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As payments speed up, can banking systems keep pace?

To meet customer expectations, financial institutions need to overhaul both their tech and their models.

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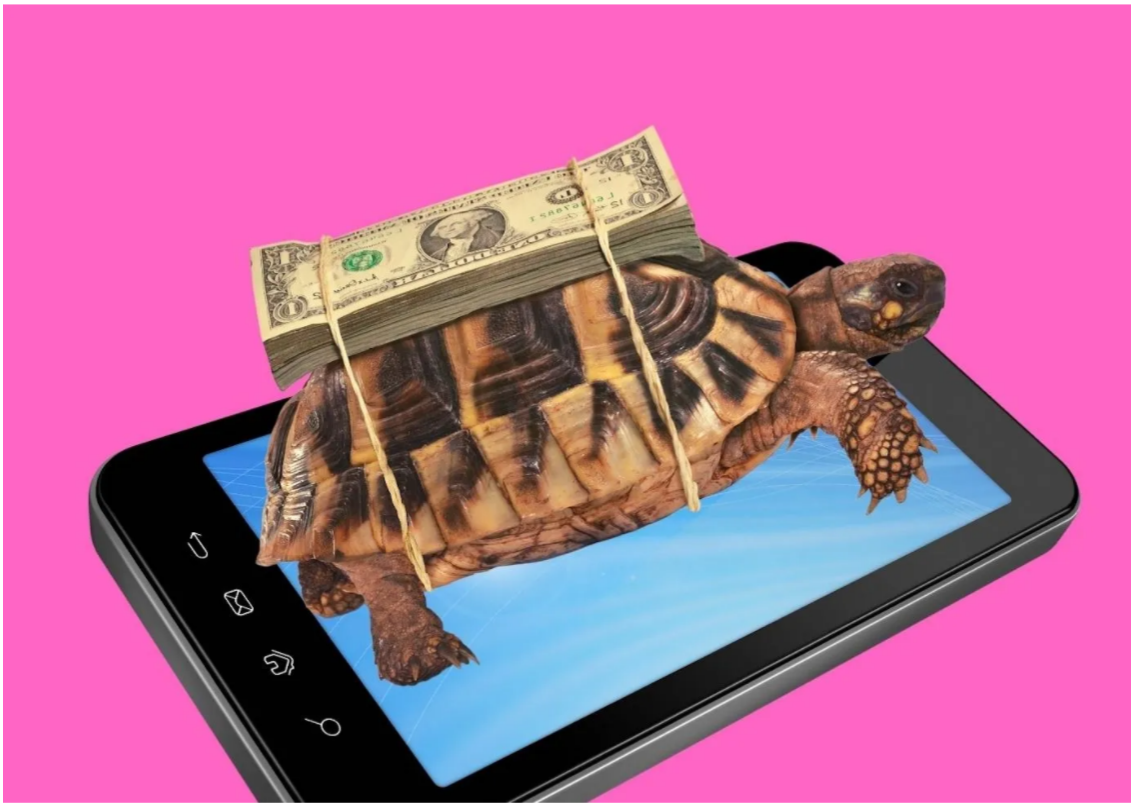

First, the good news: banks are fully on board with ensuring clients and their customers can make payments anytime, anywhere, anyhow. Given that global payments revenue was $1.9 trillion in 2020, according to McKinsey & Co., that's a big market to win.

That doesn't mean all banks can deliver such a universal experience. But they recognize the benefits of meeting user choice around payment method and being able to serve that as quickly as possible.

Payments are increasingly being served in real time, and banks need the ability to manage them 24/7. It's simply what people expect in the age of mobile internet – especially in the wake of COVID-19, when so many aspects of business and life have gone digital.

Payments are also becoming data-rich. Banks are just beginning to explore how data connected to payments can be used to predict consumer patterns, underwrite financial products, and optimize a corporate's profile so the bank knows the best way to serve them a payment.

Third, payments are becoming embedded in lifestyles and business needs, as part of the trend towards open banking and the use of APIs to connect applications.

But banks are struggling to keep up.

Faster is harder

"Faster payments are wonderful if I'm a client and my expectation is 'instant'," said Roland Brandli, strategic product manager of SmartStream Technologies' digital payments control service. "But if I'm a bank, it's creating a lot of pressure to keep up."

Correspondent bankers note that there is a difference between consumer and corporate expectations.

Nigel Dobson, banking services lead at ANZ, says financial institutions must distinguish between serving consumers and large companies. Big corporate clients want a slower, more predictable experience, with payments wrapped in data and insights. "They want large banks to curate data so they can see information about their payments status, and records," he said at this year's Sibos event.

Western Union, the remittance company, makes a similar plea. "The relevance of payment options varies around the world, so these don't scale overnight," said Shelley Swanback, president of product and platform, at Sibos. "All financial institutions are challenged by offering these options right away, with a good customer experience."

But even if financial institutions wish to compartmentalize some segments of payments users, it's just a question of pace, not direction. Fintech disrupters have already eaten away at lower-value retail payments and are now targeting the high-value corporate market.

Citing her corporate customers in e-commerce, Evelien Witlox, ING Bank's global head of payments and cards, said, "This is pushing us to develop solutions."

Can't we be friends?

Speaking at Sibos, Witlox says the industry would like to see the market come together to build common infrastructure. "What you see now are solutions targeted to specific use cases or corridors…what we need is a general cross-border payments solution that is as easy to use as doing a domestic payment."

Once banks start to introduce differentiation, it presents a challenge for their systems. SWIFT messages provide standardization for large-value cross-border payments using correspondent banks. But SWIFT can't meet the proliferating alternatives, such as mobile and QR codes; it doesn't serve the remittance market; nor can it easily link domestic payments systems to provide a real-time experience for cross-border transactions.

Most of all, the high-value correspondent banking system isn't geared to handle real-time transactions. And maybe it will never be.

Although banks often talk about the desire to harmonize infrastructure (and regulation), the fact is that they compete by being different. Otherwise payments is a pure commodity.

Take foreign exchange, for example. As fintech competitors squeeze banks on margins in core payments, they may find new revenues from FX.

But the infrastructure for forex is not a commodity either.

"Interlinking payment systems should differentiate between retail payments challenges – which is a demand to use these instantly beyond the domestic market – and a wholesale market, where the challenge is more about managing liquidity," said Marc Bayle de Jesse, CEO of CLS, which serves as the world's leading utility to process FX trades.

The problem with standards

SmartStream's Brandli says efforts to create standards often end up paving the way for new forms of complexity. As data sets related to payments have mushroomed in size, SWIFT has been encouraging the industry to adopt a new messaging standard, ISO20022. It is a big help in making domestic payment systems more interoperable at the cross-border level.

But Brandli notes that while this new standard gets everyone to agree on what fields to use in their payments and securities messages, it doesn't address syntax – the exact terminology that firms use.

This was manageable for old-school correspondent banking, when a payments message had only 30 or so fields to fill out. But under ISO20022, there are up to 2,700 such fields. Even a no-frills corporate payment requires 600 or 700 fields.

"Every infrastructure provider sees an opportunity to establish themselves in the market by defining themselves with a unique syntax," Brandli said. "This is how they seek to keep clients."

So don't expect this to change any time soon, regardless of banks' desire for harmonizing processes, Brandli warns.

Turning point

The need to keep pace with digitalization in payments and moving securities means banks will no longer be able to rely just on updating their legacy technology.

"We are at a turning point for technology in banks," Brandli said. "The world has changed drastically in the last 10 years."

Patches and middleware fixes won't be enough for banks that want to engage in multi-channel, fast-paced, and data-rich payments. Institutions are going to have to decide how to move to new, agile technology stacks.

In the new world of open-source development, modular design, and the need to be omni-channel, banks will have to look to partner or work with vendors, to complement their in-house capabilities.

Despite these challenges, the future is bright for those banks that can both simplify the user experience while navigating the complexities hidden in the back. The tech makes it possible to operate more at scale, and banks are more comfortable with partnerships and outsourcing.