

Reducing the Risks of Multi-Country Bank Card Outsourcing



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“Multi country banks are now aggressively searching for harmonised, lower cost, centralised card processing platforms. However are they fully aware of all the key issues associated with major transformations and are they transferring too much risk to Europe’s card processing sector?”

Europe’s multi-country banks face many complex and difficult issues if they are to fully leverage their assets in the EU, CEE and the Russias. Many of these 25 to 30 banks are the result of a decade of takeovers, mergers, regional alliances and government privatisations. Unlike large domestic bank mergers, multi-country banks are often small players in any specific market. As a result many have found it difficult to realise significant economies of scale. In pre-recession days cost reduction, common products, and process harmonisation were given low priority when large profits could be made from lending particularly in the CEE and the Baltic countries. However priorities are now changing radically. Most large multi-country banks recognise that a loosely coupled collection of banking assets have to be consolidated into a unified banking group. But transforming many banks into one bank is no easy task, for local subsidiaries often operate to local rules and offer local products tailored to customer needs. In addition, the conversion of multiple, legacy processing platforms create significant migration problems for group wide harmonisation projects.

Why Multi-Country Banks Centralise Cards	Benefits
Implementation of common product offer/ frameworks	Improved product, lower marketing/sales costs, increased growth and revenues
Rationalisation of multiple country platforms	Lower IT maintenance costs
Reduction in system development costs	Lower IT development costs
Harmonisation of processes	Common group wide process
Centralisation of factory activities	Lower unit costs

Table 1: Key Drivers for Multi-Country Card Processing Centralisation

So where should common process begin and what are the build options? For a variety of reasons multi-country banks have first targeted cards – issuing, acquiring and ATM - as a high priority for rationalisation and major cost reduction. This starting point partly reflects a good business case based on the opportunities for rapid growth, plus the common products and infrastructure that Visa and MasterCard enable particularly in Eastern Europe. A second important consideration is that card processing can show large economies of scale if centralised and operated in a factory environment.

Multi-country banks have three primary options to build a group processing centre, namely: to use a single country card platform as a basis; to buy a proprietary software component; or to outsource to a commercial card processor. Also a fortunate few own all or part of commercial card processing businesses.

Card Centralisation Build Option	Typical Feasibility Assessment
Build on Upgraded Country Platform	Often old software, country specific, limited parameters and highly complex to make multi-country, high costs of enhancement, long timescales and bank's capability to manage project
Build with a Software Package	Attractive option for small/medium volumes but few large scale packages available – high cost of developing surround systems
Build with Outsourced Processing Service	Lower operational costs, centralised processing factory and scale capability

Table 2: Options for Card Processing Centralisation

However “how to build” is only the first of many complex issues to be resolved, the most important of which is to identify credible multi-country software and services, both of which are in short supply.

If we look back over the past ten years multi-country banks have a poor track record of delivering successful centralisation projects. Some banks made commitments with processors to deliver multi-country solutions but have since reverted to in-house solutions. Others have seen long delays in delivery and slow implementation. Why have so few projects been successful? To say multi-country card migration projects are large, complex

and high risk is an understatement. The number of legacy card processing platforms for conversion can sometimes exceed 10. Some banks with their roots in Western Europe have the added complexity of a need to harmonise domestic debit card scheme processing for both issuing and acquiring. Others struggle to define a standard group business and operational model. Local markets often resist common product mandates and as a result processing platforms must be highly parameterised to support many local product variations. Given these problems the boards of multi-country banks often conclude they lack the internal resources and skills to manage, develop and implement a group wide card processing project. Some decide that a solution can best be delivered by outsourcing to the card processing sector. However many banks are unaware that such a decision has risks and should thus not be made lightly.

Perceived Key Benefits of Outsourcing	
<ul style="list-style-type: none"> • Available multi-country application platform • Cost savings through lower processing fees • Availability of development skills/resources • Available project management skills/resources 	<ul style="list-style-type: none"> • Tested centralised processing plant • Standard methodologies for file conversion • Future proofed market leading innovation • Lower risk than in-house development

Table 3: Rationale for Outsourcing Card Processing

There are several reasons why multi-country outsourcing can be a relatively high risk. Many relate to a long term under-investment in new platform software. Over the past 20 years commercial processors have focused primarily on volume and delivering domestic market services. Meeting the needs of multi-country banks was perceived as a very high cost development with low returns. The typical customer profile consists of three to four modest markets plus many sub-optimal, low volume countries that may never show returns. Add the complexities of local debit and the failure of SEPA to remove barriers to entry and it is easy to understand why a business case to develop a new multi-country platform has been difficult to construct. In addition, some processors face similar problems to those of multi-country banks for as a result of M&A several have many legacy country specific platforms in need of

rationalisation. Only in the past two years have some of the major players invested significantly in new platforms. These are now coming on stream and reflect the very substantial investment needed to convert single licence software into multi-country user.

Large card processors have many strengths. Their principal skills are in providing high volume utility processing at low cost. Typically they seek to minimise bespoke development and are most comfortable with clients who can operate within their standard application features and parameters. As a generalisation, processors prefer to follow client's requests for new payments developments rather than lead, and few have track records of successful leading edge innovation.

Often processor core development skills have been built in markets where processing portfolio switching for credit card issuing and acquiring is relatively common place. However file conversion and data mapping tools fall short of the large scale bespoke development skills required to migrate seven or more countries to a common processing platform. As a result some processors are poorly equipped to build infrastructures that fall outside International Card Scheme (ICS) and Anglo-Saxon models. Tailored developments to support European multi-country debit protocols, diverse methods of clearing and settlement, POS and ATM authorisation and driving fall outside the experience and risk taking appetite of some processors. Despite these warning signals banks' expectations of the commercial processing sector are often surprisingly high and there is an unrealistic expectation of their capabilities to easily deliver outside their traditional model.

The recession in banking has also compounded the situation. Most of the simpler domestic market card processing outsourcing opportunities have now been delivered. Multi country processing Request For Proposals (RFPs) have increased as the recession has progressed. In the absence of other large scale opportunities, processors have sometimes little option other than to submit bids for these high risk implementations. Banks are often impressed by

low processing fees but often fail to appreciate the vendor’s capabilities to deliver large scale, semi-bespoke transformation programmes on time and to budget. Strong competition and significant bonuses have also encouraged “sales enthusiasm” with sale forces sometimes over stating their capabilities in the form of “vapourware” - the selling features and capabilities that do not yet exist.

What are the Risks?	
<ul style="list-style-type: none"> • Buy vapourware products and services yet to be developed • Poor project management, cost over-runs, long implementation delays • Limited delivery of application features 	<ul style="list-style-type: none"> • Cost saving targets not achieved • Slow development of new features and functionality • Long term lock-in and unhappy relationships

Table 4: Key Outsourcing Risks

So how can multi-country banks mitigate the significant risks they face when considering their card processing options? Eight simple rules are suggested, as follows.

First, thoroughly research the EU card processing sector and its capabilities well before issuing a RFP. Only select to bid those with multi-country experience and capabilities. Talk to users, understand their migration experience and the quality of development and implementation project management delivered. Clearly establish processor’s EU (not US) operational capabilities and the services they currently offer for card issuing, acquiring, ATM and domestic and ICS processing.

Second, before building requirements ensure strong commitment to the outsourcing concept across the group, define very clearly the business, governance and operational model needed to support development and the eventual centralised solution. Ensure the bank retains control of development. Ascertain those processes that can be centralised and those that should remain supported in each country market.

Third, replace poor processes and governance before migrating. An internal mess can result in an outsourced mess. Also build and implement a plan to encourage all countries to

migrate to common products and features and thus minimise any tailored developments. Fully understand the scope of product parameters software vendors and card processors offer. Do not be over ambitious and limit requirements to “must haves”. In RFP’s, ask for initial deliverables that are as close to vanilla product as possible.

Fourth, plan carefully, spread your risks, analyse your options and avoid a total commitment to a single vendor. Consider separate providers for credit card issuer processing and a different supplier for acquiring or ATMs. Remember the importance of retaining an internal capability and the ownership of manufacturing IP. Also think carefully about outsourcing processing to vendors who have little experience in the complexities of domestic debit. Last, avoid transferring excessive risk to vendors and pay for development upfront.

1. Research sector capabilities to develop/deliver multi-country solutions	5. Honest communications and straight talking
2. Define development, governance and operational model for service delivery	6. Ensure internal competing bids to compare with external
3. Sort out internal problems and harmonise products ahead of centralisation	7. Hire systems integrators to help with project management
4. Dual source external providers	8. Think exit strategy from the onset

Table 5: Eight Key Factors to Reduce Outsourcing Risk

Fifth, ensure RFPs have a strong emphasis on honest communications by both parties, joint risk assessment and detailed investigations into the vendor’s capabilities to develop, migrate and implement. In addition, apply great rigour to checking RFP responses to ensure the services described exist, have more than one live user and can be delivered within Europe. Scepticism is essential, as is straight talking by both sides.

Sixth, do not rely solely on an external solution. Ensure that internal bids are received from larger country operations who have potential to be developed into a group processing hub.

Seventh, identify and obtain bids from systems integrators who can provide strong project management teams able to reduce the risk of over spend and slippage, as well as manage complex migration programmes.

Eighth, think exit strategy from the onset. Have separate contracts for development and operational services. Ensure you build a framework that will allow separation should a divorce become necessary.

So to summarise. Multi-country banks need to lower their expectations from the EU's card processing sector. They also need to be very sensitive to risk when they develop their plans to centralise card processing. Such projects are highly complex and few in the commercial card processing sector offer complete solutions. Processors are more comfortable delivering standard solutions and, for historical reasons, are poorly equipped with the skills and experience to manage large scale bespoke projects. Banks should recognise that they may pass on substantial delivery risks to processors who are not fully aware of the consequences and who may often over estimate their capabilities. Processors need to re-evaluate their responses to supply services, raise the quality of their submissions, improve their risk assessment and sales training processes.

To conclude there are few silver bullet solutions to enable the low risk building of a single bank out of many! So take great care as you make your decisions and ensure you have a clear risk mitigation strategy.

About PSE Consulting

PSE Consulting is a leading European payment business and technology consulting organisation. The company was founded in 1991 by Peter Jones and operates from offices in London.

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