

European Cash Management Strategy 2008

Jasper Savelkoel, KBC Bank

This article considers current trends affecting the European cash management market and how banks and corporates are addressing these challenges.

As we begin a new year, it is an appropriate time to consider the developments currently affecting the European cash management industry. This is an important task for both banks and corporates who must adapt and align their business strategy to contend with these market trends.

The ongoing liquidity squeeze is a significant event that has certainly affected the cash management industry and re-instated credit and funding as a priority for corporates. Consequently, there is growing demand for zero-balancing solutions, which allow corporates to sweep all of their daily balances into one central account. Interestingly, this trend is particularly prevalent between third-party banks, another indication that corporates continue to seek ways to improve efficiencies within their cash management operations.

This is also highlighted by the ongoing centralisation of corporate treasury activities, with small and mid-sized companies following in the footsteps of their larger counterparts. This process requires a step-by-step approach, however, and corporates need to re-organise their operations on a regional basis first before embarking on pan-European solutions.

Banks are also offering an increasing range of electronic and web-based services and products. This is driven by corporate demand for integrated, real-time solutions to increase STP within their operations and processes. The standardisation of reporting formats will therefore be an ongoing priority for the industry, particularly corporates who operate cross-border in multiple countries.

In addition, banks are extending their traditional cash management service offering to support their corporate customers' electronic financial and administrative processes in a standardised and multi-country way. This will also help decrease costs for customers who want to centralise their treasury activities.

How Will SEPA Affect the Market?

The introduction of the single euro payments area (SEPA) is an obvious focus for both banks and corporates within the European cash management industry from a commercial and technology perspective.

Pan-European competition will increase among banks who will start to aggressively cross-sell and 'package' payment products across their service offerings. While banks will still participate in some form of lending arrangement or syndicated loan, payments transactions and volumes will become more important. As a result, the market will enjoy lower prices and fees for payment products, and smaller companies will start to require international cash management solutions.

As mentioned earlier, corporates in general will increasingly seek to centralise their treasury functions on a pan-European level through payment factories, although this will be a gradual process for a number of reasons. First, approximately 20% of the local payment instruments in the SEPA countries remain out of scope, which means that corporates will have to maintain local instruments in various countries for some time. Secondly, the new XML-based bank-to-customer reporting standard has only been defined and not yet agreed - another stumbling block to centralising payments. Thirdly, the industry must contend with the delay to the introduction of the SEPA Direct Debit (SDD), which will not be implemented until November 2009. The potential benefits derived from centralising the accounts payable process will, therefore, probably be the main driver behind corporates establishing a (pan-European) payment factory.

In light of these unresolved issues, the industry faces a long transition period where SEPA formats and domestic formats will co-exist until 2012 or even 2015. This is an expensive prospect for banks and corporates who will have to manage both sets of systems and instruments. The challenge for the European cash management industry is ensuring that the migration period is as short as possible. The implementation of the SEPA Credit Transfer (SCT) on 28 January this year is a major milestone and heightens the importance of developing an appropriate SEPA strategy for dealing with the migration period now.

Corporate Response to SEPA

The first decision for all corporates to make is whether they want to be an early adopter with regard to the new SEPA instruments. In order to make this fundamental choice, corporates should evaluate how they organise their treasury activities now as well as their future plans, and SEPA provides the ideal opportunity to do this.

Some corporates take a basic approach and simply consider what they need to do in order to become SCT compliant within their operations. A more effective approach, however, would be to consider how to make your treasury operations more efficient as a result of SEPA and the introduction of the SCT.

It is also important to consider the technology that is available, such as e-banking systems and portal solutions from banks, which can help corporates achieve their desired treasury model.

In addition, corporates should re-evaluate their banking relationships in the context of SEPA. How many do you have per country? Do you need all of them and how can they be optimised? This will be a gradual but progressive process that will extend over the migration period and the reduction of bank accounts will certainly mean that the use of domestic cash pooling solutions will become less common, as corporates seek regional rather than domestic solutions.

Clearly, there are numerous issues to consider and the introduction of the SCT is the ideal time for corporates to consider how to prepare for SEPA with the help of their banks and software suppliers. Your decisions going forward will also depend on your corporate culture and each corporate must formulate a strategy that suits its existing organisation and management style.

What Should You Expect from Your Cash Management Bank?

Cash management is now perceived as the number one 'anchor' within the bank-to-corporate relationship compared to 10 or 15 years ago when lending was the most important differentiator. This will become even more pertinent post-SEPA, as banks offer standardised pan-European solutions rather than fragmented domestic solutions.

Corporates also attach more value to bank relationship management that meets their expectations within their day-to-day operations in every European country. Moving from a decentralised regional model to a pan-European one is a complex task and corporates will be more likely to work with a bank that can deliver the same standard of relationship management on a pan-European level as they do on a domestic level.

A related trend is the increasing focus on cash management in the emerging markets, for instance within central Europe and Russia. The ability to offer cash management services such as zero balancing and a single pan-European e-banking platform in these regions will be an important strength for banks to demonstrate to corporates.

When we consider geographic coverage, the partner bank approach has proved to be a successful model by delivering a standardised, cost-efficient cross-border payment solution to corporates. At KBC, for instance, in addition to our network of central European banks and western European affiliates and branches, through IBOS1 we have established a pan-European partner bank solution for customers. This allows us to meet local banking needs in each country through the harmonised platform we have implemented to deliver standardised remote account opening services and execute all transaction banking products.

In reality, to some extent, most corporates have a decentralised structure and this is why the partner bank model provides an appropriate approach by supporting local operations through local banks at the same time as providing the benefits of global cash concentration solutions.

Other issues that corporates should consider in their corporate-to-bank relationships going forward include the reconciliation of electronic output to their ERP systems, risks related to the degree of bank dependency/concentration of exposure and straight-through processing of transactions.

Future Trends

- *Corporate access to SWIFT is a growing phenomenon and one that offers corporates numerous benefits. It has become an accepted solution for large corporates but mid-sized companies are also now showing an interest, although implementation costs still seem prohibitive. Corporates should follow this area closely for further developments.*
- *Supply chain products from banks are increasingly being managed electronically. For instance, e-invoicing initiatives and the SwiftNet TSU are helping corporates make their supply chain as efficient as possible and this is a significant trend to monitor in future.*
- *Corporates will increasingly demand greater transparency of bank charges.*

- *More banks will offer their electronic banking applications, such as trade finance, money market funds, FOREX and e-banking, through one single web-based portal in order to make connectivity easier for corporates.*

Conclusion

The European cash management industry is undergoing an unprecedented amount of change and this is set to continue. Against this backdrop of continuing development, by taking a holistic view of their cash management structure and operations, corporates will be well positioned to address the challenges ahead.

Corporates should demand more from their cash management banks. They should seek standardised, integrated and electronic pan-European products and services across all countries in which they operate that is underpinned by a dedicated, multi-country customer relationship model that manages the full delivery of these services. Indeed, the combination of best-in-class services with a high standard of customer support will be a fundamental factor of all bank-to-corporate relationships within the European cash management market going forward.

1 The IBOS Association is an international banking alliance focused on providing corporate customers with international cash management solutions. IBOS is based on its 12 members and their subsidiaries, each of which is a supplier of local banking services in their domestic markets.