THE TRILLION DOLLAR CHALLENGE: LIBERATING CASH FROM INTERBANK HIGH VALUE PAYMENT CYCLES

Every day, the equivalent of over **US$10 trillion** in large value cash payments is made between banks, *after* other asset-specific netting and payment compression processes (e.g. CHIPS). To facilitate these significant global payment flows, over **US$1trillion** of cash is required to be held in bank payment systems as a liquidity buffer. The actual – and opportunity - cost to banks of having so much cash tied up supporting gross payments can be measured in the **US$10s of billions** every year. (Costs that can only increase as interest rates rise). Apart from these huge numbers, current processes for managing high value payments are inefficient and create unnecessary risk.

A new netting initiative, **Cash Netting Services (CNS)**, addresses these issues with an efficient, centralised service that identifies netting opportunities for high value payments.

Netting is not a new concept – it is used extensively by banks at a transaction level. In the FX market, for example, CLS Bank 'nets' some US$5trillion of gross FX volumes daily between bank counterparties. However, few central bank payment systems offer any form of netting capability, and those that do focus mainly on domestic activity. CNS analysis (based on extensive service modelling) indicates that bilateral netting between banks could reduce the overall value of these interbank payments by over 90%, representing significant cost savings and capital management efficiencies, while reducing associated risks.

"From an analysis perspective I can see [the CNS] concept potentially being applicable and beneficial to quite a significant degree." Global Bank

Effective control - and risk mitigation - of intraday liquidity supporting bank payments is subject to increasing regulatory oversight, with associated and onerous compliance obligations. Previously, regulators did not require banks to calculate – or report - cross-enterprise intraday credit costs accurately. However, Basel III and recent mandates such as BCBS 248 are exposing the real costs of intraday liquidity.

Latest regulations require banks to ring-fence sufficient 'High Quality Liquid Assets'(HQLA) to cover 100% of 'stressed' net cash requirements over 30 days (Liquidity Coverage Ratio). For major international banks, this can mean $billions of assets are inaccessible at any time. Interest charges ('cost of credit'), far more stringent capital adequacy obligations (CRD IV) and regular stress testing put further pressure on banks' cash and liquidity management practices and processes.

There is relentless pressure on banks to use capital more efficiently. Removing traditional business silos (e.g. by asset class) provides senior management with far greater visibility to a bank's overall capital utilisation and supports a more holistic approach to managing cross-business credit and counterparty risk.

While the requirements of the Basel Committee (and other supervisory frameworks) are ratcheting up cash and liquidity management costs, high value payments netting can reduce the size of cash 'liquidity buffers' and release significant capital (HQLA) back in to the business.

By reducing (compressing) the value of daily interbank cash payments using CNS, banks can reduce liquidity risk and enhance intraday liquidity and cash management efficiency.

Cash Netting Services (CNS) was launched by financial technology professionals and business entrepreneurs, John Barber and Nick Dyne. John Barber held senior positions in Dow Jones Telerate (MD EMEA) and ICAP (now NEX Group). Nick Dyne has a long history of delivering innovative financial technology solutions, from real time data servers to sophisticated 'straight through' trade messaging for FX transactions. It is partnered by CGI, one of the leading providers of transaction and payment netting software to international and central banks globally.

To find out more, contact nick.dyne@cashnettingservices.com or go to www.cashnettingservices.com

See also: **"Industry Initiative Targets $10 Trillion Daily Interbank Payments Flows"**