CFO Payment Pulse

Change is coming but who's driving?

The risks, challenges and opportunities of open payments

ixaris
Perfect Fit Payments

Content of this issue

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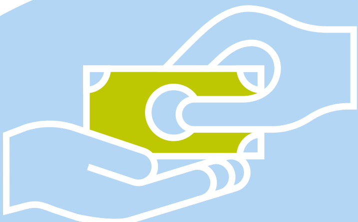
Change is coming but who's driving?

The risks, challenges and opportunities of open payments

In the first report from the CFO Payments Pulse, published in June 2017, we identified healthy potential for new technologies and new commercial payment types, as well as a healthy degree of optimism among CFOs, CPOs and treasury departments in corporates across a diverse range of sectors. Those findings still stand. Potential and optimism have in no way diminished. There is a largely receptive audience for new ideas and new approaches to commercial payments. There is also an acknowledgement that embedded systems, attitudes and relationships present a number of challenges on what is already a complex and nuanced journey to a more open payments culture. Awareness of the risks is high, while resources are low; and concern about the scalability of new solutions and their providers' stability remains. However, the move towards a more open banking ethos, the advent on PSD2 in Europe, and impetus from retail consumers could all be the catalysts for change in commercial payments.

In this paper, we look in more depth at the opportunities – as well as the challenges and hurdles – presented by the move to open payments. As the responses to the survey show however, driving the change will require significant cross-industry collaboration. An effort that will need to combine the drive of fintechs with the engine of the banking sector to encourage CFOs to take full advantage of a growing array digital payment tools now available to them.



8% of CFOs want to increase their outsourcing or collaboration with payment suppliers

Priorities and fundamentals

The banking sector itself is going through a period of unprecedented change. However, there is little to indicate the existential change on the horizon within the corporate treasury departments that make up banks' commercial customer base. The latest research conducted for this Payment Pulse series, shows that for CFOs, CPOs and treasury departments core business fundamentals remain the main priority. As before, respondents were asked to choose their top three priorities and rank them in order. Of the seven categories to choose from, there were two distinct groups. The first group consists of:

1. Cost reduction
2. Risk mitigation
3. Increasing competitiveness

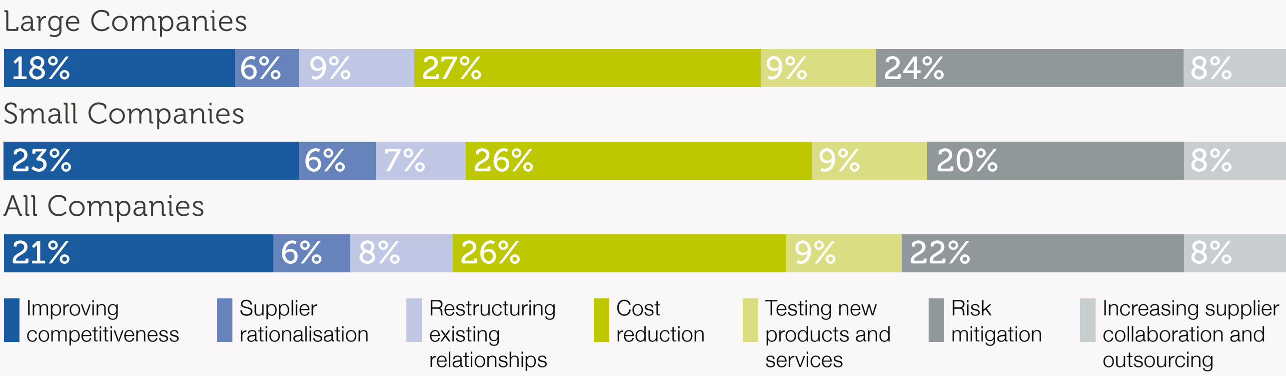
These three goals appeared in respondents' 'top three' most often, and there was not much to choose between each of the three. Cost reduction was the top priority for both large and small companies (those with an annual turnover of less than $10 million). Although slightly fewer respondents at larger companies selected 'increased competitiveness' as one of their top three choices, when they did select it, they were more likely to make it their number one priority. Similarly, among smaller companies, increasing competitiveness narrowly beat mitigating risk to second place.

The second group got significantly less votes and lower overall rankings than the first group. There is a notable gap between 'increasing competitiveness' in third place overall and 'testing new products and services', which came fourth overall and topped the second group, as follows:

1. Testing new products and services
2. Increasing supplier collaboration and outsourcing
3. Restructuring existing relationships
4. Supplier rationalisation

In this group, the main difference between larger and smaller companies was that bigger firms put 'testing new products' on a par with 'restructuring existing relationships' – although supplier rationalisation remains at the bottom of the list for all companies. As we noted in our first edition of the Payments Pulse, this suggests that there is an appetite out there for new products and services within corporate treasury departments – once the operational essentials have been addressed. Moreover, this is a slightly higher priority than categories that explore new ways of working with suppliers, partners and other stakeholders. Overwhelmingly however, insights from interviews with treasurers reveal that while finance teams are on the look out for ways of doing things differently, in reality they are, and will continue to be, heavily reliant on the banks to introduce them to new innovations. This implies however of course a degree of openness by banks to work with external providers. As one CFO told us: "banks must work together on implementing the same level of technology and payments set-up but I think this is a step too far [for them]."

What are the top 3 priorities for CFOs, CPOs and Treasury departments in 2017?



Source: CFO Pulse, Ixaris September 2017

77% of CFOs feel they would benefit from more automation for payment approval, 69% from invoice delivery or capture

Automation not experimentation

These priorities were also evident when CFOs and treasurers were asked about their incentives for using new types of payment technology. Business process automation and efficiency topped the list, suggesting that many CFOs rightly see automating technology as a key enabler of any cost reduction and risk mitigation strategies they choose to implement. The survey also told us where CFOs expect to see the greatest benefit from automated business processes. When considering the entire payment lifecycle, the consensus among survey participants was that the following would all benefit – at least moderately - from automation:

1. Payment approval
2. Invoice capture
3. Reconciliation
4. Ordering and procurement
5. Invoice approval
6. Consolidating payment execution processes
7. Remittance delivery
8. Maintaining master vendor records

Of all these functions, reconciliation was most often seen as the area that would benefit a lot from automation – although among smaller companies, invoice approval scraped ahead in the rankings. At the other end of the scale, ordering and procurement was most commonly cited when respondents were asked to identify areas that would not benefit at all from business process automation. Once again, there was a very small difference between smaller and larger companies: in this case,

> "Banks must work together on implementing the same level of technology and payments set-up but I think this is a step too far [for them]."

CFO, global technology company

a greater number of bigger firms decided that it was remittance delivery that would not benefit at all from automation.

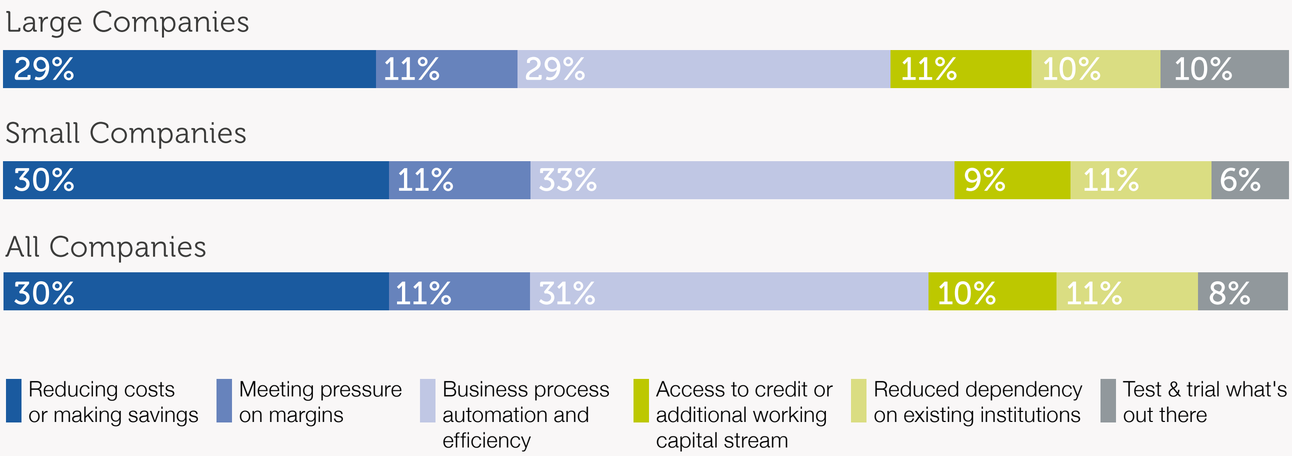
A number of companies indicated that all these functions would benefit from automation. A similar number indicated that none of them would. But the overwhelming majority gave a mixed response, carefully selecting which areas would benefit and by how much, as well as areas that they considered not relevant.There is clearly an appetite in corporate treasury departments for higher levels of automation: an appetite that many emerging technology providers are able to fill.

The second biggest incentive was not, nor surprisingly, to reduce costs or make savings. Meeting pressure on margins came next, followed by reducing dependency on existing institutions and accessing credit or additional working capital stream, which were clustered together with very similar scores. However, at the bottom of the list was 'testing or trialing what is out there'. Although testing new products and services is emerging as one of the CFOs' priorities for 2017, there is very little interest in looking at new technology simply for the sake of it. New technology has to have clearly outlined purpose and proven benefits if it is to attract the CFO's attention.

This hints at one of the challenges that potential technology providers in this space must overcome: the sense of inertia that can overcome harried treasury departments. As Bob Novaria, Partner at Treasury Alliance Group and the former treasurer at BP America put it: "Many treasurers work on the basis that if it ain't broke, why fix it? They won't spend money until they have to."

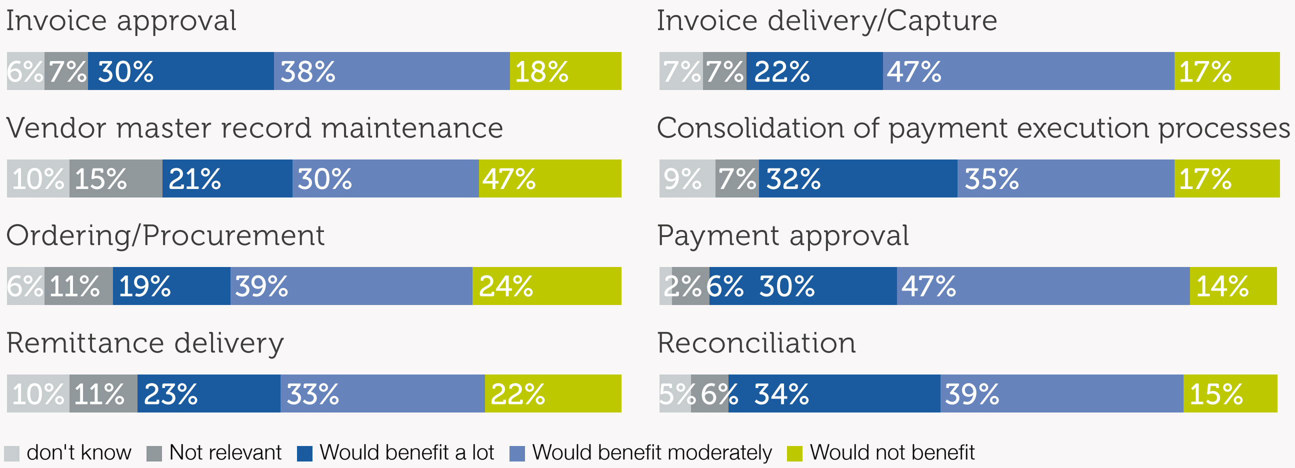
This sentiment was echoed by David Blair, Managing Director Acarate Consulting, who pointed out: "[Treasurers] want to see what everyone else is doing

What are your incentives for using new payment technologies?



Source: CFO Pulse, Ixaris September 2017

How much would you benefit from payment automation for the following areas?

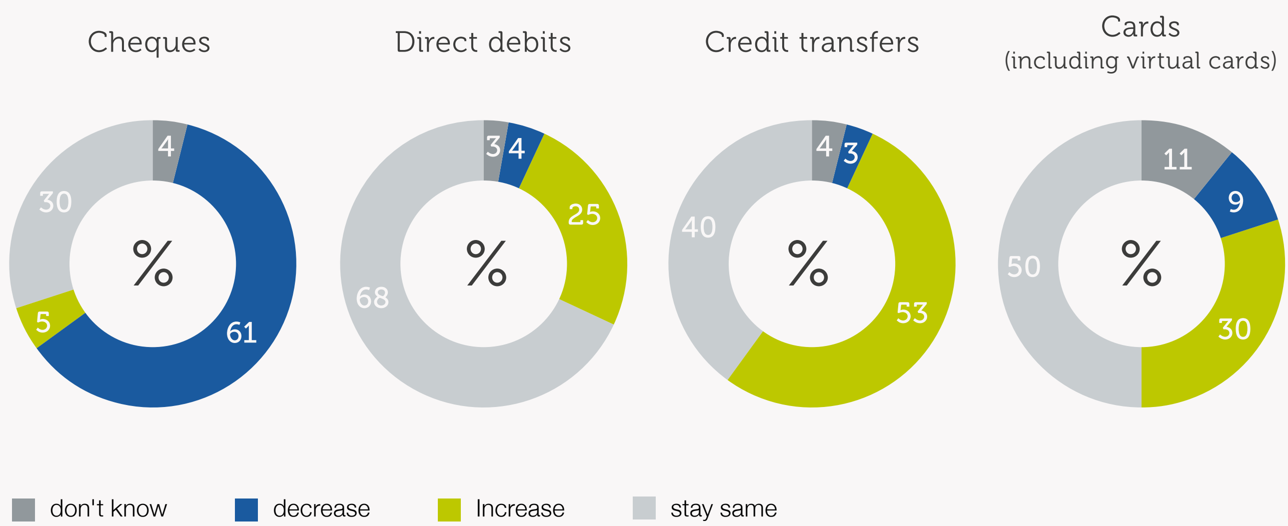


Source: CFO Pulse, Ixaris September 2017

it first: they are not a very experimental bunch. There are exceptions, but that's a fair statement in general."

Returning to the survey, we can see illustrations of this attitude in action. For example, when asked how their use of cheques, credit transfers, direct debits and commercial cards (including virtual cards) would change in 2017, 'stay the same' was by far the most common answer overall. Of the four possible options in four separate categories, it accounted for just under half of all responses. Even the predicted plummet in the use of cheques couldn't dislodge 'stay the same' from the top spot.

How will your anticipated use of the following payment products change in 2017?



Source: CFO Pulse, Ixaris September 2017

Green shoots or feet of clay

There is an inherent conservatism here that is not necessarily specific to payments and related technology, but which certainly influences take up among corporate customers. For many years that conservatism has been echoed in the banks with whom treasury departments have the most trusted relationship. As Novaria put it: "Treasurers are not first movers and they are risk averse. They'll just wait for their banks to tell them what to do."

Nonetheless, there are signs that the opportunities for more innovative suppliers of payment services in the commercial sector are growing. Anecdotal evidence from Ixaris suggests that there is almost always someone within the finance team who is keen to find ways of doing things differently to the way that banks offer. They may not be the loudest voices as yet, but these individuals are playing a critical role in moving payments culture forward.Then there is the desire to reduce costs. This reflects the reality of treasury life where certain functions remain unreasonably and unnecessarily expensive. The margins of incumbent suppliers for cross-border payments and foreign exchange, for example, mean that these areas are ripe for challenge from newer and nimbler providers.

The rush of innovators in the consumer or retail space has led to companies like Zoom in the US and Transferwise in Europe taking on the traditional currency providers. Yoni Arbel who leads the treasury products team at Transferwise, acknowledges that CFOs with small teams don't have time to properly research solutions on top of creating the new infrastructure to move to new suppliers. He points out, however: "In the next two years we will see a lot more businesses using our services. Challenger banks are already collaborating with us and it will not be long before first-tier banks realise that they will lose business if they don't use Transferwise for their customers."

Smart CFOs are looking at the retail sector for inspiration and potential crossover. This more positive interpretation is also reflected in the quantitative results from the survey. Look again at what incentivises treasurers and CFOs have to adopt new payment technology: there is some interest in reducing dependency on existing institutions. Although some way behind process automation and cost reduction, this was the third most common driver for adopting new payment technologies among larger companies. That is not quite true for smaller companies, who are slightly more reluctant to look for new ways of managing their external relationships. For firms with less than $10 million turnover, reducing dependency on existing institutions came fifth in their list of reasons to use new payment technologies – just above testing and trailing what is out there. We might expect these smaller companies to be more able to adopt new payment processing services from innovative Fintechs. But where this operational flexibility exists, it is often countered by lack of resources needed for implementation.

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>
> Bob Novaria, Partner, Treasury Alliance Group

71% of small companies, 69% of large companies said that the ease of payment product use is the leading priority

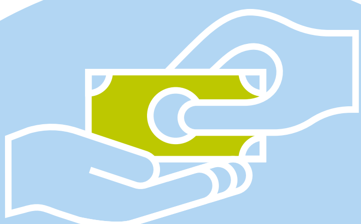
New suppliers and old friends

In January 2018, the EU's second payment services directive (PSD2) will come into effect. Among other things, the new directive mandates that established financial institutions open up their customer and transaction data to new types of payment service provider. The goal is to encourage greater levels of innovation within Europe's banking sector, and to create a more competitive landscape in which bank customers can take advantage of new products and services being developed by innovative Fintech companies. Although PSD2 is confined to the EU, its effects are likely to ripple out beyond the continent. PSD2 is in effect putting a rubber stamp on an existing trend towards a more open banking and open payments environment. For banks the effects could be dramatic. Industry analysts have described several new business models for financial institutions. These range from the compliance only model in which banks are simply providers of data and liquidity to the 'hub' model in which banks become a one-stop app shop for all kinds of financial and related services.

> "[Treasurers] want to see what everyone else is doing it first: they are not a very experimental bunch. There are exceptions, but that's a fair statement in general."
>
> David Blair, Managing Director, Acarate Consulting

To date, the language around open banking has been more frequently directed towards the consumer rather than the business customer. The new payment providers are often disruptive Fintechs that are discussed in the same breath as more familiar names from the consumer technology space. Explanations of the APIs required to make the system work are illustrated with reference to the new digitally native giants of the digital consumer space: Amazon, Uber, or AirBnB. The lightweight, real-time, agile world that these Silicon Valley favourites embody is often at odds with the compliance-driven environment of inflexible legacy platforms with which most CFOs and treasurers are familiar. Whereas new payment providers like PayPal and Square are seeing adoption rates grow among merchants and retail customers, take up is much slower within the B2B space. Only one participant in the survey (whose turnover was greater than €200 million) said that they currently use PayPal alongside their commercial cards, cheques, direct debits, credit transfers, wire transfers and cash.

Nonetheless, open banking does create new possibilities as the financial institutions that CFOs trust converge with the innovation that they need. Not least because in the new environment, trusted banks act as the honest broker between commercial customers and innovative Fintech products and services. For some time, experts at Gartner and elsewhere have been advising bank CIOs to develop their own incubator network to bring the best of Fintech innovation under their wing as a means of addressing the changes wrought by Open Banking. We have seen more banks adopt the incubator model as a cost-effective means of harnessing innovation, especially in the decade since the global financial crisis. This is by no means the only model for Fintech innovation, but it is an increasingly well established one that should be particularly attractive to risk-averse, bank-dependent CFOs. The stage is therefore set for a more collaborative and partnership focused approach in which established financial institutions, their commercial customers and disruptive Fintechs work together for mutual benefit.



47% of CFOs don’t expect to change their use of payment methods

Open banking and commercial payments

For banks

Although the move to more open banking has in part been driven by a new cohort of digitally native customers who are looking for the same connectivity and service levels from their banking provider as they get from entertainment providers, holiday rentals and car share services, there is a great deal of value to be had from commercial customers

The challenge for established banking institutions is cultural, technical and financial. Cultural because it requires on the one hand a more open – although not necessarily more frequent – dialogue with commercial customers, and on the other a more collaborative approach to Fintechs and other partners.

Technical because sclerotic legacy platforms that silo data, functions and insight are ill suited to the open banking environment. Replacing them with modern, open systems not only opens up the possibility of customer-centric, multi-channel payment services for both retail and corporate clients, it enables them to take on a valued role that avoid disintermediation from the payments lifecycle.

Financial because in this new environment traditional revenue streams and are likely to change shape or be eliminated altogether. It requires a radical rethink of the business model when the monopoly on customer data is no longer in place.

For CFOs and treasurers

Open banking presents a major opportunity for finance officers to overhaul bureaucratic processes, and develop technology-enabled strategies to support the overall aims of the business. Banks are being obliged to change their own business models through a combination of market forces and new regulation. New products and services to enable payments will become available through long-established banks – as well as more recent challengers.

CFOs have the opportunity to retain trusted relationships that reassure all internal and external stakeholders, while exploring innovation in a relatively safe environment. By keeping the conversation open with banks, CFOs have the opportunity to direct the changes that banks are obliged to make in their own direction.

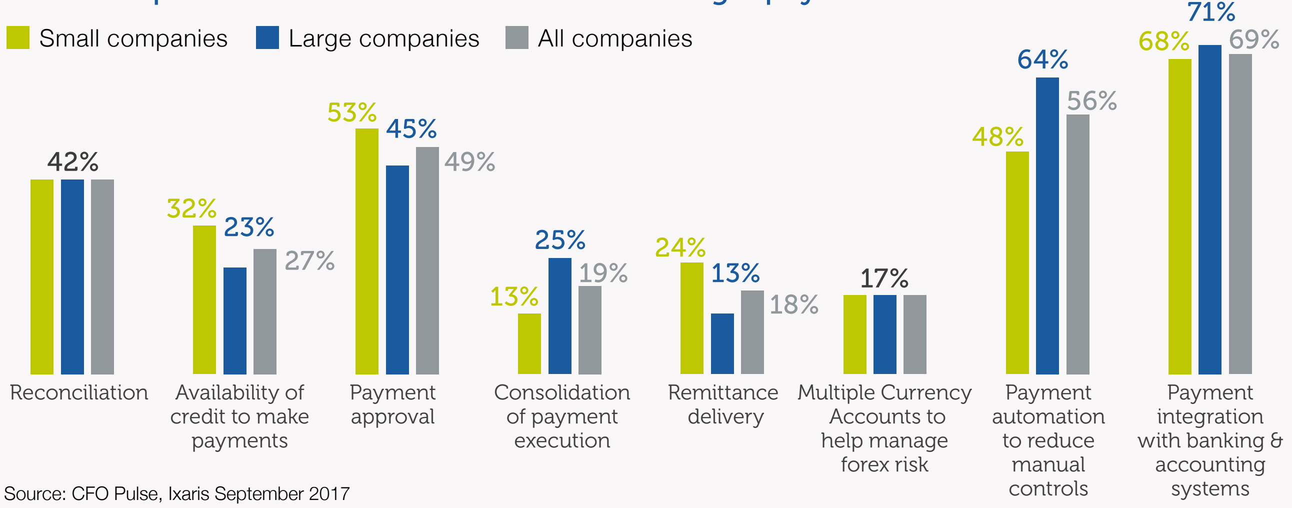
For Fintechs and payment service providers

The opportunity here is for those financial technology innovators who understand that commercial payments are at least as valuable a source of revenue as retail payments. As we have seen, many CFOs already accept that key areas of the payments chain such as reconciliation will benefit from greater automation. Other areas of the survey also show that, when asked to select the three most important considerations when choosing a payment solution, 69 per cent of CFOs chose payment integration with banking and accounting systems - a strong indication that corporate treasuries are looking at ways to break down the traditional data silos that can constrain value creation.

Fifty-six per cent chose payment automation to reduce manual controls, indicating traditional ways of working are no longer delivering either for the treasury or for the business as a whole, while 49 per cent chose payment approval. The top three answers have not changed since the first iteration of the Payments Pulse survey, suggesting that CFOs continue to be interested in automation and integration over functional specifics.Tapping into these concerns is likely to be the most fruitful approach for new providers to target, particularly as automation is essential for firms that are serious about sharing data and functionalities across their financial operations, with their other business units, and with external partners and suppliers.

However, there is a caveat. As we have pointed out: this is not a sector that experiments for the sake of experimenting.

3 most important considerations when choosing a payment solution



Source: CFO Pulse, Ixaris September 2017

The lure of the new is not enough: solutions have to be carefully targeted at what CFOs actually want and need.

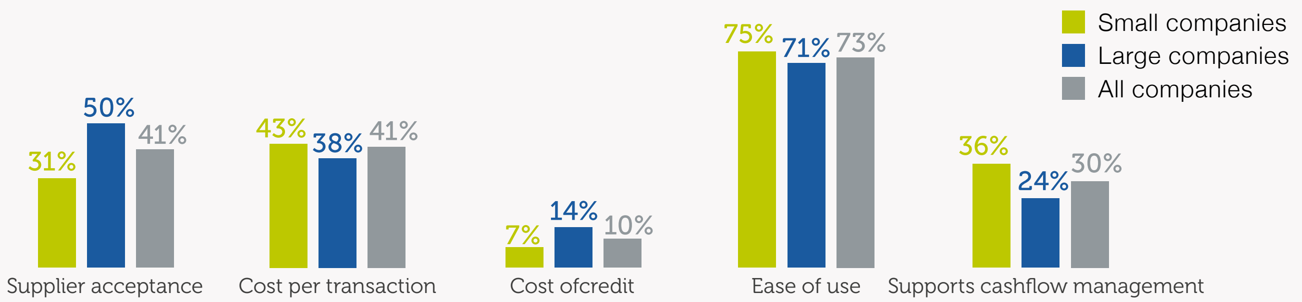
What suits a company with less than $10 million in turnover may not suit one ten times the size. For example, we noted above that payment automation to reduce manual controls was an important consideration when selecting new technologies. However, in contrast to the 64 per cent of larger companies who put it in their top three, only 48 per cent of smaller companies did so. What CFOs like about their current preferred payment types is also a useful guide for new providers. Seventy-two per cent of survey participants gave ease of use as one of the main reasons they liked their current payment technology. Given the complexity within most treasury departments, the multiple regulations that different sectors and different geographies are exposed to, the demands of KYC and AML compliance, and the isolated pools of data dotted round the business, this is not surprising.

The theme of ease and convenience can be seen again when more than 40 per cent of all participating companies – and 50 per cent of larger firms – said that supplier acceptance was the reason they liked their current payment options. Changing payments in the commercial ecosystem almost certainly requires Fintechs to have an ecosystem of their own – including banking partners - to deliver multi-lateral solutions.

Approximately 40 per cent of CFOs also said they liked the cost per transaction offered by their current payment systems. As we have seen throughout this paper, cost and cost reduction are a major concern for CFOs. A new solution that offers convenience and greater control in a complex environment is unlikely to win converts if the price remains too high.

What are the reasons for your preferred payment methods?

Source: CFO Pulse, Ixaris September 2017



30% of companies expect no change in use of cheques in 2017

Conclusion:

As we noted in our first paper, the scale of the commercial payments opportunity is encouraging news for incumbent financial institutions. It's also good news for employers of forward thinking CFOs who can expect more efficient treasury operations driving value throughout the business.

There is also a growing interest among CFOs in expanding their payments ecosystem, re-assessing the way they interact with current suppliers, and reducing dependence on existing institutions. They are still a minority, but one that is receptive to new ideas, new services and new ways of working - despite the general risk aversion of the industry.

The opportunities we noted in our earlier edition are most likely to be realised if all market players work together to embrace the changes being ushered in by the move to more open banking. Mutually beneficial relationships built on a spirit of collaboration and partnership can be developed among established and disruptive providers – and their commercial customers – provided that regulations like PSD2 are seen as not just a compliance exercise but also a genuine opportunity for change.

> "Many treasurers work on the basis that if it ain't broke, why fix it? They won't spend money until they have to."
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> Bob Novaria, Partner, Treasury Alliance Group

Methodology

The CFO Payment Pulse survey was carried out online between June and July 2017. More than 200 companies from the UK, mainland Europe, North America, Latin America and the Caribbean, the Middle East, Asia and Africa took part. Ninety-nine companies had a turnover of less than US$ 10 million, 48 had a turnover between US$ 10 million and US$ 200 million, 43 had a turnover of more than US$ 200 million, and 11 declined to give or did not know their turnover. Participants represent a diverse range of sectors including: charities, public authorities, blue-chip technology firms, fast-moving consumer goods companies, manufacturing, entertainment and hospitality, and financial services.

About Ixaris

Our passion is giving our clients the agility to adapt to new and evolving markets. Key to this is our technology and expertise, letting us rapidly and cost-effectively deliver solutions that perfectly fit your business and your target markets. More than 75% of our workforce is dedicated to payments innovation. This means our technology is continually evolving to keep up with your business's growth and the changing landscape of your payments environment.

Contact us

www.ixaris.com

dropusaline@ixaris.com

@ixaris

UK

Ixaris Technologies Ltd

10 Midford Place

London W1T 5AE

Malta

Ixaris Systems Ltd

Capital Business Center

Triq Taz-Zwejt

San Gwann SGN 3000

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Ixaris Technologies Limited, 10 Midford Place, London, W1T 5AE

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