VIEW POINT

PLATFORM ECOSYSTEMS: A SECOND CHANCE FOR PAYMENT HUB SOLUTIONS

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Payment hubs were supposed to be the backbone of payment transformation in a bank. However, a payment hub as a concept and as an application itself has changed. While originally serving as one place to manage all things payments, now, payment solutions are more modular and allow flexibility to be deployed for individual payment types or for managing a singular process across multiple payment types. Payment hubs now look to bring in the efficiency of a modern solution at a far more granular level instead of at the holistic level as originally envisaged. What caused this transformation?

The biggest impediment was the cost to 'rip and replace'. Costs were often much higher than what was originally anticipated, and many banks had to abandon their efforts halfway. Organizational challenges around the way payment business teams were organized in the banks also played a role: for a program this size to be successful, all product teams had to align their vision and investment objective.

Fast forward to 2023 – is the concept of a payment hub dead? At its most basic level, the payment hub application orchestrates a payment transaction and ensures that the bank does not lose visibility all throughout the lifecycle. Given the multitude of payment types today, banks possibly need this capability more than ever before. While today's payment modernization initiatives may not involve a single central solution to act as a 'hub', many banks are investing in building smaller chunks of functionality that are loosely coupled to replicate a payment hub-type environment. The payment hub is not dead, but in this new iteration, the journey looks different, and banks now have new options to implement.

To build or buy: What makes the decision even more pertinent today?

Banks beyond a threshold size face the question of building or buying. In the last five years, accelerated digitization and growing popularity of real-time payments have influenced these decisions. While there are many factors at play, Infosys has observed the following 4 key recent trends in banks taking the 'buy' option:

1. Developing tighter ecosystems with customers and other banks

Payment applications are no longer operating in isolation. They are now expected to be part of a broader platform ecosystem within their customers' treasury and accounting platforms that can access data and transact almost instantaneously. Being part of this broad network, interfacing with other applications that customers use while maintaining a seamless flow of information - is often beyond the scope of just one individual organization. Some market-ready payment applications cater to this functionality more effectively. The strength of their alliance networks, and a cadence of integrated testing processes that some have defined amongst themselves, gives them the advantage of managing these types of external integrations far more efficiently than any individual bank can accomplish on its own long-term.

2. Adapting to dramatically different expectations around data

Clients seek data from banks for everything from information reporting to reconciliation and analytics. Modern treasury systems and accounting platforms are generating more data as well as insights than ever before, and now banks are expected to do the same in real-time. Data needs are also constantly evolving, and the transition to data rich XML-based payments is a prime example.

Third party payment applications either from leading payment players or fintechs in the market again carry an advantage whenit comes to managing the flexibility that clients expect around data. As an example, many banks in the United States are still working through their ISO 20022 transition journey, while most leading vendor applications are already there. Clients and customers expect much faster and more transparent data across in all parts of the process and we expect this need to keep growing. Data tends to always be the foundation, and we believe some of the leading payment products have created a solid data foundation to build their applications on, that gives their customers a head-start when it comes to data.

3. Managing change through bank mergers and acquisitions

Most home-grown applications in banks tend to hug very tightly with their specific processes with little allowance for variations. When banks merge, mapping processes between two different banks almost always brings difficult challenges. Vendor products can offer an easier transition due to higher levels of industry standardization and configuration options that accommodate process deviations.

4. Adopting new payment types with an increasing complexity around speed and compliance

Instant payments are quickly growing as one of the most preferred modes of digital payment, and leading banks all over the world have invested heavily in this space in last 36 months.

Given the deluge of new payment types emerging, payment product providers were quick to create standardized solutions for instant payments. These solutions – all built on powerful XML data structures, and through 'smart technical architecture' – were able to support many different instant payment types through simple 'configurability'. This standardization has helped the providers roll out solutions much faster and cheaper.

On the other hand, we've seen banks forming different silos of teams to support some of these newer payment types with each team on their own path, drawing up their own roadmaps and timelines. As we see today, in some cases, these implementations may not have worked as expected in terms of client adoptionand/ or a consistent customer experience. Also, given the uncertainty of customer adoption, many banks have been cautious in committing to any large investments and have resorted to supporting 'limited functional capabilities' in initial phases.

Here again, we believe a 'buy' approach leads to a cost and time advantage for banks: higher levels of product configurability which enables support of these newer payment types with significantly lesser effort.

Erika Baumann,

Payments Practice Head at Aite-Novarica

"The flexibility of what a modern payment hub solution provides today offers so much opportunity for financial institutions of all sizes to modernize and implement infrastructure that supports not only the current end-user demands, but also the flexibility to adapt to new demands over time. This is a critical time for financial institutions as end-users are more receptive to utilizing Fintechs for cash management and payments needs. Banks have to respond by providing more robust payment options and better tools to support the experience. Without investment in modernization effort to meet these demands, banks are at significant risk of losing clients as well as diminished new customer acquisition."

A Case for Banks that Choose to 'Build' Instead of 'Buy'

Despite all advantages, some banks still prefer the 'build' approach. Banks have a clear visibility into industry, trends, and customer adoption better than anybody else, and they may decide it's more strategic to build in-house, even in the constantly evolving payments technology landscape.

Banks who choose to take the 'build' approach typically prefer to be able to manage the complexities of their internal technical environment themselves – rather than depend on the vendor, as well as create a level of differentiation. Vendors, on the other hand, love a repeatable, cookie-cutter approach – and adapting their products to a specific non-standard environment requires higher customization. When banks start to heavily customize vendor products, costs escalate, and programs may run into trouble. Banks also want to be in control of managing their own payments destiny in the future and try to avoid a dependency on the vendors.

Banks may also avoid vendor solutions due to:

- **Creating a price mirage**

  The overall implementation costs can turn out to be significantly higher than the original proposal.

- **Vendors being driven by new customers**

  Changing business priorities and commitment levels makes it difficult for the bank to have the same level of product or roadmap influence.

- **Lack of a stable roadmap for implementation**

  When banks buy a product, they get frequent upgrades and better functionality. But for that to happen successfully, vendors' product vision needs to consistently align with the bank's priorities.

- **Risk and compliance requirements**

  Any change to vendor products has a dependency on their release schedules and product maintenance process. Risk and compliance issues need a quick response time, which is sometimes faster in-house.

Our recommendation: Find the middle ground for smarter payment strategy.

Creating a more fragmented payment environment to support emerging payment types and related processes does not simplify the environment, but neither does having one singular application for managing 'all things payments'. The latter actually tends to create its own challenges.

So, Infosys recommends a hybrid approach which entails a **foundation layer composed of a basic market-ready vendor product,** but also **'complemented' with a strong 'differentiation layer'** that the bank can own and build over time based on how their customer and/or internal needs evolve.

Through their modern architecture, leading payment products in the market today offer such 'differentiation layers' in the product itself. This gives the bank a platform for easy customization and in many ways a direct control over creating their own distinct payment journey. Choice of specific customizations, when and how to do it, can be defined and driven by the bank. Smaller banks that prefer a more 'out of the box' approach can benefit from a market-ready solution as well as the 'configurability options' to create their own product nuances in future if required. From a technology perspective, the stack becomes more manageable and creates more bandwidth for the bank to focus on areas that really matter.

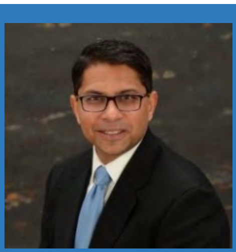
A hybrid approach reduces the focus of banks from rebuilding something that already exists in the market to instead focusing on what their customer, risk managers and service staff want. It forces banks to critically look at their differentiation strategy and ensures sharper focus on costs. By allocating budgets to the areas that matter most, banks can create a much higher ROI for their investment dollars.

Mohit Mehta

CTO, Wholesale Banking and Payments at Truist

"Technology teams are always faced with the task of having to do more – with less. At every opportunity – they are wanting to ensure that their investment dollars go further in creating better value for their customers. Our focus at Truist is always just on that - how can the investments we seek to make today, create a more unique, intelligent or an efficient offering thru products or service for the customer. It could be use of smarter analytics, better risk control or even efficient customer servicing tools – all of which help creating a positive payment experience for our customers. We really want to focus more on these critical areas, we believe these are the key differentiators. This is what in our opinion, future client relationships are going to evolve around."

Author



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Rahul Heads the Global Commercial Banking practice for Infosys. He is a seasoned banking professional with more than 20 years of experience in product management and technology for US and European banks. Over the course of his career, he has been involved in successfully leading several transformational programs in the wholesale banking space around payments, credit and operational risk management.