A new treasury ecosystem:
Leveraging the evolution of transaction banking

HSBC | Opening up a world of opportunity

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Treasury is not an island; it is influenced and supported by the ecosystem that surrounds it. Transaction banks play a pivotal role within this network – and they are continually innovating to enable treasurers to leverage industry developments such as banking-as-a-service. As a result, business models are changing, sustainability is rising in importance, and co-creation is the order of the day. It's time to 'let go of the legacy' – and no treasurer can afford to get left behind.

The natural world offers many parallels to the business ecosystem. It is a competitive environment where climates can be hostile and unpredictable. In order to survive, and prosper, many species have adapted in incredible ways. Take the Alaskan Wood frog, for example.

This ingenious amphibian enters a semi-frozen state in winter; it stops breathing and its heart stops beating. Surviving temperatures of -60C in this suspended state, the frog then 'thaws out' in spring and continues life as normal. Meanwhile, at the opposite end of the extreme weather spectrum, the kangaroo rat has evolved to survive in the desert without ever needing to drink water[1].

Corporates and banks are becoming similarly creative in finding ways to adapt to the shifting operating landscape. Jared Smith, Managing Director, Global Head – Corporates, Global Liquidity and Cash Management, HSBC, comments: "In the past 18 months we have seen a huge push towards digital interaction. While this was the broader market trend, it has been accelerated by the Covid-19 pandemic."

In this rapidly evolving environment, resilient corporates are flexing their business models. "We are witnessing the rise of electronic platforms and marketplaces where both buyers and sellers are able to connect. Direct-to-consumer (D2C) sales are becoming essential survival strategies for organisations, even those that have never contemplated such an approach previously. It's very much a case of evolution in sales channels in order to supplement traditional distribution mediums," notes Smith.

In turn, this shift has created a need for corporate clients to have flexible payment and collection solutions embedded within these platforms. Channel-agnostic collections have become a critical ingredient in modern business, says Smith, in a nod to the bank's Omni-Channel proposition. Having flexible foreign exchange (FX) rate propositions baked into e-commerce platforms is also becoming more important, he believes.

[1] https://www.businessinsider.com/these-7-animals-have-crazy-adaptations-to-help-them-to-survive-in-their-habitats-2016-7?r=US&IR=T#kangaroo-rats-survive-without-ever-drinking-water-2

"International buyers and sellers want transparent FX rates. We are operating in a world where 'hidden surprises' in business transactions are no longer welcome. In fact, negative online interactions can now taint entire business relationships. Clarity and visibility are called for in all aspects of online business in order to deliver the best possible customer experience. And accurate, real-time data for all parties in the supply chain is vital."

Embedded finance opportunities

One development that could help corporates to deliver this optimal customer experience that Smith describes, is banking-as-a-service (BaaS). According to Brian McKenney, Chief Innovation Officer and Head of Strategic Initiatives, Global Liquidity and Cash Management, HSBC, BaaS involves banks enabling customers to embed financial services into their own products – hence why it is sometimes called 'embedded finance'.

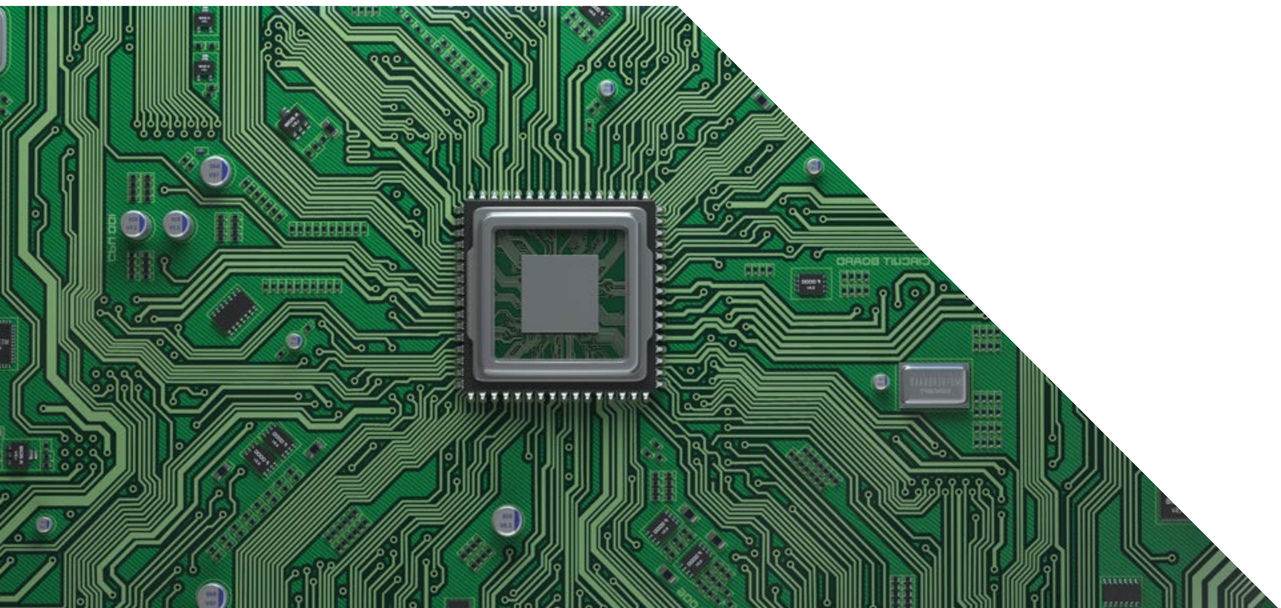
"The client can offer the bank's solutions to their customers and/or their suppliers – all via seamless API-based solutions," says McKenney. This could range from payments capabilities to lending, insurance and investments – so treasurers may well find this on their radar in the months ahead. "Potentially, this is a great opportunity for treasury teams to collaborate with their colleagues in product and strengthen the sales proposition by embedding financial services in their products. By doing this, companies in many different sectors could see greater customer conversion and retention, which could ultimately translate into increased, and more predictable, cash flows. Some organisations are also re-inventing their business models on the back of BaaS developments [see box 1] and it's exciting to see treasury teams pivot to adopt the capabilities that transaction banks are offering."

Although the term 'BaaS' feels relatively new, some sectors are already leveraging it to great success – think of food delivery and taxi apps, for instance. Financial institutions (FIs) have also been pioneers in this space, laying the groundwork for embedded finance, says Nadine Lagarmitte, Managing Director, Global Head Financial Institutions, Global Liquidity and Cash Management, HSBC. "Historically, many of our FI clients have provided their customers with services whereby a banking product is consumed as some part of the client journey, although, in the past, this might have happened through a separate platform rather than being fully integrated."

Examples of such transactions include sending a digital payment to settle a premium for an insurance policy that has just been purchased; funding a margin call into a trading account with a broker; or securing working capital financing. "But all of these have typically involved leaving the service provider's environment, and separately engaging a bank to buy and/or use this product," she explains.

Now, with embedded finance, the same banking services will be seamlessly integrated into the corporate's platform or ecosystem 'as-a-service'. This will have two main benefits, says Lagarmitte. "Firstly, it will reduce friction and enhance the experience of the underlying customer. Secondly, BaaS will broaden the offering that our clients can bring to their customers, enabling complementary products to be offered at the point of need, potentially generating new sources of revenue."

From a treasurer's perspective, this means that their banking partners are now taking on an additional role – they are becoming potential partners for the broader business, not just the finance function. McKenney comments: "This is a turning point in the traditional relationship between transaction banks and corporates. It's also an opportunity to tear up legacy business models and embed totally new, better and more sustainable ways of operating."



The new business ecosystem supported by APIs

Turning the tables: BaaS in action

Bringing the concept of embedded finance to life, McKenney cites a hypothetical example. "Imagine furniture retailer, which primarily sells to consumers. This organisation is reviewing the way it interacts with customers, and the way customers use, and dispose of, its products. The company is aware of a secondary market for its products – whereby used goods are sold on via online marketplaces or community noticeboards.

"With new business opportunities in mind, as well as the desire to embrace a circular economy model in order to reduce carbon emissions, the company is looking to roll out a furniture-as-a-service model. This is essentially a loan agreement where the asset that's pledged is the furniture – and the lease is all arranged seamlessly at the point of purchase," McKenney explains. "Through this model, the buyer pays only a portion of the original price of the furniture and pays only as long as they use it. When they return it, the loan agreement is terminated – but then another customer can make use of the furniture, again through a loan agreement."

At the same time, the retailer is considering new markets, such as the office furniture sector. "Again, the leasing model would work well here and could significantly increase revenues," says McKenney.

In summary, by offering furniture-as-a-service, the company can extend the life of an asset, reduce waste and improve sustainability metrics, while increasing the number and type of customers the organisation deals with. "BaaS is a catalyst for business transformation – and one that treasurers should be keeping a close eye on," suggests McKenney.

Taking ESG to heart

As the above example illustrates, BaaS can be extremely effective in combination with environmental, social and governance (ESG) initiatives. And according to Smith: "Treasurers have a significant opportunity to work with their banking partners to add value to the wider organisation by proactively contributing to ESG efforts."

McKenney agrees, adding: "Forward-thinking treasurers are already embedding ESG into their daily processes, so it's business as usual, rather than a standalone initiative. We know that embracing sustainable practices can offer resilience to shocks, and boost growth potential over the longer term, so building ESG into treasury activities is an essential part of robust future-proofing and adaptability."

As the focus on ESG intensifies, so the range of sustainable solutions open to treasurers is growing too. "While green assets have been the talk of the town for a while, and flows into our green deposits continue apace, what we're starting to see is a rise of the 'S' and the 'G' elements," says Smith. Sustainable deposits are also being created to enable corporate money to be earmarked against social bonds held by banks, for instance.

More innovation is hotly anticipated in the ESG space, from short-term investments to FX. Cross-product ESG innovation is also on the radar. And it's an area where McKenney expects much more interaction with corporates in the months ahead. "ESG-conscious organisations are already challenging the banking sector to be even more creative in our provision of sustainable solutions. They are clearly stating their ESG needs and looking to the banks to deliver cutting-edge solutions. As we head towards 2022, this co-creation dynamic will result in products that not only assist treasurers in their day-to-day responsibilities but also benefit the triple bottom line – people, the planet, and profits."

ESG adds real value

Despite 'greenwashing' being mentioned in the ESG headlines, there is real progress happening in the space, McKenney believes. HSBC's research shows that more than half of investors and three-quarters of issuers say the pandemic has either reinforced their commitment to ESG or made them realise they'd paid too little attention to it.

HSBC Global Research has also found that stocks of large companies with stronger ESG ratings have outperformed the global average by 4.7% since mid-December 2019. For climate-related stocks the gap is even bigger, with performance 13% better than the global average over the same period.

Combining expertise

Co-creation has already proven fruitful in the digital space, says Smith. "I only see this trend accelerating in the years ahead – it is a critical concept that drives many of our client engagements and subsequent product development." The important element to note about co-creation is that this particular type of collaboration is based firmly on client needs. "This underscores the notion that while banks may be able to provide a capability map for core parts of their products, innovation in the truest sense is largely client led," emphasises Smith.

One example of this is the collaboration HSBC began in 2019 with Singapore Exchange and Temasek Holdings to explore the use of distributed ledger technology (DLT) in local bond markets. The result was the launch and settlement of the first digital bond issuance on the exchange's digital servicing platform in September 2020, completed for Olam International. The project took the bank into new areas of explorations, says Smith, using an on-chain payments solution which allowed for seamless settlement in multiple currencies and enabled the transfer of proceeds between Olam and its counterparties.

Lagarmitte adds: "We can now look to deploy similar solutions for other clients – that is the beauty of co-creation. Clients often have similar challenges. Some are just more vocal than others, so they have solutions built for them by the bank and its fintech partners."

McKenney echoes this, noting that: "Demanding clients have transformed at a rapid pace. They challenge us as a bank to do better for them every day. While once this might have appeared to be an unusual way to approach a banking relationship, it's now becoming the best way to innovate. We actively encourage open and honest dialogue with our corporate clients – we want to know how we can deliver more for them."

Arguably, he believes: "Co-creation between clients, banks and fintechs will form the basis of solid relationships in this new era of collaborative working – especially where BaaS is concerned. At every point of reviewing treasury operations and looking to optimise, the corporate and the bank should take time to bounce around ideas and look at ways that innovation can be inserted into workflows, or could even transform the business model."

Review and upgrade

Against this backdrop of evolution in the transaction banking space, this is the moment for treasurers to consider taking stock of their current treasury set-up – and challenge themselves, and their banking partners, to improve. Manish Kohli, Head of Global Liquidity and Cash Management, HSBC, comments: "Now is the time to look to the future. With the catalyst of the Covid-19 pandemic at their back, and the advent of exciting solutions encompassing embedded finance and ESG innovations, treasurers have a unique window of opportunity."

From cash flow forecasting tools to real-time data at the touch of a button – treasurers can, and should, challenge their banks to deliver. As Kohli concludes: "This is the era of as-a-service transaction banking. It's time to let go of the legacy and build for an agile future based on digital and sustainable foundations."

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