



The Shift from Paper to Electronic Payments

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The Shift from Paper to Electronic Payments

Executive Summary

Trends and Implications

Impact Drivers

Action Plan

- Size the Impact
- Locate the Impact
- Refine Factory and Business Strategy

Questions / Discussion

Executive Summary

Paper volumes are declining, transforming the economics of treasury management

Treasury Strategies projects that declining paper volumes could reduce treasury management revenues by 5 to 10% and pre-tax profit by as much as 15 to 25%

The impact for a particular institution will depend upon a variety of factors:

- Customer portfolio composition
- Operating infrastructure
- Scale position
- Business strategy

By assessing the impact of the shift from paper to electronics, financial institutions can develop operating and business strategies to mitigate the impact and leverage opportunities

Trends and Implications

Trends and Implications

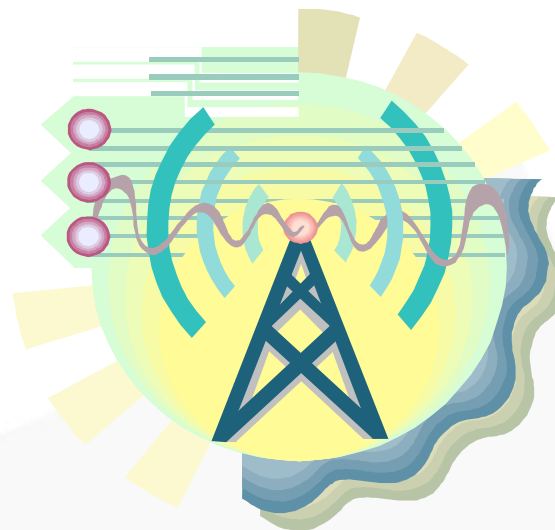


Paper volumes decline

- Margins deteriorate
- Scale dynamics intensify

Electronic volumes increase

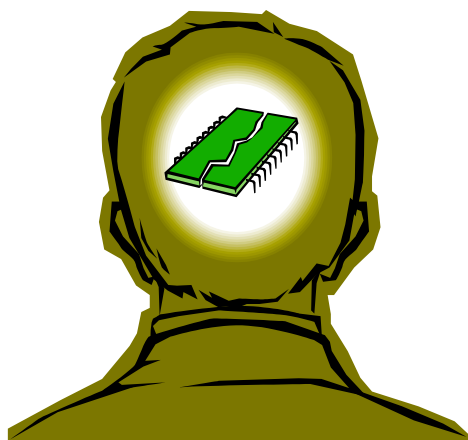
- Risk increases
- Winners yield scale benefits
- New exchanges evolve



Trends and Implications

Float and idle balances decline

- Decline in paper volumes produces corresponding reduction in float
- Firms invest more aggressively as electronic settlement improves confidence in cash forecasts



Imaging transforms business economics

- Scale dynamics increase
- Cost to serve declines
- New pricing strategies are introduced

Trends and Implications

New value-added services emerge

- Select competitors move further into the customer's financial value chain
- Electronic scale leads to new business and settlement exchanges
- Scale of electronic payments meets threshold needed to justify significant investment in trade integration and e-commerce



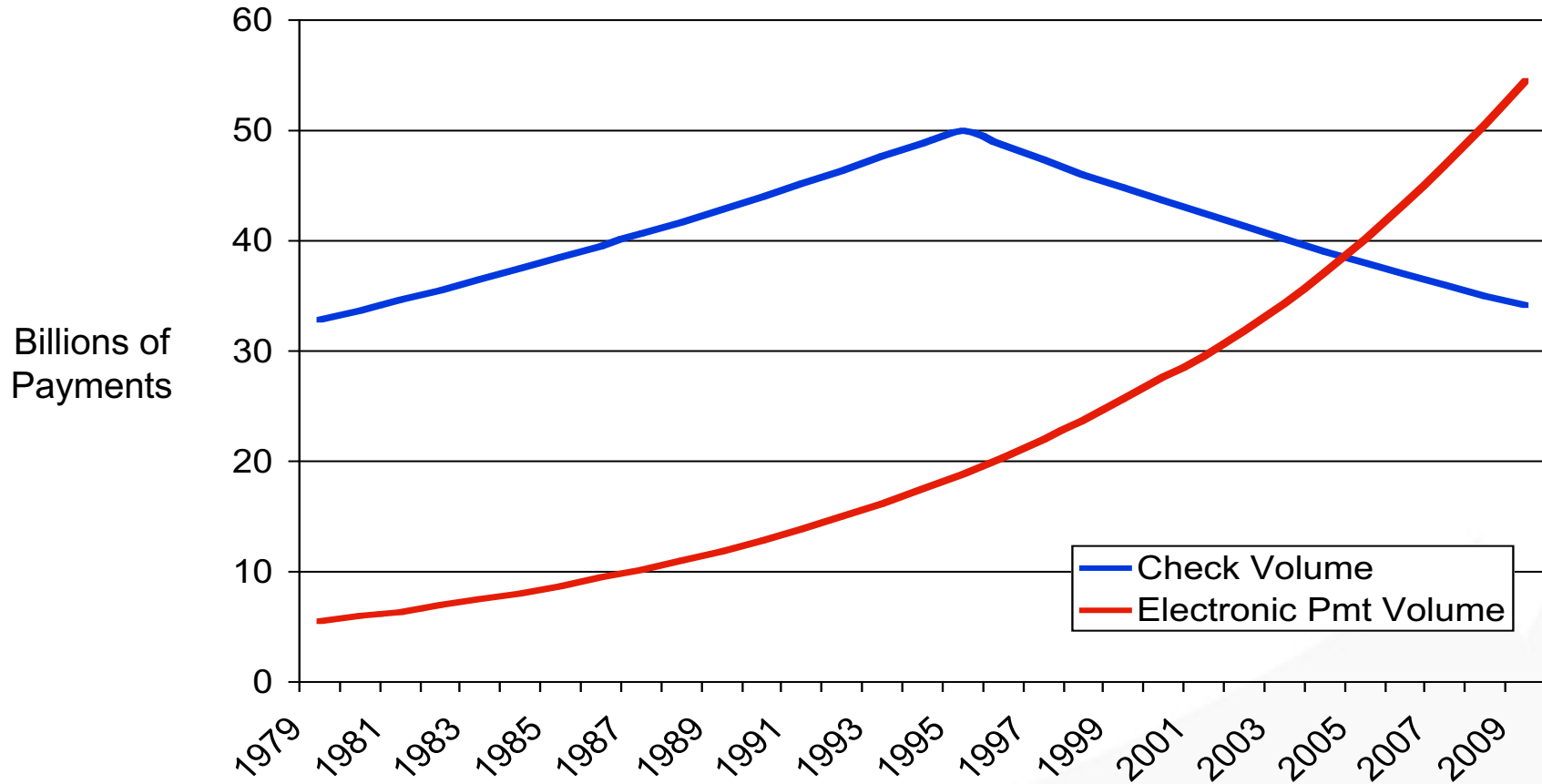
Trends and Implications

Adjusted for inflation, revenues could decline by 5 to 10% and contribution by 15 to 25%

	2003		2008	
	Revenue	Contribution	Revenue	Contribution
Paper - Based	200	60	140	15
Electronic	100	10	135	20
General	125	50	140	56
Information	75	40	90	45
New Services			?	?
TOTAL	500	160	505	136

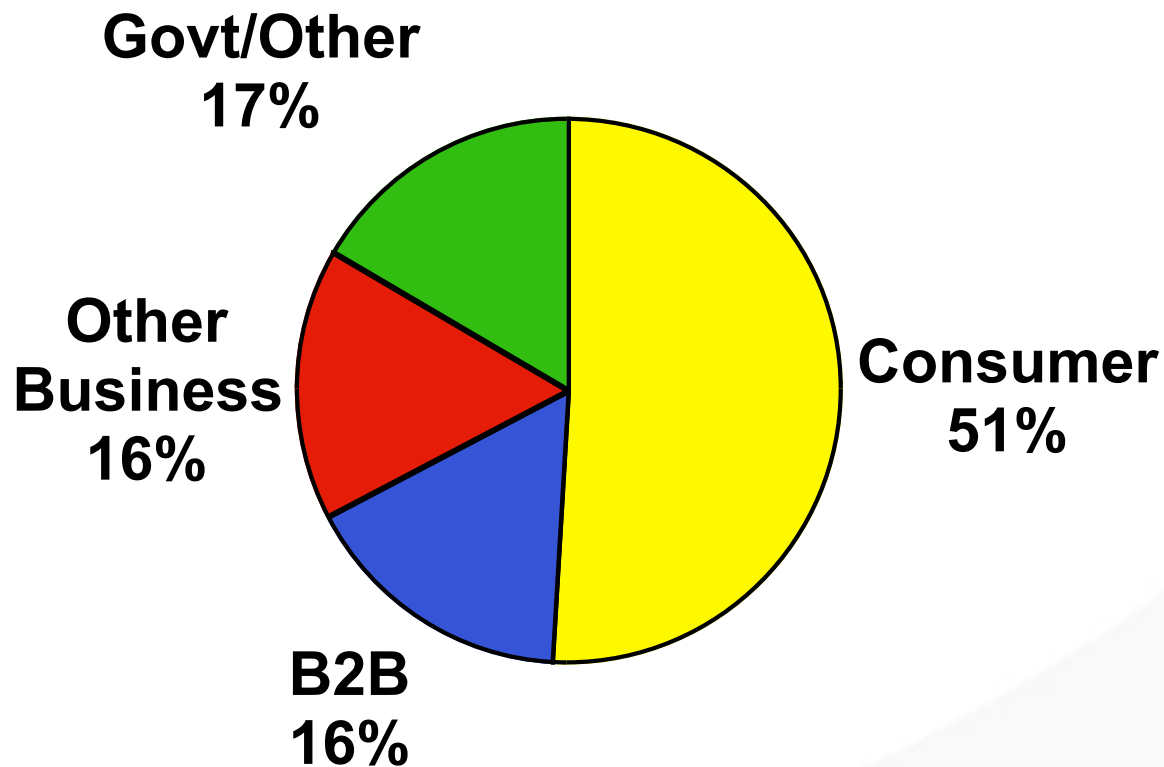
Example: Modeled bank with \$500MM in annual treasury management revenues (price x volume); impact on net interest margin not included in example

Paper Volumes Decline



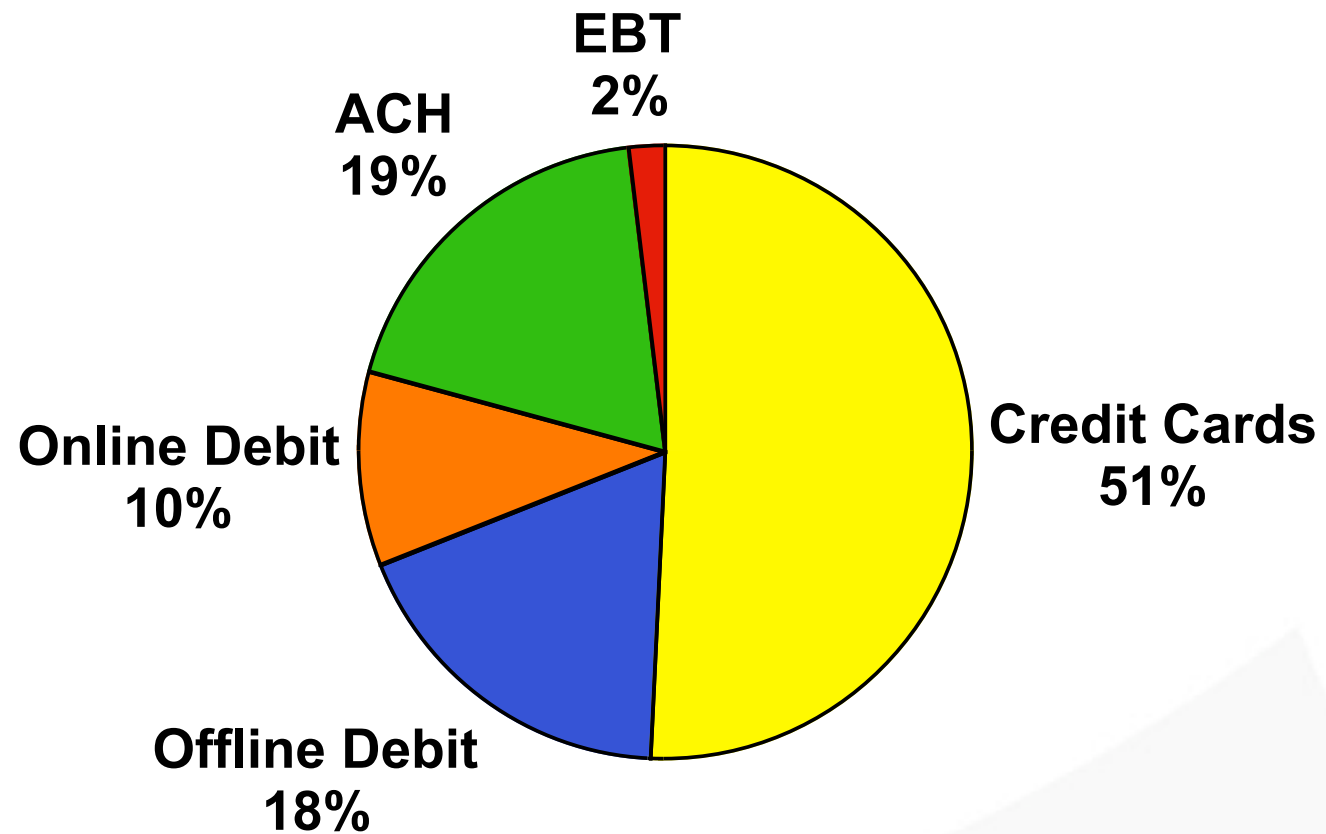
Source: Federal Reserve research; Treasury Strategies estimates

Composition of Paper Checks



Source: Federal Reserve research

Composition of Electronic Payments



Source: Federal Reserve research

Paper Volumes Decline

Not all paper volumes will decline at the same pace
Pace of change depends on clearing point and
counterparty dynamics



Cash letter

- › Significant declines possible as a result of check truncation - especially for non-local clearing points

Retail lockbox

- › Paper-based consumer payments convert to direct-debit, bill pay, electronic check, WEB / TEL, etc.

Imaging Transforms Business Economics

Scale players have invested or are investing in prime-pass image capture

- New service delivery models are arising in anticipation of check truncation
- Speed of image delivery has become a competitive point of differentiation

Image services reduce manual customer service requests

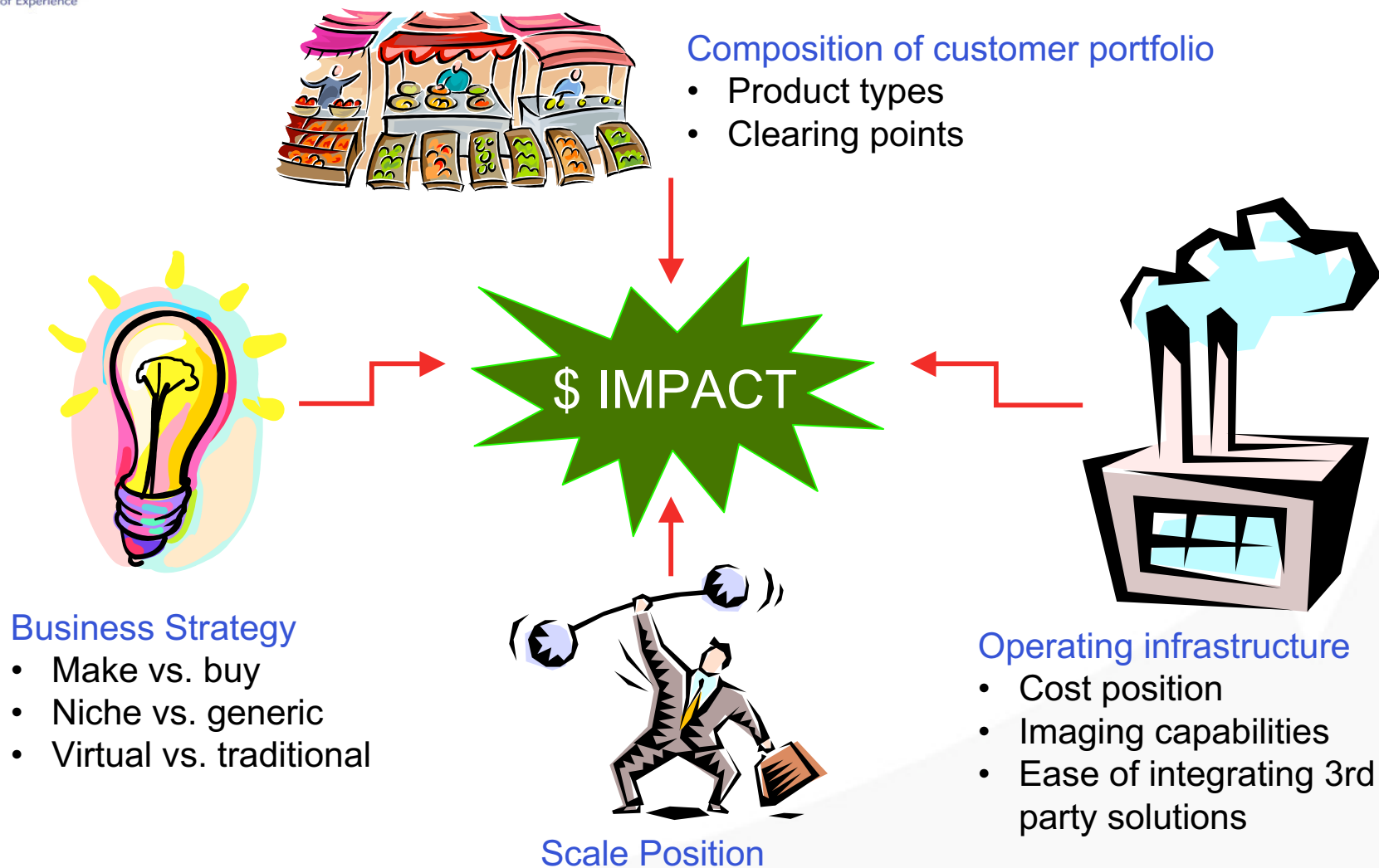
Financial institutions struggle to balance seemingly conflicting goals

- Yield revenue by selling image as value-added
- Reduce service costs by promoting broad adoption of image

Impact Drivers

What will the impact be for my institution?

Impact Drivers



Action Plan



Action Plan

1. Assess the impact
2. Locate the impact
3. Refine factory and business strategy

1. Assess the Impact

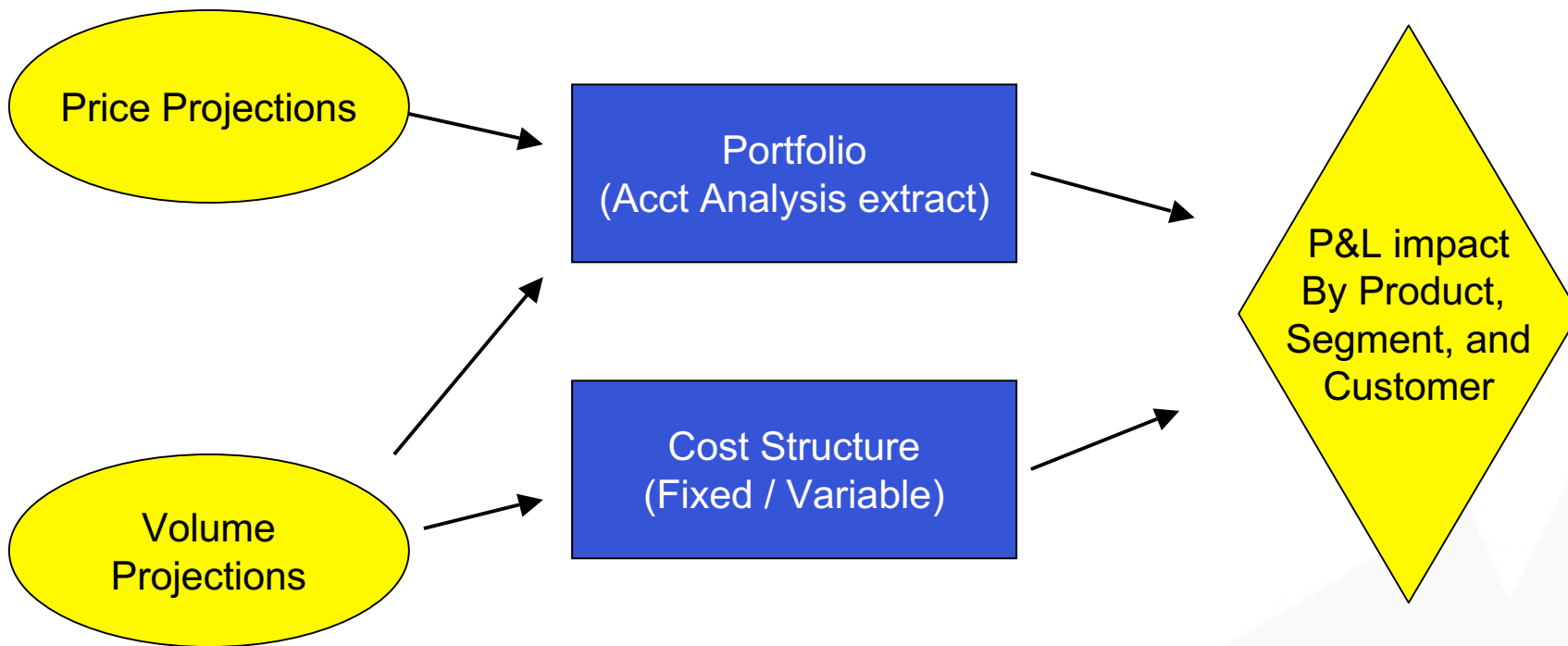
Understand change in revenue

- Project volume declines / increases by key portfolio segment
 - › Counterparty segments
 - › Capture and clearing points
- Assess changes in price by service / segment
 - › Pricing for paper-based services will increase steadily
 - › Competition may intensify for large-scale business to “fill” the factory
 - › Pricing for electronic services and imaging may be flat or increase modestly

Understand change in cost position

- Assess impact of growth / declines on cost structure
- Identify new investment requirements and impact
 - › Prime pass imaging
 - › Truncation

1. Assess the Impact



1. Assess the Impact

Sample Model Assumptions

Annual Volume Change	Small Business	Corporate	Private Label
Collections	-3.00%	-3.00%	4.00%
Disbursement	-1.50%	-0.50%	2.00%
Imaging	5.00%	4.00%	8.00%
Electronic	9.00%	6.00%	8.00%

Annual Price Change	Small Business	Corporate	Private Label
Collections	2.50%	2.50%	0.75%
Disbursement	2.00%	2.00%	0.50%
Imaging	-3.00%	0.00%	1.50%
Electronic	2.50%	1.00%	1.50%

1. Assess the Impact

Sample Model Assumptions

% Fixed Costs	
Collections	50.00%
Disbursement	60.00%
Imaging	50.00%
Electronic	85.00%

Current Cost Base \$MM	
Core Paper	136.50
Value Add Paper	32.50
Imaging	45.00
Electronic	70.00



The Power of Experience™

Action Plan

1. Assess the Impact

Sample Model Output

\$MM	2002 Actual	2003	2008
Collections	\$ 195	\$ 195	195
Disbursements	58	59	61
Imaging	75	78	87
Electronic	40	43	56
Total Revenue	368	375	399
Collections	137	140	151
Disbursements	33	35	36
Imaging	45	52	61
Electronic	30	32	35
Total Cost	244	259	283
Total Contribution	124	116	116
Margin	34%	31%	29%



Action Plan

2. Locate the Impact

Measure impact by key business segments - examples

- Market segments
- Products
- Significant clients
- Customer behavior
- Service channel

3. Refine Factory and Business Strategy

Model strategic options

- Invest to reduce costs
- Outsource
- Exit / enter markets
- Shift portfolio weightings / emphasis
 - › Market segment
 - › Product
- Private label / scale strategies
- Pursue new business opportunities

Questions / Discussion



Treasury Strategies Background

Independent global treasury management consulting firm

Founded in 1982

Services include:

- Global treasury and financial consulting for a wide range of domestic and international corporations
- Strategy, marketing, and decision support consulting for commercial banks and other treasury management service providers
- Outsourced treasury management support for corporations' treasury operations

30 + consulting professionals with extensive and deep treasury management and banking experience

Comprehensive focus on treasury management

Financial Institutions Practice

Treasury Strategies combines in-depth, customized consulting with powerful analytical tools – including more than a dozen proprietary computer models – to translate data into relevant, understandable information. Our efforts result in actionable solutions that address your organization’s priorities and complement its problem-solving style.

Treasury Strategies’ key competitive advantage stems from our experience and from the fact that, through our family of practices, we serve financial institutions and corporations. This unique balance enables us to provide unparalleled insight into each financial institution’s issues and priorities – insight that we transform into truly effective problem-solving strategies for our clients.

Treasury Strategies Can Help You:

- Grow your revenues
- Improve profitability of your product portfolios
- Determine your competitive strengths and weaknesses
- Understand your buyers’ behaviors
- Gain market intelligence
- Manage your customers’ liquidity
- Understand the implications of key industry trends
- Shape your critical strategic direction

