Executive Summary

The recent financial crisis, subsequent economic turmoil and tougher credit environment has reestablished the importance of optimizing working capital, placing the issue atop the corporate treasury’s agenda. Corporate treasuries across the globe are undertaking new initiatives to consolidated and rationalize internal operations to achieve better visibility and control over their working capital. Thus, banks that serve corporate treasuries as their clients need to keep pace with these changes and develop capabilities to deliver new and value-added services in line with their clients’ requirements.

Apart from the changes taking place at the client end, banks have to increasingly deal with external factors such as regulatory tightening and severe competition from rivals and non-banking entities. These changes, combined with forces of globalization and technological advancement, are causing business disruptions in traditional banking methodologies and operating procedures.

This white paper details the drivers that are influencing the current state of the transaction banking business and offers practical solutions and pointers that banks can leverage to deal with the challenges. It also provides a maturity model that banks can use to assess their needs and benchmark their progress in creating an integrated transaction processing platform.

Drivers Influencing Transaction Banking

To contend with trends in transaction banking, financial institutions must be cognizant of the drivers that are directly influencing their businesses. These drivers can be visualized under three categories (see Figure 1, next page).

Client Demand Drivers

To counter the challenges of liquidity constraints and the related credit crunch, corporate treasurers are consolidating their operations to optimize working capital. To attain this, they are increasingly visualizing cash and trade processing under a common umbrella. Treasuries are also looking at methodologies that are less cost intensive and involve fewer operational interventions. Shifting from traditional trade finance methodologies to open account methods is a case in point. As corporate leaders embark on institutionalizing change within their organizations, they expect their banks to provide products/services in line with their new priorities.

Regulatory Drivers

The aftermath of the global financial crisis has led to an increased focus on banking industry regulations. Banks are required, both by clients as well as internal management, to generate exhaustive compliance-related data. To do this, banks need a holistic, granular view of both their clients’ needs and internal operations. Banks
are increasingly looking for tools to help them capture complete client-side activity and provide one view of their operations – thus reducing the effort to consolidate regulatory data across different internal teams.

In addition to the direct regulatory impact, banks are increasingly focusing on industry-wide standardization initiatives such as Single European Payment Area and Payment Service Directive. This has placed an extra burden on banks to enhance their IT systems capabilities and inculcate standardization requirements into their day-to-day operations.

Enhanced Competition Drivers
As a result of increased globalization, local and regional banks are facing increasing competition from international players. In some cases the competition is not from traditional banking institutions but from non-banking players such as Bolero and Trade Card that have emerged as major competitive threats. These companies provide niche services such as multibank and open account services that were previously the exclusive bastion of traditional banks. As a result, banks are seeking levers to attain direct competitive advantages against such players.

Banks are also focusing intensely on cost efficiency. This forces them to optimize their internal operations, which, due to legacy systems or other circumstances, primarily function in silos leading to severe inefficiencies. For example, a bank with strictly demarcated trade and cash operations would not be in a position to identify the payments due on a corporate loan against an offered trade finance arrangement and adjust these payments against the corporate receivables. This would increase the number of payment iterations, leading to inefficiency.

Integrated Transaction Banking to the Rescue
Historically, corporate treasuries organize payments and cash management processes within a single subunit while trade and supply chain finance processes remain nonintegrated and function under a different subunit. This has hindered corporate treasuries from getting a holistic view of their working capital and cash positions. But with the recent focus on boosting working capital, corporate treasuries are increasingly treating cash and trade as an integrated unit. Taking a cue, banks are also integrating their silo-based cash and trade lines of business to better address corporate needs.

Figure 2 (next page) illustrates how an integrated transaction banking platform would not only encapsulate corporate treasury needs but also help the bank to respond effectively to regulatory requirements and better fortify it against industry competition.

Encapsulating Client Needs
**Corporate Treasury Optimization:** With an integrated solution, a bank can align its cash

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**Figure 1**

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**Transaction Banking Business Drivers**

- Corporate Treasury Optimization
- Open Account Trade
- Escalating Competition
- Focus on Cost Efficiency
- Tightening of Regulatory Regime
- Enhanced Focus on Standardization

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management and trade finance product suites with its client-side treasury structure. Furthermore, by integrating the delivery of closely related services banks may be able to offer clients improved visibility along the entire length of their financial supply chain – an aspect greatly valued by many clients. In addition, banks can deliver a holistic treasury solution to clients through a single platform, enhancing the client’s treasury consolidation efforts.

**Open Account Trade:** The open account method offers greater avenues to integrate payments and trade. For example, once the invoice received from the seller is approved by the buyer, the payment is executed. Banks with integrated systems will be in a better position to seamlessly execute the two legs of the transaction (i.e., receipt of the invoice and execution of the payment).

**Addressing Regulatory Initiatives**

**Tightening of Regulatory Regime:** An integrated solution will bring homogeneity to a bank’s internal checks and balances. Because the integrated system will combine trade and cash data into a single holistic report, it will provide better visibility over client-side transactions and limits, as well as the bank’s own exposure levels.

**Focus on Standardization:** As referenced earlier, the trade and cash world is increasingly being exposed to numerous standardization initiatives. In order to continuously respond to these programs, the system must be scalable to incorporate new requirements without fundamentally changing the existing system. Since an integrated solution incorporates concepts such as shared services, it provides the requisite levers to easily integrate future standardization efforts. For example, an integrated solution will be better placed to integrate SWIFT Trade Services Utility requirements than a distributed cash and trade system.

**Handling Industry Competition**

**Escalating Competition:** With banks facing stiff competition from other rivals within and outside their current geographies as well as from nonbank entities, traditional transaction banking services are increasingly becoming a commodity. Therefore, banks need to find points of differentiation to gain a competitive edge. An integrated transaction banking platform provides such an edge. Through a single platform, the bank can provide transaction banking services as well as niche services such as multibank capabilities that are offered by nonbank entities.

**Focus on Cost Efficiency:** Many operational silos exist within a bank’s transaction banking operations, leading to fragmentation and inefficiencies. Lack of automation and an overreliance
on manual processes add to the inefficiencies. With an integrated solution, banks can condense their silo structure and leverage opportunities to garner synergies between different operational teams. The system provides automation avenues like Straight-Through Processing (STP), diminishing the possibilities of human error. Many banks have already implemented STP for their payments modules. If the same system is enhanced to process trade messages as well, user involvement can be obviated in what is usually a highly labor-intensive task.

Maturity Levels of the Integrated System

The school of thought that recognizes the imperative of trade and cash convergence has produced a variety of definitions of “integration.” As a starting point, banks must define the scope and nature of business solutions that should be offered under the umbrella of an integrated system. Furthermore, banks must consider the technology costs associated with integrating the identified solutions. As we can easily imagine, the need to make large strategic investments upfront may place certain aspects of integration out of reach of some smaller players. In such a scenario, banks should set internal targets to achieve integration maturity in a step-by-step manner. Figure 3 (next page) depicts a logical progression of integration maturity that banks can work towards in an incremental fashion.

• Level 1: As a first step towards integration, banks should present to its customers a single portal capability for accessing both trade and cash products — which might continue to exist as separate product suites internally. In addition, banks should introduce a centralized entitlement framework that can optimize authorizations and access levels across trade and cash products. This will help banks align both their product proposition with client-side treasury optimization initiatives and also their sales teams with a more focused penetration proposition.

• Level 2: Next, banks should aspire to integrate business activities across a comprehensive set of trade finance, payment and receivable management services by identifying shared processes that are closely linked. For example, the techniques required to generate or receive payments under trade transactions are virtually identical to those required to process stand-alone payments. An incoming MT103 can be a clean payment or a payment under a collection sent by a bank. This level of integration will help banks align their back-office and credit limits management operations as a single unit that can handle both trade and payments functions.

• Level 3: Once external portal and back-end operations are aligned, banks should look to enhance overall reporting and cash-flow forecasting capabilities, which are critical to clients aspiring to optimize their own treasuries. Another important step at this stage is to develop capabilities to directly integrate with clients’ ERP systems. This would require the bank to generate reports in formats acceptable to client-side systems. Again, many banks may already have this capability but the idea is to cluster this capability in the integrated system and thereby enhance the maturity of the system. Also, this is a stepping stone in developing the multibank capabilities that are an important aspect of a fully mature integrated system.

• Level 4: At this stage, the time is ripe for the bank to advance its trade and payments offerings. Capabilities that can be included at this level are electronic direct presentation (EDP) for trade instruments such as LCs. EDP can significantly reduce the gestation period of an LC, resulting in direct benefit to the client’s working capital management. Open account activities such as customized purchase orders, e-invoicing and SWIFT TSU capabilities can also be installed at this stage. A critical piece that the banks should include at this level is event-trigger-based workflow capabilities. A simple example is the generation of alerts notifying concerned parties that a specific event has taken place – such as the generation of a purchase order or receipt of an invoice. Honing this capability at this stage will provide banks significant competitive advantage when they aspire to build supply chain finance capabilities.

• Level 5: By now the bank should have a robust integrated transaction banking system with all the basic prerequisites and critical pieces...
built in. The bank now has a system that can be offered to a wide number of syndicated institutions without losing operational efficiency. Furthermore, it provides clients a true multibank experience by directly integrating with the client’s internal system and providing information from multiple sources without the client worrying about handling different formats from various sources. Further extrapolating, the bank can opt to white label the integrated system to other banks, thus creating an additional revenue stream.

A critical aspect for the success of the integrated transaction banking platform is scalability. While developing the integrated system, and while progressing from one maturity level to the next, the bank should look for avenues that could provide future integration possibilities (a few of which are discussed in the “Next Steps” section on page 8). Continuously identifying such shared services is a key success factor for achieving a truly scalable integrated transaction banking system.

The Right Maturity Level

The previous section described a tiered approach for banks to migrate from a nonintegrated product proposition to a more sophisticated and integrated solution. But a mature integrated solution requires significant up-front investment. An investment of such magnitude requires careful consideration. Each bank must perform its own due diligence to justify this investment. An influential consideration is where the bank wants to position itself in the cash and trade value chain vis-à-vis its positioning in the competitive landscape. Different banks have different target client segments and value proposition strategies; a mature integrated system should fall in line with this strategy.

Once a bank understands its markets (i.e., its target clientele and the strengths of its competitors), deciding which maturity level to achieve should be easy. Figure 4 (next page) depicts a tabular representation of various bank clusters and the corresponding maturity levels that banks in the respective clusters should achieve to bring their flavor of integrated transaction banking in line with the needs of their target customer segment and their own competitive strategies.

Implementation Considerations

Once the bank has defined its competitive landscape and determined the most appropriate maturity of the required integrated system, the next step is to outline the implementation strategy. Before finalizing the implementation strategy, the bank must evaluate factors that might impact the strategy. These considerations, in turn, depend on the bank’s “as-is,” or current state, system. Figure 5 (next page) depicts the four typical types of legacy systems and Figure 6 (see page 7) outlines a simple model that can serve as a tool for banks contemplating such considerations. The model pivots around four types of legacy systems and then presents what it would take to promote integration over each category of legacy system.
Homegrown/Proprietary System: Banks with homegrown cash and trade systems can easily make changes to implement single sign-on and integrate basic features of cash and trade. Beyond that, they would need to internally develop new capabilities such as electronic direct presentment and e-invoicing. This would be costly and require a longer gestation period. Architecturally, they would have to deal with a system’s complexity and consider a wide spectrum of services that need to be implemented. On the other hand, the advantage with this kind of system is scalability and differentiation.

The bank also has the flexibility to design a future-ready system that delivers new services such as supply chain finance that will be required over the long term.

Banks’ Incumbent Systems

<table>
<thead>
<tr>
<th>Nature of Operations</th>
<th>Local Banks</th>
<th>Regional Banks</th>
<th>Global Aspiring Banks</th>
<th>Large Global Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type</td>
<td>Situated only in small or mid-size region and have extensive branch networks in that region.</td>
<td>Have presence in a few national markets.</td>
<td>Have presence in some of the major commercial centers across the globe.</td>
<td>Have global operations in most of major commercial markets across the globe.</td>
</tr>
<tr>
<td>Target Clientele</td>
<td>Focused on local clients in SME space or local public sector clients.</td>
<td>Serve companies in local markets such as lower middle-market companies, SMEs and public-sector entities.</td>
<td>Serve companies that operate across region, typically larger regional companies or MNCs.</td>
<td>Have capability to serve clients across spectrum from small SMEs to large MNCs.</td>
</tr>
</tbody>
</table>

Figure 4

Figure 5
• **Combination of Vendor Products:** Banks that have implemented third-party cash and trade systems could add single sign-on capability but it would be difficult to establish an entitlement framework considering the potential disparity in their code bases. Similarly, implementing a centralized back-office system might be difficult. But banks with this system would find it cheaper and faster to implement new services. The complexity would be primarily from an IT environment perspective, but the bank would be spared from having to design the application-level architecture. The most significant constraint with this type of incumbent system is achieving true integration. With disparate code bases, it is very difficult to build a shared service infrastructure where services that are common to both cash and trade system systems can be centrally utilized. Furthermore, the bank will not be able to achieve any significant differentiation against its competitors as it utilizes the same product base as many of its peers.

• **Hybrid of Homegrown and Vendor Product:** As in most hybrid cases, the idea is to bring in the best of both worlds. Similar to the homegrown system, this system can also easily achieve Level 2 maturity. As such, this type of system would enjoy the lower cost and faster gestation of vendor products coupled with better integration and scalability of home-grown systems. Complexity can pose challenges in this particular case, as the bank needs to seamlessly integrate both home-grown applications and vendor products.

Banks with this kind of system can differentiate themselves by customizing the products in-house or by building a wrapper over vendor products to deliver additional value-added services.

• **Outsourced from Other Banks:** Banks with such an incumbent system would face problems even implementing Level 1 maturity if the other bank system that they have private labeled does not have such a capability. The same problem would apply in trying to achieve a higher level of maturity: these banks will always be in control of the implementing bank upgrading the system. This type of system would initially provide some cost, gestation and complexity advantages since the bank would be implementing a tried-and-true system, but once implemented and locked in these aspects will vary with the whim of the implementing bank. It would be advisable for these banks to explore a hybrid system concept for long-term scalability and differentiation.

### Implementation Considerations

<table>
<thead>
<tr>
<th>Considerations for Achieving Highest Maturity Level</th>
<th>Homegrown/Proprietary System</th>
<th>Conglomerate of Vendor Products</th>
<th>Hybrid of Homegrown and Vendor Products</th>
<th>Outsourced from Other Bank</th>
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**Legend:**
- Low
- Moderate
- High
- Extremely High

Figure 6
Next Steps

A state-of-the-art integrated system entails all the basic transaction banking functions such as trade and payments combined with a robust information reporting and cash flow forecasting capabilities. The system also has capabilities such as open account processing and event-trigger-based workflow solutions that facilitate more advanced solutions. As stated earlier, if such a system is designed with scalability and a shared service concept at the heart of its architecture, many other services can be easily included as and when they become pertinent to the bank's value proposition strategy (see Figure 7). These services include:

- **Supply Chain Finance**: These solutions are the logical next step to an integrated transaction banking platform. A built-in open account service automatically captures buyer-side purchase order and seller-side invoice generation activity. With this, the bank obtains a clear view into the order-to-cash cycle of sellers and the procure-to-pay cycle of buyers. Banks can then integrate financing solutions that can reconcile demands of buyers seeking to extend their payment terms and of sellers pressing to expedite receivables. Prospective solutions could include services such as documentary credits or solutions such as factoring and invoice discounting.

- **Liquidity Management and Cash Concentration**: With a holistic view of the integrated system on client accounts, banks can also include physical and notional cash concentration services. Further, banks can build capabilities that will automatically release balances to a short-term investment solution based on the client's individual risk-return profile and convenience.

- **Multicurrency and Forex Capabilities**: These will help banks introduce integrated services to new geographies without any significant investment. Including Forex services will also bolster the bank's reporting capabilities and bring completion to client-side treasury activities.

- **Other Value-Added Services**: With a mature, integrated system, banks can consider offering other value-adding services to bolster client treasury management capabilities and help them unlock working capital savings. One way is to develop a system that establishes efficient KPIs for a client’s treasury activities. Historically, corporate treasury has used ratios like day’s sales outstanding to determine the efficiency of their working capital management. But these ratios are not transparent enough. They combine balance sheet and P&L information, instead of data points that originate directly from operational processes. With an integrated system, banks can directly look into the process details such as the payment terms given and the overdue period, and then generate an efficiency report for the client.

Figure 7

Integrating the Transaction Banking Encore
About Cognizant

Cognizant (NASDAQ: CTSH) is a leading provider of information technology, consulting, and business process outsourcing services, dedicated to helping the world’s leading companies build stronger businesses. Headquartered in Teaneck, New Jersey (U.S.), Cognizant combines a passion for client satisfaction, technology innovation, deep industry and business process expertise, and a global, collaborative workforce that embodies the future of work. With over 50 delivery centers worldwide and approximately 137,700 employees as of December 31, 2011, Cognizant is a member of the NASDAQ-100, the S&P 500, the Forbes Global 2000, and the Fortune 500 and is ranked among the top performing and fastest growing companies in the world. Visit us online at www.cognizant.com or follow us on Twitter: Cognizant.

About Cognizant’s Wholesale Banking Group

A unit of Cognizant’s Banking & Financial Services Business Unit, the Wholesale Banking Group provides end-to-end information technology, consulting and business process outsourcing services across various lines of business within the wholesale banking sector. The group has extensive experience across wholesale banking product suites, serving large global banks across geographies.

With a unique combination of deep industry and technology expertise, garnered through delivery of multiple clients' cash and trade requirements, we have developed deep process-level knowledge across all wholesale banking sub-domains. Cognizant Business Consulting provides business-technology consulting services that assess current state IT architecture, defines the business roadmap and develops the best possible implementation strategy. This knowledge provides us with insights when delivering reengineering projects such as designing an integrated transaction banking platform. It is a conscious choice to focus on business services rather than just the products that enable these services. This helps to inculcate the best practices prevalent in industry encompassing both cash and trade areas.

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