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ANALYSIS: REAL-TIME NOSTRO

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The time for real-time nostro?

It has taken time to come to fruition, but with a number of global banks already on board, and more paying close attention, it looks as though the time for real-time nostro may have come. Tom Alford talks to one of the main protagonists, Gresham Computing

In an increasingly commoditised financial industry, where margins are pared to the bone, the watchword for banks and their customers is added-value. Having slowly shifted product focus from the interest-based to the more predictable fee-based, banks have been at pains for some time to find new ways of giving their customers something for their money and retaining loyalty, whilst maintaining profits for themselves and keeping the regulators happy. It is a balancing act almost worthy of The Great Blondin, especially in an arena so fundamentally important to every day banking activity as nostro account management.

The traditional way of handling nostro accounts, and there are many that still do this, involves the issuance of statements, such as MT950s or MT940s, at the end of the day. A bank then reconciles these against its transaction records, and from this it will be able to determine its cash position. Often this is carried out using the humble spreadsheet.

Quite apart from not delivering an accurate statement of position intra-day, this labour intensive process can place undue strain on the exceptions process, with an estimated average failure rate of eight per cent (more on payments received than on payments made). The knock-on effect of such a percentage of error, especially as volumes are on the rise,



Andrew Walton-Green,
Gresham Computing

is to create additional workload, greater risk, unhappy customers and, ultimately, spiralling costs for the bank. Added-value is nowhere to be seen.

But nostro account movements have been the focus of an apparent technological saviour for several years, in the form of real-time information systems.

The essence of real-time nostro (RTN) is the need to share information, in a standard format, on an international basis, so that banks can better manage their liquidity and risk, and know where they are in real-time. 'They can't manage what they can't see,' notes Andrew Walton-Green, CEO of UK-based vendor, Gresham

Computing. He likens the RTN system to the DHL parcel tracking system, enabling banks to see where a particular transaction is during the course of the day.

The development of the system can be traced back to the late 1990s. Almost from the outset, two strands of RTN had developed, each with its own working group for development and a set of big bank supporters. On one side, the Nostro Account Information (NAI) Swift working group proposed a decentralised or distributed model for bank-to-bank information exchange. On the other was a larger consortium of banks which had been working with Cable & Wireless (C&W) and Gresham Computing on the creation of a centralised utility for nostro account data interrogation.

The user community for both models is made up of banks of all sizes and locales. The users depend upon live data feeds from providers which are generally the large international clearing banks. But, as Walton-Green notes, for a fully functioning system 'you don't just want the biggest currencies'. The risk around the 'less obvious' currencies can be significantly higher so 'they have a part to play too, albeit in far lower volumes'.

In linking this disparate network of large and small financial institutions, Swift's distributed version provides transaction data directly to banks' counterparties and

customers, using a query and response model, without a central engine. The centralised version, however, takes a 'hub and spoke approach', where data is pooled into a secure central hub, hosted and managed by C&W. Gresham's part of the deal is to manage the day-to-day running of the programme and supply software that 'normalises and aggregates the data' into industry-standard XML ready for integration with a bank's existing systems. The data is made available over an internet browser, SwiftNet or via an application programming interface. Each authenticated bank user registered to the service is

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permitted to access any nostro data related to its accounts with a similarly registered RTN clearing bank.

Whatever route is taken, a real-time system enabling users to see their positions intra-day seems like a valuable proposition, seemingly adding value for customers. But what else can it offer? Although Walton-Green says it is difficult to state what RTN's primary benefit is ('it touches so many areas of banking'), it is certainly true that having data almost on tap can enable both bank and client to manage liquidity with greater confidence, and gain control over the exceptions process. Indeed, the two go hand-in-hand. An accurate intra-day global liquidity position ultimately means the days of over-supplying capital to cover exceptions are over. 'If you can reconcile today instead of tomorrow, you can use that liquidity for something else,' states Walton-Green.

RTN can also deliver improvements in administrative efficiency, greater transparency, and reduced risk in the form of increased payments certainty and knowledge that customers can be kept in line with their individual credit arrangements.

All of this of course means a bank is likely to improve margins whilst adding value for its customers. Indeed, Walton-Green notes that many banks now realise their corporates want real-time information on payments over the internet, rather than end-of-day batch reports. They also want to know their own cash positions. 'It simply

isn't acceptable to corporates that their bank, irrespective of size, doesn't know where their money is. And the only way a corporate can know, is if its bank knows.'

But Walton-Green points to another driver for real-time information that has altogether more serious consequences if left unattended: compliance. 'This is perhaps the single biggest thing that is starting to impact people's decision to take up real-time information in banks,' he notes.

The big banks tend to be hit first and hardest by the regulators, but the effects will always trickle down, eventually encompassing every player in the market.

'Not knowing what's going on until after the day has closed, which is too late to do anything about it, is clearly not best practice.'

Richard Pattinson, a senior director of Barclays and current chairman of the Real-Time Nostro User Group, certainly concurs with this view. He is quoted as saying: 'Real-time information is all pervasive in the banking world and a service such as real-time nostro is likely to play a major part in accessing and controlling such data as regulatory pressures grow'.

The improved visibility and control that both Walton-Green and Pattinson see in RTN sits well with the demands of Basel II. In order for a bank to maintain its capital adequacy ratios, it must retain a buffer with its reserve bank. The amount of buffer that is needed goes down if there is proven visibility. This can mean a well-managed organisation earning a superior commercial rate of interest with its reserve bank overnight.

Aside from the obvious demands of Basel II and other stringent regulations, a recent move by the UK's FSA (and other regulatory bodies may well follow) asks the largest financial services suppliers to be able to produce critical financial data on demand in the event of a crisis (see p38). This includes elements, such as liquidity positions, that are likely to change rapidly during such an event. These will require repeat updates as the information becomes available. Having a real-time data flow will facilitate such a demand.

RTN also has a disaster recovery capability, says Walton-Green. 'Clearly it is something that is outside of the bank. If you have systemic failure inside the bank, and you don't know what's going on because your systems are down, you would still have a connection to the outside world, either via SwiftNet or VPN.'

With a wealth of benefits then, it seems odd that uptake has been rather sluggish. The smaller banks might argue that they don't need intra-day data of this kind, but this brings us back to the point at the start of this article, that where shrinking margins and customer disloyalty are concerned, added-value of some description really is required.

That the technology has been slow to take off does, however, rather belie the fact that some of the world's largest banks are on board. In early 2003, the 18 major banks involved in the two obviously overlapping initiatives finally saw sense and joined to form a Real-Time Nostro Account Information Steering Group (RTNAISG). The Group comprised ANZ, Banco Bilbao Vizcaya y Argentaria, Barclays, BNP Paribas, Citibank, Danske Bank, DnB, Deutsche Bank, Handelsbanken, JPMorgan Chase, Mizuho, Royal Bank of Canada, Royal Bank of Scotland, SanPaolo IMI, Société Générale, Standard Bank of South Africa, UBS, and UFJ.

As a senior director of Barclays, Pattinson voiced the opinions of many at the time, saying that the industry needed one single solution, and that the establishment of the RTNAISG was 'a major step in the right direction'.

The Group subsequently chose Swift as its facilitator, and SwiftNet as the messaging platform for the industry. Were Gresham and C&W aggrieved? 'Swift are setting the standards in the area of cash reporting. The RTN is a cash reporting solution,' says Walton-Green. 'We are adopting the standards that Swift use, and then providing an outsourced service to the banks.'

In countering the accusation of slow uptake, Walton-Green argues that similar concepts of cooperation, such as CLS or Swift, took years to reach a point where they were enmeshed within the fabric of financial society. 'It will take us a while to get there, but with backing from some of the largest banks in the world, we're

making good progress.'

At the start of 2005, four of the early RTN adopters were live and providing data. At the end of that year, twelve were live. There are currently around 22 signed up to the Gresham/C&W RTN offering, including seven of the world's top 20 banks, and all of the top four. As Walton-Green points out, the top 20 banks are responsible for around 70 per cent of all international funds that are pushed around the world on a daily basis, so even with the limited coverage that RTN has to date, it still marks a significant volume of traffic.

Clearly the focus with RTN right now is for more banks to get on board, either on their own or on a white label basis. 'We have to get more providers and more users,' says Walton-Green. 'The more people that provide data into this, the more valuable that aggregated view becomes.'

Recent years have seen a number of other vendors, such as IBM, CSK Software and Network Computer House (NCH), plying their trade in the field, anticipating greater volumes of RTN traffic. Meanwhile, the structure of the Gresham/C&W partnership has undergone a few changes. Gresham continues to offer its RTN solution with C&W, but where C&W initially led the sales of the subscriber service, since April 2006, Gresham has taken over day-to-day management of the programme and now leads the sales process, with C&W scaling back its involvement.

With SwiftNet to the fore, the product focus has shifted slightly too, says Walton-Green. The system continues to deploy

C&W's secure centralised hosting facility and managed IP infrastructure, but the concentration is now increasingly on SwiftNet connectivity for receipt of data into and out of the hub. Explaining this shift, he says the aim is to 'leverage the infrastructure that the banks have already built'. This decision may well have been influenced by powerful newcomers to RTN, such as HSBC, wanting to make better use of their investment in SwiftNet.

But even with this agreeable new status, there is still room for the two-model offering. When C&W and Swift both hit the market with nostro cash reporting services, it would have been a fair assumption that one would lose out to the other. To date, this has not been the case. Indeed, a number of banks have opted for both models in order to meet customer demands. In August 2004, the spirit of cooperation extended when Swift granted C&W its own unique Business Entity Identifier (BEI) operating code. This allowed banks in the C&W clan to provide data into the RTN hub, and users to be able to source their consolidated reports over SwiftNet using a single Swift address.


But without applications to manage and manipulate the data once on site, the benefits of real-time information are largely academic. To this end, application providers have lined up to offer complementary services to the RTN solutions. The main players that naturally interact are those that are strong in the reconciliation space – vendors such as Sungard, Smartstream, CheckFree, and City Networks between them they have

something in the order of 90 per cent of the market. RTN also connects up to 30 or so different payment systems. 'The opportunity for all these players is to help banks change their systems to meet increasing regulatory demands,' says Walton-Green.

He stresses that in order to fully utilise RTN, a bank must really want to tie it in with all its core systems. This, he says, would leverage the possibilities of real-time reconciliation and real-time liquidity management, hence the strong interest from the other vendors.

But Walton-Green acknowledges that not all banks have the functionality for this kind of service. In this case he recommends starting from the position of having the data so at least the treasury department, liquidity managers, or compliance people can review what's going on. This, he says, would enable the bank to manage its higher ticket items. From this position, more internal users can be added on the browser side.

The next step is to integrate data directly into the core systems, as has been done at Barclays and Royal Bank of Scotland. This allows true online and real-time processes such as the afore-mentioned reconciliation activity, which can be used not only for internal bank consumption but, in some cases, may even be sold on as a packaged offering for corporate customers who might similarly require intra-day global cash position data.

In a commoditised banking world, being able to supply this level of service to your customers is surely adding value. 

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