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Payments to Developing Countries: Complex, Not Impossible

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Agenda

- Global Market Trends and Implications for Corporations
- A Look at Payment Flows to Developing Nations
- Examples of Payment Flows
- Infrastructure/Tax and Legal Considerations
- Cost Considerations
- Banking Relationships and Risk Management Considerations
- Selecting the Right Partner
- Case Study: Intel
- Case Study: Google
- Key Takeaways

Global Market Trends and Implications for Corporations

Key Market Trends

Globalization

- Despite slow economic recovery, international trade remains an important growth engine for corporations
- Continued outsourcing of services to international locations with supplier and vendor networks located around the world
- Global mobility and migration are on the rise with customers employees and retirees reaching around the globe

Macro Economic

- Global economic recession
- Continued FX volatility, and declining interest rates
- Tightening credit markets

Technology

- Increasing electronification of flows
- Continuous evolution of payment methods - credit to debit to prepaid to virtual

Regulatory / Infrastructure

- Increased and enhanced regulatory conditions governing the transference of funds - IAT
- Transnational payment systems and government-led initiatives and mandates are increasing – SEPA, IPFA, UK Faster Payments

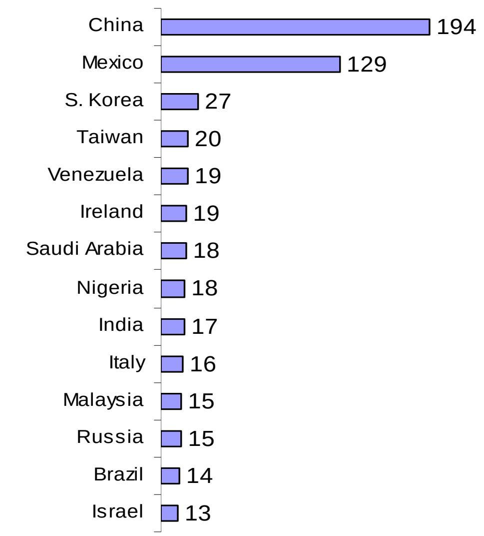
Implications for Corporations

- Higher volume of cross-border payments to customers, vendors, employees and retirees
- Increased exploration around less costly ways of making payments
- Increased importance to improve working capital management and unlock trapped liquidity
- Continued drive towards greater automation
- Greater drive and focus towards internal efficiencies

A Look at Payment flows to Developing Nations

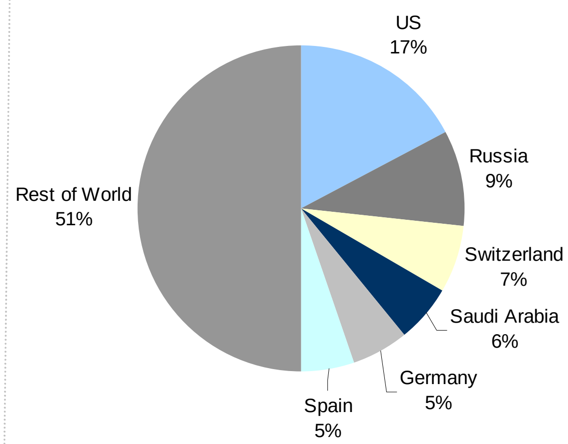
The 2010 US Imports for goods and services reflect significant origination from developing nations. In 2009, cross-border person-to-person remittance flows totaled $420 B with $317 B sent to developing countries

US Imports by Origin Country



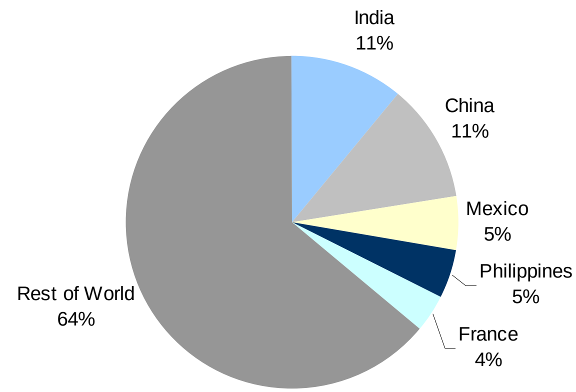
All figures in $ Billions. *Other countries account for $538 B

Top Remittance Origination Countries (% of total flows)



Source: World Bank

Top Remittance Destination Countries (% of total flows)



Source: World Bank

Trends

- US imports* grew from $1.45 T to $1.95 T from 2000 to 2009, resulting in increased demand for cross border payments
- Some of these countries are still developing their payment infrastructure to deal with cross border payments

Remitters

- US the top origination country, with almost twice the remittance outflows than the next largest country, Russia
- Un-banked and under-banked segments are the largest users of remittances, although banked users are growing

Beneficiaries

- India, China and Mexico are the leading recipients of remittance flows, followed by Philippines
- Remittances account for a significant % of GDP in poorer countries like Haiti, where they account for ~20% of GDP

* Source : BEA.gov

Examples of Payment Flows

Payor		Beneficiary
Corporations	Corporations source from global network of vendors / suppliers / Applications (Apps) developers as a means to lower cost	Vendors / Suppliers / Developers
Corporations / Pension Administrators	More retirees choosing to live in remote locations during their retirement years	Retirees
Non-Governmental Organizations	Developing nations are important destinations for humanitarian aid and fieldwork	Grant, Aid Recipients/ Volunteers
Immigrant Labor	Global remittances continue to rise with volume expected to total nearly half a trillion by 2011	Family Members
Insurers	Rising number of patients seeking care in developing countries as cost of healthcare rises in developed countries	Providers

Considerations For Successful Payment Delivery

Appropriate due diligence is required to manage Infrastructure, Cost, Banking Relationships and Risk Management Considerations before initiating Payments to Developing Economies

Infrastructure / Tax and Legal requirements

- Market practices and requirements
- Technology and scalability
- Extensive legal requirements compared to major currencies

Costs

- Foreign exchange costs related to tertiary currencies
- Higher lifting fees as a result of deductions from correspondent banks

Banking Relationships

- Maintain local currency accounts
- Manage multiple banking relationships
- Multiple reconciliations

Risk Management

- Manage FX risk
- Manage compliance risk
- Manage return item risk

Infrastructure/Tax and Legal Considerations

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Infrastructure / Tax and Legal requirements

- Extensive legal requirements compared to major currencies

A Few Examples:

KOREA : Payment Documentation Requirements

- $1,000 and under – neither call nor documents required from Beneficiary
- $1,000~$20,000 – no evidential documents required. However, purpose code and vendor ID are required which could result in need to contact Beneficiary
- $20,000 and above – Purpose code, vendor ID and documentation required. The payout bank must obtain a copy of the invoice (usually via fax) from the beneficiary each time. The invoice should contain the following information: payer, vendor name, itemized payment details with total amount due

INDONESIA : Payment Documentation Requirements

- All payments must include a detailed reason
- Payments above IDR 100 MM (approx $ 11 M) require additional documentation such as invoices from the payment originator. These documents are reviewed "in-country" before a local bank can execute the payment

- It is essential that the receiving bank has sufficient information and documentation to execute on the payment. Your banking partner should have the means to **Acquire**, **Validate** and **Transmit** this information
- **Global footprint** of your banking partner becomes highly relevant to ensure adequate awareness of such requirements and improved visibility over payment status through the entire delivery chain

Infrastructure/Tax and Legal Considerations… Continued

Infrastructure / Tax and Legal requirements

- Market practices and requirements
- Technology and scalability

A Few Examples :

INDIA : Local Clearing Requirements

- The fate of the payment depends on use of the local clearing code IFSC
- If Beneficiary Bank is on the local clearing network, payment will be distributed within the country electronically provided that the IFSC code is present
- If IFSC code is not available or if the receiving bank is not a direct participant into the local clearing environment, the payment is distributed by local bank through a Bank Draft which is then sent by local mail to the beneficiary bank
- Payments through the draft method could take almost 5 to 10 days for credit to beneficiary

Local Clearing Requirements for other countries

- Payments into **Russia** need a VO code from an officially published list of such codes
- Payments into **Thailand** require a purpose code from an officially published list of such codes
- Payments into **Kazakhstan** require a Single Payment Classification code and a Tax ID number. Tax related payments also require a Budget code

- It is critical for your banking partner to have **connections into various domestic clearing systems** such as RTGS or NEFT for India. Without these connections, payments could take much longer than expected and result in service issues (e.g. draft lost in mail)
- Also, **upfront validation** of such detailed requirements across countries by your bank takes away downstream service issues.

Cost Considerations

Costs

- Foreign exchange costs related to currencies
- Higher lifting fees as a result of deductions from correspondent banks

An Example :

TAIWAN : FX Booking Considerations and other Costs

- FX contracts cannot be booked till requisite local requirements are fulfilled. This creates a latency between the time payment is initiated and when the underlying FX contract can be booked. This also exposes originator to FX volatility
- All payments go through a confirmation requiring "Advice of Inward Remittance" to the beneficiary bank and getting requisite documentation as applicable . Thus local operational costs are incurred to arrange for such confirmations
- Downstream banks in the country can apply their own fees and deduct such charges from payments
- There is no standard fees across all banks and deductions could differ depending on local bank pricing. Coupled with FX volatility related spreads and the operational costs, the overall cost for payments to Taiwan can be very high

- FX volatility costs can be minimized by a **efficient local in-house delivery** process that reduces latency and exposure. Such efficiency can be achieved by keeping confirmation processes within the preferred local branch of your banking service provider
- The use of a **preferred local branch** also allows for "all in" costs to be upfront determined and applied to you instead of incurring hidden costs through deduction from beneficiary payments

Banking Relationships & Risk Management Considerations

Banking Relationships

- Maintain local currency accounts
- Manage multiple banking relationships
- Multiple reconciliations

Risk Management

- Manage FX risk
- Manage compliance risk
- Manage return item risk

Need for reducing Banking Relationships

- It is preferable to use a single account funding through your Banking Partner instead of various in-country accounts which require separate reconciliation and account management costs
- Some countries have restrictive regulations governing use of in-country accounts by non residents
- Many developing countries have non-liquid currencies which cannot be easily procured. Thus the banking partner should have access to all these FX markets else you will need to manage multiple counterparties and associated risk
- Comprehensive awareness of local requirements required to ensure compliance with a host of dynamic regulations
- Better visibility on payment flows and partners in delivery chain to ensure issues/investigations are dealt with efficiently and returns can be processed in a timely fashion
- Ability to deploy country specific solutions which capitalize on innovative distribution mechanisms that keep surfacing in developing countries

- An in-country account solution where originators open accounts in each country they want to deliver payments, does not support a very large distribution footprint as it substantially increases overheads
- Multiple FX providers, multiple local bank partners and fragmented delivery process increase costs, complexity and reduce visibility over payments. These should be replaced with a **Banking Partner who can provide consolidated services** through its own capabilities

Banking Relationships & Risk Management Considerations...Continued

Banking Relationships

- Maintain local currency accounts
- Manage multiple banking relationships
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Risk Management

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Are developed countries easy ?

- Some countries pose unique challenges. For example Japan runs a dichotomous clearing environment. Domestic payments are cleared through ZENGIN and Cross Border payments are cleared through Gaitame.
- GAITAME also links into local Tax reporting & Central Bank reporting for Japan
- The complexity comes in due to use of Katakana language as the only acceptable language for Zengin clearing. Translation from English to Katakana doesn't yield results accurate enough for use in clearing systems.
- If you have a business presence in Japan and thus have both domestic payments as well as cross border payments for Japan, you might end up maintaining information in two different languages and two formats to meet payment needs for a same vendor/supplier/developer.
- Bank partners with advanced technologies might be able to create & host a beneficiary database for you and thus take the pain away from creating complex applications in your organization to deal with such scenarios

- The focus and attention on selecting a good banking partner for developing markets should not come at the cost of creating an additional banking relationship just for this purpose
- Payments into developed countries can be as complex as developing countries especially if you do not have adequate insight into the multiple options available on specific needs for your business

Selecting the Right Partner

Making cross-border to developing countries poses many unique challenges. Therefore, it is crucial to partner with a provider that ….

- has the **infrastructure and network** to meet your specific payment needs
- has **operational scale** in order to cut your operating costs and simplify your payment processes
- possesses **in-country knowledge** to understand the nuances of domestic clearing systems
- Is a **direct participant** in local markets and understands the complex rules, regulations and requirements that govern payments in those markets
- possesses a **strong culture of innovation** in order to meet your needs in the constantly evolving marketplace
- is **flexible and nimble** enough to succeed in an increasingly complex environment

Key questions to ask…

- Does the bank's network match your footprint?
- What options do they offer for competitive exchange rates for tertiary currencies?
- What type of payment methods do they offer?

Case Study: Intel

Customer Profile*

- Intel is the world's largest semiconductor chip maker, based on revenue. Intel develops advanced integrated digital technology products, primarily integrated circuits, for industries such as computing and communications. They have a presence in 51 countries spanning all the major regions of the world including The Americas, Asia, Europe and Africa

The Goal

- Reduce Payments cost by engaging one banking partner having Payments expertise in both emerging and developed economies

The Challenges

- Varying Payments needs in more than 40 countries
  - Payments to vendors
  - Intercompany Payments
  - Payments to partners and affiliates
- Lack of a transparency in the Payments process
  - Integrating Payment activity with various treasury management tools at Intel
- Making investment related Payments via SWIFT in different countries

The Solution

- Banking partner with significant payment expertise and multiple tools to manage International and Domestic Payments
- One banking Platform allowed Intel to integrate the Payment activity with their Treasury management tools and ERP system
- Standard procedures and tools to create and track transactions
- Engaged with banking partner to overcome technical challenges of local SWIFT requirements and integration with Treasury systems

* Source: Intel Website

Case Study: Google

Customer Profile

Google connects millions of people around the world with information every day. Headquartered in California, Google is a globally recognized name employing more than 20,000 people in 40 countries around the world including Americas, Europe and Asia

The Goal

- Reduce payment costs in EMEA by leveraging SEPA as preferred payment method

The Challenges

- High volume of payments made in Euro payment zone
  - Payments to vendors
  - Payments to employees
  - Payments to partners
  - Payments to Google subsidiaries
- Lack of data required for SEPA payments
- CBR requirements
- Integration with existing Google systems

The Solution

- Google engaged their banking partner to identify the population of SEPA capable payments
- The Bank's SEPA experts established standard data requirements
  - Example: aggregate payments into one file across SEPA region
- One platform/file enabled Google to make payments as desired
- Process was made transparent through:
  - Communication with internal payment partner (AP) for eliminating other payment types for SEPA region
  - Establishment of process to on-board all new vendors to SEPA payments only
  - Communication with vendors to identify type of payment sent

Key Takeaways

Flexibility is key as payments processing capabilities vary country to country

Be nimble in order to respond to evolving regulatory and infrastructure environment

Align payment method appropriately based on the demographics of the country

Choose the appropriate validation engine, whether in-house or third party provider

Perform rigorous testing by country and currency to ensure low rate of returns

Partner with a provider with the in-country expertise and knowledge in the developing areas to which you are sending payments

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