Management. In order to see if the usage of local Cash Management teams depends on company size, a split by employee numbers shows the following result.

Figure 18: Degree of centralization of Cash Management by company size (number of employees)



The split by company size indicates that centralization is very advanced in general and especially in companies with more than 5,000 employees. Despite all centralization, between 45 % and 50 % of the large companies with more than 10,000 employees take regional expertise into account when making Cash Management decisions.

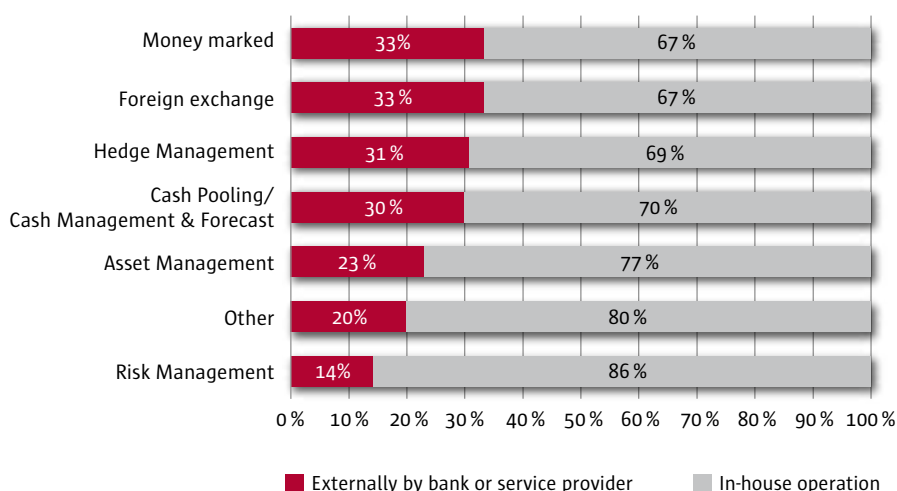
As only 15 % of the responding companies operate local Cash Management teams, the split by company size clearly shows that only smaller companies with less than 5,000 employees use local Cash Management organizations. This reflects the business model and organizational structure of the companies, as it was exactly those participants of the study who indicated that a Shared Service Centre for Payment Processing would not be applicable for them.

In summary, the centralization of Cash Management functions has in recent years been optimized to a high degree and reasonable level. Therefore further centralization seems improbable as this also implies some distance to local markets and regional expertise.

3.6.2. Treasury Services Provided by Internal Operations or by External House Bank or Service Provider

There are several services in the field of Cash and Treasury Management that companies can source from external banks and other service providers. The alternative would be to perform all those operations and services internally. The following figure assesses the level of business process outsourcing in the area of Cash and Treasury Management.

Figure 19: Treasury services provided internally or by external house bank or service provider

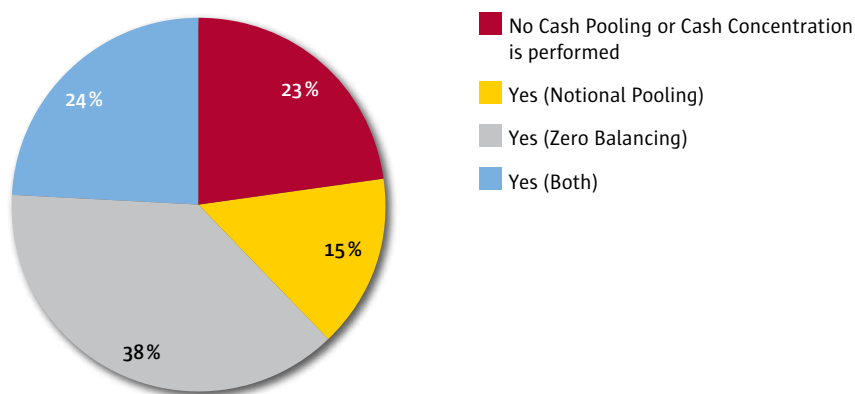


The study shows that up to one-third of all companies use external services provided by their house banks in order to manage or at least support internal Treasury and Cash Management operations. The results also indicate that there is a wide range of different services being used. The area with the lowest level of outsourcing is Risk Management, which is not surprising as it requires access to sensitive data and has the highest level of complexity. Rather surprising is the fact that only 30 % of the companies state that they use cash pooling as a service from their banks. This leads to the conclusion that cash pooling is to a high degree actively triggered by the responding companies, as 76 % of them use cash pooling in one way or the other, as shown in the next chapter.

3.6.3. Performing Cash Pooling or Cash Concentration

The participating companies were asked about the use of different kinds of cash pooling instruments, each with the aim to concentrate liquidity.

Figure 20: Performing Cash Pooling or Cash Concentration



Three-quarters of the companies perform one or several kinds of cash pooling, where only Zero Balancing leads to payment transactions. Handling many payment transactions on a presumed large number of house bank accounts boosts the potential effectiveness of performing Cash Pooling or Cash Concentration and therefore makes it a necessity for bigger companies. A split by company size of the above statistics again shows a clear dependency on the company size, as only companies with less than 5,000 employees indicated that they would not perform Cash Pooling or Cash Concentration.

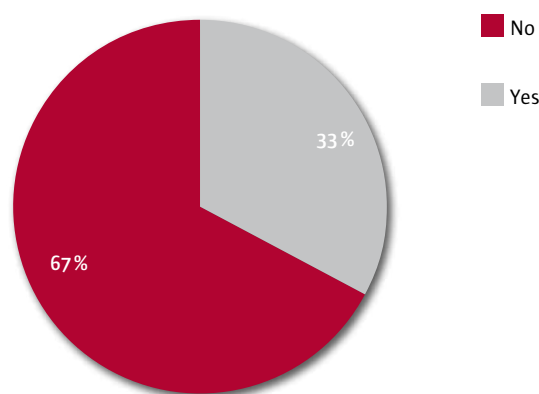
These companies were asked about the background of their decision for not using Cash Pooling or Cash Concentration. Three-quarters stated that they neither use Cash Pooling nor Cash Concentration because they do not see any reason to perform these activities. Other explanations were limitations imposed by corporate policy or tax regulations. No respondent named restrictions due to local law or a lack of appropriate tools.

There are different possible scenarios in which there is no need for performing Cash Pooling or Cash Concentration. Generally there might only be a small number of accounts used or there are specific reasons why money is kept in several bank accounts. When subsidiaries operate more or less independently in their local markets with rather balanced in and outgoing cash flows per currency, there could indeed be only a limited use for Cash Pooling, e.g. when earnings are only transferred once a year in the form of a dividend.

3.6.4. Details of Using and Processing Cash Pooling or Cash Concentration

Companies that perform Cash Pooling or Cash Concentration were asked about their activities concerning other countries than those of the SEPA.

Figure 21: Usage of Cash Pooling or Cash Concentration beyond the SEPA



Two-thirds of the participating companies already perform Cash Pooling or Cash Concentration beyond the SEPA countries. More than 80% of those companies responded to the question about the degree of centralization of their Cash Management with the information that they also carry out globally-managed Cash Management to effectively control the disposition of liquidity in bank accounts in several countries.

This leads to the following conclusions:

Some of those companies that do not yet perform Cash Pooling or Cash Concentration will rethink their decision based on the new possibilities offered by SEPA instruments. The introduction of the ISO 20022 format for SEPA payments will facilitate an increase in Cash Pooling or Cash Concentration transactions even in currencies other than the euro. Companies can directly debit their local bank accounts by sending SEPA Direct Debit payment orders to these house banks where they wish to pool their liquidity. Using such a process, they no longer need to take local bank connections and local payment formats into account.

Those companies that do Cash Pooling and Cash Concentration and do not use an automated service provided by their banks can reduce the number of payment formats by using the ISO 20022 standard, leading to a considerable reduction in complexity, bank charges and IT infrastructure cost.

4. Summary and Outlook

The European Union exerted significant pressure on the banking industry by introducing SEPA. The usage of the ISO 20022 standard as a modern XML-based payment format is pushing this standard far beyond SEPA. Corporates can and already do benefit from this development through banks that have already reduced their fees, by reducing domestic and cross-border payment formats and thus reducing complexity and IT interface and infrastructure costs.

The trend for corporates to centralize the execution of external payments still prevails. The pure settlement of payments for a group is more and more organized in Shared Service Centres similar to the reconciliation of open items in Accounts Payables and Accounts Receivables in the past. Integrated systems in these centres enable cash managers to steer liquidity on a short and medium-term basis.

The cash in bank accounts is increasingly concentrated and pooled in group target accounts either by contracts with banks or self-initiated by Cash Management software. The management of cash and liquidity as well as FX exposure is a central treasury function, often in connection with regional centres, depending on the global reach of the corporate group and can be supported by an In-house Bank.

The major obstacle for global Cash Management and In-house Banking are countries with restrictions on cross-border cash transfers. In the long run they will either slowly open their markets (such as China for example) or fall behind in their development. The task remains that, country by country, corporates need to consider local restrictions and risks involved in including subsidiaries in these countries in cash pools.

Currently, already more than half of the companies stated that they did not need to adjust their Risk Management measures in the financial crisis. The increase in centralization and harmonization of payment processes empowers Governance Risk and Compliance Management to be progressively more efficient. Fraud is getting difficult in an integrated process where every transfer has an audit trail in the Financial Supply Chain ensuring there is no payment without posting, no posting without invoice, no invoice approval without purchase or sales order.

In terms of business process outsourcing, only one-third of the participating companies use external bank services to support their internal treasury functions such as FX Exposure and Hedge Management, Cash Pooling or Risk Management. The majority of the companies perform these tasks with the help of internal resources and internal systems with limited interfaces only. The technical basis for service-oriented architecture (SOA) already exists in many ERP and Treasury Systems. While companies increasingly integrate their supply chains with their business partners, this process is just starting in the area of Financial Supply Chain Management.

The migration to SEPA can open significant chances for improvement as the majority of responding companies that have already implemented SEPA perceive the benefits to be much greater than the costs. Considering SEPA not only as a mandatory change will create the opportunity to harmonize and streamline internal and external payments by initiating an overall redesign of the company's payment infrastructure and cash collection processes and to deliver additional value to the business.

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