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Market Commentary

Revealing priorities in payments for financial institutions in 2021

Addressing the payments landscape became a hot topic in 2020 for financial institutions. The COVID-19 pandemic encouraged broad scale digital adoption as businesses moved to remote work environments, and consumers sought ways to manage money in a contactless society.

"Real-time payments are now available in forty countries, with more than half a dozen more ready to go live before 2023."

Deloitte, 2020

For most countries, regulation will set digital priorities

While the COVID-19 pandemic was a major driver for payment innovation in 2020, regulation is likely to set financial institution priorities in 2021 for most of the world. In Europe, for example, the Retail Payments Strategy (RPS) will lead payment innovation agendas, requiring financial institutions to support instant cross-border payments by the end of 2021, despite current interoperability between settlement and clearing mechanisms.

While interventionist regulation like RPS drives much of the world toward instant payments, the U.S. continues to lag behind. The Federal Reserve, which links nearly every financial institution, will not have a real-time payment service available until 2023 at the latest.

Meanwhile, The Clearing House Payments Co., LLC (TCH), owned by the country's biggest banks, has made more significant progress. TCH announced in September that its current connections to core processors could potentially bring online nearly seventy percent of U.S. deposit accounts, though reports of "patchy network coverage" persist.[1]

Looking ahead to 2021, we see a transformation in digital capabilities emerging as the rapid adoption of real-time payment capabilities accelerates the analogue to digital journey for financial institutions.

In the absence of regulatory pressure in the U.S., consumers are leading the charge on real-time payment adoption, promising to keep instant payment capabilities at the top of U.S. financial institutions' agendas throughout 2021.

Accelerating the analogue to digital journey

Even before the impacts of the COVID-19 pandemic were felt, real-time payments transaction volume was projected to increase from $734 million in 2019 to $4.2 billion by 2024 in the U.S. alone.[2] Now, as health and economic concerns continue to spur demand for contactless payment methods and instant access to cash, the real-time payments market continues to grow, saturated with a bevy of players.

In fact, real-time payments are now available in forty countries, with more than half a dozen more ready to go live before 2023, according to Deloitte.[3] In 2021, we anticipate that this well-defined market will inspire wide-spread digital transformation.

For one thing, real-time payments platforms are built on APIs. APIs offer a simple plug-and-play functionality where financial institutions easily connect to products and services.

With APIs in place to support real-time payments, banks and credit unions are free to connect other API-supported innovations, expanding the products and services available to consumer and business customers. In essence, the rapid adoption of real-time payments capabilities in 2020 will accelerate the change from analogue banking to digital in 2021.

State of the art technology like APIs also support better data access and advancements such as ISO 20022. ISO 20022 is a standard for exchanging electronic messages, allowing senders to include far more information with a payment than could previously be accommodated. Enhanced data supports more wide-spread automation of business AP processes, providing faster reconciliation and a decrease in days sale outstanding.

By migrating to the new standard, financial institutions will gain added efficiencies as well. For instance, the highly structured messaging format of ISO 20022 supports faster and more accurate machine reading, opening opportunities for automation.

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While SWIFT will not enable ISO 20022 messages on cross-border payments and cash reporting businesses until the end of 2022, many high value payment systems have already moved to the new standard, according to Accenture, including those in Japan, Switzerland and China. Several additional countries plan to adopt ISO 20022 over the next five years.

Trust in cloud adoption accelerates

A year ago, skepticism was widespread about cloud-based payment services. As we move into 2021, a growing acceptance has emerged. While countries continue to seek control over cloud location and security principles, on-premise demands related to software, hardware and management are falling by the wayside, in support of faster transformation strategies.

Cloud is infinitely accessible and adaptable, enabling financial institutions to access evergreen software that is always updated to current standards and regulatory requirements. Without the need to continuously bring on-premise systems and software up to speed, banks are free to focus budget and resources on more revenue-generating activities, such as customer acquisition efforts.

> ***"The widespread, sudden disruptions caused by the coronavirus have highlighted the value of having as agile and adaptable a cloud infrastructure as you can — especially as we are seeing companies around the world expedite investments in cloud to enable faster change in moments of uncertainty and disruption like we faced in 2020."***
>
> **Daniel Newman**
> Contributor to Forbes

In the Baker McKenzie Digital Transformation & Cloud Survey, financial institutions identified the top drivers of cloud adoption. Sixty-eight percent expect to mine greater operational efficiency, while half plan to open new revenue streams.[4]

Open banking supports agility and innovation

Both the adoption of cloud-based services and APIs will underpin the analogue to digital journey in 2021. As financial institutions continue to embrace the platform economy, they move from a position, where technology is fixed and integrated inside the financial institution to an agile stance, where innovation and transformation are easily attained.

Forward-thinking solution providers are already partnering with Fintechs in support of innovation, using APIs to offer plug-and-play adoption of third-party products to financial institutions. The simple functionality opens opportunities for banks to adopt new products as necessary, including solutions that reduce payment risk and manage regulatory requirements.

APIs offer customer-facing advantages as well, enabling consumers and businesses to more securely integrate their world of financial management behind their bank. Currently, fifty-four percent of consumers utilize an outside app to manage money and payments, according to a Bankrate survey, but eighty percent did not realize that third-party providers store bank account usernames and passwords.[5]

Financial institutions can solve security issues like these in 2021 by offering similar payment services through simple plug-and-play adoption.

Overall, the rapid digital acceleration in 2020 has set the stage for the next chapter in the digital payments journey, allowing banks to more efficiently and effectively meet regulatory requirements and emerging market demands with innovative plug-and-play solutions.

For more information
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About Finastra

Finastra is building an open platform that accelerates collaboration and innovation in financial services, creating better experiences for people, businesses and communities. Supported by the broadest and deepest portfolio of financial services software, Finastra delivers this vitally important technology to financial institutions of all sizes across the globe, including 90 of the world's top100 banks. Our open architecture approach brings together a number of partners and innovators. Together we are leading the way in which applications are written, deployed and consumed in financial services to evolve with the changing needs of customers. Learn more at **finastra.com**

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