A GXS INSIGHTS ARTICLE

Ten Forces Transforming Corporate Banking Connectivity

GXS Market Perspective

The past five years have witnessed the emergence of a number of new operational models, regulatory changes and technology paradigms in the corporate treasury and banking sector. The result is radical changes to the structure of treasury functions within multi-national corporations. The changes are also impacting the relationships between corporations and banks—both the way in which banking products are selected and the service level expectations treasury organizations hold for financial institutions are evolving. There is also a significant paradigm shift in the technical approaches used to exchange information between corporations and their cash management banks.

GXS has compiled a list of the ten primary forces transforming the way in which corporations and banks communicate electronically. The list is based upon studies of market-leading multi-national corporations based in Western Europe and the United States. The ten forces are not mutually exclusive, but rather interdependent. Five of the forces outlined are changes that affect overall corporate banking practices—new organizational structures, payment strategies and management models. The remaining five are technology developments that are impacting the electronic communications between banks and corporate clients.

Transforming Corporate Banking Practices (#1-5)

1 **Conversion from Checks to EFT**—Corporations are rapidly migrating away from checks and paper instruments to Electronic Funds Transfer (EFT). The most significant transition is occurring in the US, which historically utilized checks as the primary B2B and B2C payment instrument. Credit cards, debit cards, on-line bill pay and lockbox-based image conversion are rapidly driving B2C payments to EFT. Adoption of EFT in the B2B payments segment has been slower. However, procurement cards and Automated Clearing House (ACH) are quickly becoming the primary payment instruments for large corporations. The result is that corporations must communicate a significantly higher volume of electronic payment instructions to financial institutions than with checks. For large multi-nationals, the net increase in number of payment messages sent to banks could be in the millions per year.

2 **Payment Factories**—Historically, corporations have maintained separate Accounts Payable (A/P) organizations in each country to provide the necessary local tax and payment expertise. However, there is a growing trend towards centralizing A/P functions into shared service centers, otherwise known as "payment factories." The shared service centers enable opportunities for higher levels of efficiency in the back office. Productivity improvements can be gained by eliminating country-level staffing and by embracing best practices on a regional level. Further savings can be gained by relocating A/P functions to either captive or outsourced service centers in lower cost geographies. Transitions to centralized, payment factories require staffing and procedural changes, and standardization of A/P applications. Many multi-national corporations are re-evaluating their approach to payment processing as they transition to shared service centers.

3 **Centralized Treasury**—In addition to creating shared service centers for A/P, corporations are re-evaluating organizational models for the treasury function. Many multi-national enterprises are centralizing treasury groups on a regional or global basis. Historically, corporations allowed each country to manage its cash needs locally. Centralization enables a number of efficiencies in the areas of cash forecasting, foreign exchange and cross-border payments. However, to realize the benefits, corporate treasury organizations need access to real-time information on account balances, investment holdings and securities prices from their financial institution.

Consequently, the transition to centralized treasury models is driving higher demand for straight-through processing of information between corporations and financial institutions.

4 **In-House Banking**—Many large corporations are establishing in-house banks to complement centralized treasury functions. These banks are not officially regulated or licensed financial institutions. However, they act much like a commercial bank by offering payment processing, liquidity management and collections functions to various subsidiaries of a large, global corporation. The creation of an in-house bank substantially impacts the corporate banking interface. Instead of each operating company routing payment transactions directly to a local bank, all disbursements are channeled through the in-house bank at headquarters. Centralized payment processing applications managed by the treasury group are configured to evaluate opportunities to reduce banking fees. Multi-lateral netting, supplier payment consolidation and local funding techniques are examples of services provided by an in-house bank.

5 **Consolidation of Banking Relationships**—Along with centralization of internal functions, multi-national corporations are also rationalizing the number of banking relationships they maintain. Changing regulations in the US, the European Union and countries such as China have enabled numerous financial institutions to develop a global footprint. Consequently, multi-national corporations no longer need to establish local banking relationships in each country of operation. Instead, corporations can consolidate banking providers to the minimal number appropriate to cover the necessary geographic footprint and offer the appropriate product features. As part of the consolidation process, corporations are demanding that financial institutions provide lower processing fees, higher service level agreements and stronger technical integration. Corporations are mandating a minimal set of technology requirements which financial institutions must comply with in order to compete for global banking contracts.

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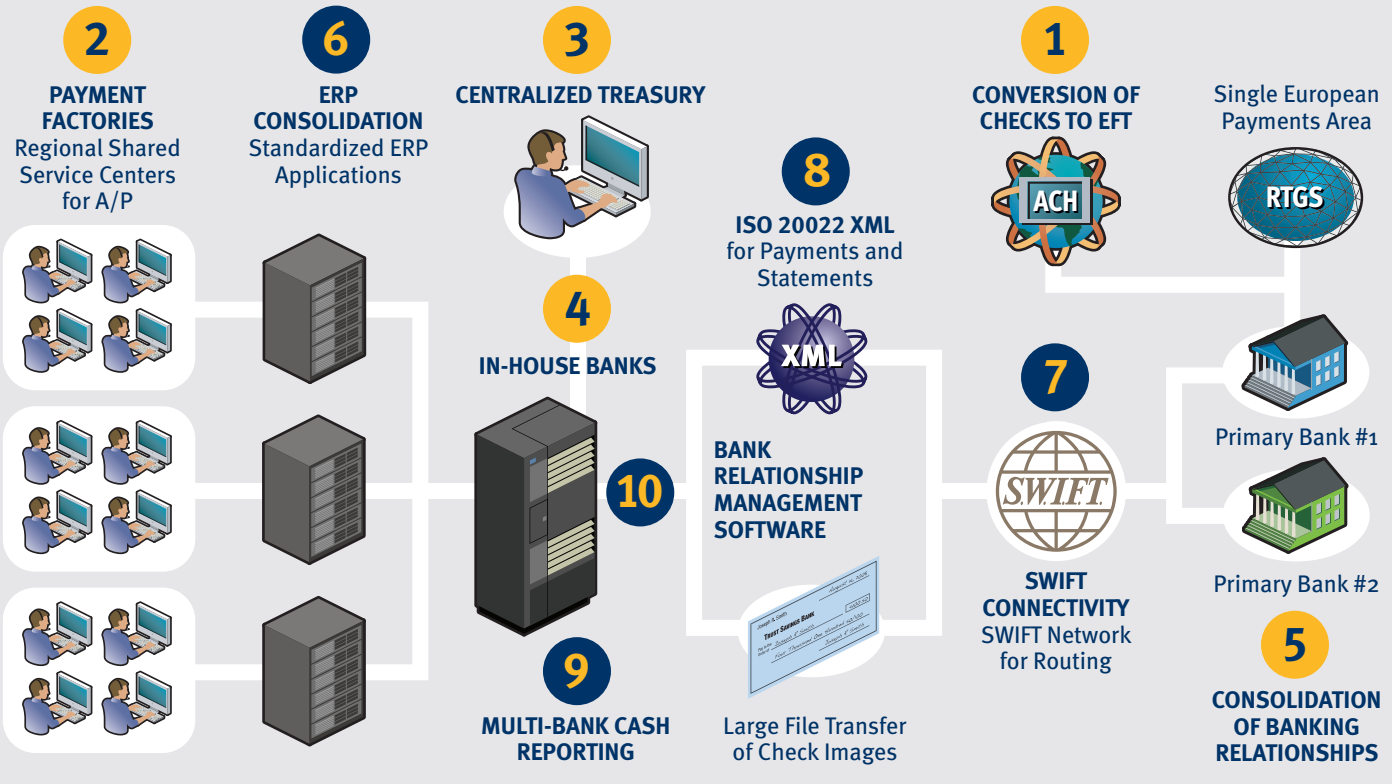

Transforming Corporate Banking Connectivity (#6-10)

6 **ERP Consolidation**—Most multi-national corporations have a project underway to standardize and consolidate the various ERP applications being utilized within their enterprise. Historically, different brands, operating companies and legal entities have operated autonomously with their own enterprise systems. Fragmentation of ERP platforms prohibits sharing of information across divisions and with headquarters. Standardization of ERP onto a common platform (e.g., Oracle 11i) enables consistent business practices across divisions and the utilization of shared service centers for back office functions. As multi-national corporations consolidate and standardize their finance, accounting and treasury modules, IT organizations are re-evaluating their approach to bank connectivity.

7 **SWIFT Connectivity**—Several hundred large corporations have registered to participate in SWIFT's corporate access programs. SWIFT connectivity can reduce the costs and complexity associated with corporate banking communications. Corporations utilize a number of different transmission mechanisms to exchange data with their banks. High volume data transfers typically occur over private lines or Internet-based file transfer. In some cases, older technologies such as dial-up connections and fax transmissions are still in use by smaller corporations. Web portals have become an increasingly popular option for bank interfaces recently. With SWIFT access, corporations can replace the broad mix of connectivity mechanisms with a single standardized approach. Messages and files can be sent to SWIFT for routing to any of the over 7,000 banks on SWIFTNet reducing cost and complexity.

8 **ISO 20022 XML**—Otherwise known as the Universal Financial Industry (UNIFI) standard, ISO 20022 XML is designed to replace the myriad of local file formats used for payment processing around the world with a single, global message schema. Today, most corporations utilize EDI (e.g., EDIFACT, ANSI X12); country specific ACH formats (e.g., NACHA in the US) or legacy banking standards (e.g., BAI, SWIFT FIN) to exchange information with financial institutions. The file formats used to send payment instructions and receive account statements vary from bank to bank. In some cases, corporations are required to send more than one type of file format to different divisions of the same bank. The UNIFI vision is for corporations to be able to utilize one message schema to exchange information with any bank in the world.

9 **Multi-Bank Cash Reporting**—One of the key benefits achieved from centralizing treasury functions is the improved cash management capabilities. Treasury personnel with visibility to all cash positions at bank accounts worldwide are better equipped to perform cash forecasting, borrowing and investment activities. Treasurers must be able to easily collect account balance information from all bank accounts in all countries. Multi-bank reporting applications developed by financial institutions and technology providers offer account aggregation services. The services consolidate end-of-day and intra-day balances for all accounts onto a single web portal or channel the information directly into a treasury workstation. Corporations armed with enhanced cash visibility can make borrowing or investing decisions earlier in the day, reduce probability of overnight idle balances and accelerate the processing of exception items.

10 **Bank Relationship Management Software**—Bank connectivity has become such a complex issue for corporations that several ERP vendors have introduced specialized software modules to simplify integration. SAP recently introduced its "Bank Relationship Management" application. The SAP module offers native support for ISO 20022 XML and SWIFT corporate access. Furthermore, the SAP application has seamless integration with the vendor's treasury and accounting modules thereby lowering the barriers to straight-through-processing with financial institutions. Out-of-the-box support for emerging standards from major ERP vendors will accelerate adoption by multi-national corporations.

Additional Forces

The ten factors listed above are revolutionizing the way corporations interface with their cash management banks. The list could be further extended to include regulatory changes such as the Single European Payments Area (SEPA), technological forces such as Large File Transfer and banking innovations such as Payments Hubs.

- **Single European Payments Area (SEPA)**—Starting in the 1990s, the European Union began the SEPA initiative to harmonize and simplify payments across the 15 countries which have embraced the Euro as the national currency. The goal of SEPA is to establish a common set of regulations, processes, standards and technologies for making payments across the Eurozone. Consumers and corporations will enjoy consistent pricing and service levels regardless of their country of citizenship and the location of their bank account. As a result, citizens and corporations will be able to make payments in any Eurozone country as easily and cost-effectively as they could in their home nation. With a harmonized approach to payments across Europe corporations will begin to shift their country-specific finance, accounting and treasury functions to broader Pan-European models. Additionally, selection criteria for banking partners and products will evolve as financial institutions expand their geographic footprint and introduce new, low-cost cross-border payment services.

- **Large File Transfer**—Corporate treasury groups are seeking more information in faster time frames than ever before. For example, in the US the rapid growth of image-based check substitution is driving demand for copies of check images to be distributed to corporations. Collections organizations retain the check images for customer service, record-keeping and exception processing purposes. Today, check images are burned onto a CD-ROM and shipped via courier to a corporation. The CD-based distribution is becoming too cumbersome and complex for most corporations to manage. Consequently, financial institutions are migrating towards Internet-based file transfer of check images. However, many banks and corporations lack the technology infrastructure to support such high volumes of data exchange. New low-cost, high-volume services for Large File Transfer are emerging, promising to further simplify corporate banking communications.

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