FORM3 FINANCIAL CLOUD

If a problem shared is halved… how much smaller can we make it together?

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We get asked a lot for our views on Brexit and its potential implications for our PSP and Bank clients.

In the world of payments, knowing the answer to any regulatory impact and its unintended consequences can be really tough ahead of an event.

What I can share is how we think about technology and tackling mandated changes for business critical and customer critical services.

Legacy brought into focus:

Brexit has opened up some serious challenges and uncertainties – where you are based matters, where your data centres are located matter, which instances you run matters, and how fast and faithfully you can add new instances and environments matters. In a legacy technology estate which is predicated on performant, centralised tech in proprietary data centres – these are real challenges, expensive challenges, and critical challenges to overcome.

How do you spin up new links, new connections, and new processing capability into new markets to enable you to operate in the UK and Europe seamlessly whatever Brexit throws at you? You can rebuild, or you can think about leveraging technology which is flexible, scalable, resilient, secure and most of all simple to consume and spin up.

Lets' game out a Hard Brexit for a few of the types of clients that we work with:

UK only banks with EUR accounts in London

One of the major benefits that banks have benefitted from in the UK has been access to both EUR and GBP clearing systems through a single location. A very efficient model providing local processing access for payments across both markets. In a hard Brexit, will the same level of access to EUR clearing be available? If not, then it practically means moving either to a cross border / cross currency disbursement model for your payments or exploring the use of local businesses in market to hold your clearing access. The former is expensive at a transaction economics level and imprecise settlement timescales can make this model unattractive from a user journey perspective but is a very credible option for low volumes – provided you have the infrastructure in place for those cross-border flows.

The latter will depend on the status and nature of your business in market, do you have the required licences and as importantly the ability to deploy local operations and technology – starting from scratch could well be a challenge here.

UK banks passported to Europe

For those UK institutions which have leverage the passporting rules for access into European markets for local clients a 'Hard Brexit' may lead to the need for applications for new local licences directly from a European regulator. Now in practice it may well be the case that for many clients these relationships exist, certainly informally, but there is clearly a difference between that and more formal ongoing oversight. In that case, the application for licence and indeed the decision over the nature of licence required will all be a critical consideration. In any event, this provides a challenge to deploying a business model and a technology infrastructure that suitably satisfies that new regulatory oversight.

European banks passported to the UK

Much like for UK banks operating in Europe, under a 'Hard Brexit' there is no guarantee about the approach and status of operations in the UK for European banks. Just as with UK banks operating across Europe, it will be critical to assess the nature of oversight and the necessity for local operations and infrastructure.

UK branches of foreign banks

A somewhat underpublicized, but critical group of Banks are those who are international in nature but who utilise London as their base for both domestic UK and European operations. For these banks any 'Hard Brexit' changes to passporting or clearing access will absolutely be of importance. In some respects, these challenges may be even more magnified. Typically, these branches / offices perform critical services to support important group wide clients or services, but in many cases do not handle the same scale of payment volumes which may be enjoyed by local banks with larger local consumer franchises. For these UK branches, the idea of subdividing or creating new locations, entities and operations to maintain the current levels of service for end clients who may be on other sides of the world, is a really tough ask. In many cases these organisations have not benefited from the scale of group wide transformation programmes on payment infrastructure undertaken by many large banks over the last 10 years. Instead they are running old, legacy, locally deployed and in some cases very manual activities – replicating these, is, in some cases simply impossible and at the same time essential.

In any of the cases above local oversight and local business presence means local licences, multiple direct central bank relationships, and / or new banking partners combined with a data centre and technology model which enables that.

Worst case, for payments you are going to need to evaluate business presence, local licence and infrastructure for multiple locations.

For one of those locations, it's a scaling back of what you already have in place – technically, probably, not that complex, but economically this might really hurt. Wrestling with your unit costs against reduced volumes makes for challenging competition against bigger local players and economies of scale between markets will be harder to achieve. But in this circumstance, you're already connected, permissioned and with operational processes for managing client servicing and payment processes.

For the other location(s), you need to either carve your infrastructure and deploy it locally to that new environment (really tough) or spin up a new technology platform to access that markets clearings for your clients. That's not a single payment scheme issue, it's a full access issue. Keep your eyes open for the inevitable incremental licence fees and support fees.

These changes may also cause you to take a look at whether your now segregated volumes warrant a different settlement model with direct access clearing scheme and central banks – this is a lapse time measured in many months – something you'll need to look at in short order. There are clearly some major risks here – for those who do it well though, a potential differentiator and a chance to capitalise on the hard work.

Softer Brexit

In a 'Softer Brexit' there are clearly an infinitely wider range of options that may evolve.

On the licence front

Varying degrees of passporting may greatly reduce the complexity of the regulation from a hard Brexit, right through to no change – but it is probably fair to assume a greater interest from UK and European regulators in parallel and the ability to demonstrate the appropriate management of your operations in these multiple markets, supported by very robust MI and logical segregation will be important.

On the payment technology and clearing access front

Again, a continuum from maintaining what you've got to full separation. I would suggest here the biggest challenge is to manage the efficiency of scale vs independent operation. Uncertainty here is probably one of the biggest challenges you really face - at a minimum MI is going to be totally critical to your success as is resilience – sub scale builds and bolt ons to achieve the timescale will certainly be something to avoid if you can, for many that may not be possible, but the complexity in this arena is already extreme and adding more cannot help in the long run. 'Designed-in' flexibility now must be the aim for an evolving soft Brexit.

One area that offers some real hope for all of the clients and potential clients that we talk to is the use of cloud native payment platforms. A catalyst of change, of the scale of Brexit, happens once in an economic cycle and gives all financial institutions the chance to pause before adding to legacy estates with replicated legacy in more locations. Now is the time to step change into a platform architecture which can exist in any market. These architectures seamlessly exist in multiple locations, provides access in an integrated way and enable local as well as harmonised approach.

Seizing the initiative in this complex arena by quickly and efficiently gaining access directly to clearing systems, is one way to tackle head on the challenge of worsening unit economics from segregated volumes and at the very same time enables clients to take advantage of the now established real time user experience that all of us expect from all of our banks.

Even more importantly, in a multi-tenanted model you are not alone working this out. We strongly believe that our clients represent a community. We are custodians of a shared technology for them and because of this any changes are delivered once - for all clients, any scheme changes are deployed continuously - to all clients and powerful real time API's insulate our clients and provide the same access – to all payment schemes. It is our belief that our clients should be able to focus on ensuring the 'outcomes' of payments are both safe and cutting edge, without the need for each client to become an expert on all of these issues.

We don't have all the answers for Brexit – no one does… but we are serious about ***'powering the future of payments'*** – sometimes that's amazing real-time payment journeys and sometimes it's about helping to take on challenges like Brexit with our clients.