

FISERV PERSPECTIVE

Managing currency in an uncertain economy



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Not too long ago, it was common to hear people say, "I never carry cash." That may have been the case for many consumers as they readily swiped their plastic cards. The truth is that cash is the oldest and most universally accepted form of payment in the world. In fact, currency in circulation is on the rise globally. Economic factors are influencing consumer preferences for whether or not to use cash. High rates of unemployment and low economic confidence have made consumers budget-conscious. And, while consumers are still reaching for their cards, it may not be at the point of purchase, but rather to get cash from ATMs.

It's no wonder people love cash. Cash transactions are fast, convenient, anonymous and free when consumers use their own financial institutions' ATMs. But while accessing cash may be free for consumers, making sure there is enough cash at the ATM, branch or vault when customers demand it is by no means free for financial institutions or other entities in the cash supply chain. These organisations face the challenges of meeting constant changes in customer cash demand, while minimising cost exposure associated with staff, transportation, insurance, security and clearing. Increasing regulatory demands and tighter recirculation policies will also force banks to do more with less. Those without a cash management strategy will be left holding the bill, and probably a hefty one.

Cash is cheap, so why worry about cash management?

People typically get cash through the ATM. When customers attempt to withdraw cash and see the dreaded 'Out of Service' message, they are unhappy. Financial institutions need to ensure high levels of cash availability to avoid the risk of negatively impacting the customer experience and pushing them one step closer to the competition next door.

But stockpiling too much cash means higher cash balances and costs. After all, idle cash is a non-earning asset and even the slightest cash reduction can potentially free up capital for greater leverage. The cost and impact on profitability can be staggering, especially in cash-intensive countries with high or fluctuating interest rates. Increasing fuel and transportation costs, tighter central bank control and sourcing restrictions, and the need to optimise the currency supply chain become immensely obvious and raise the question: "Is cash really cheap?"

How are new regulations impacting currency management?

Central banks are no longer in the business of providing free cash services and will continue to shift cash processing costs to financial institutions. This is happening all over the world in the form of increasing fees and regulations of recirculation policies. The growing levels of currency in circulation are forcing central banks to take the necessary steps to maintain banknote integrity and availability of denominations to meet public demand. As central banks are no longer an unlimited source of funds, financial institutions must find better ways to manage and recycle currency supplies. When evaluating transportation routes and capacity constraints, the need for optimisation in the currency supply chain becomes even more evident. Just-in-time cash forecasting models are used in Europe, Latin America, and South Africa, but banks need to consider these constraints to effectively optimise supply and demand at the lowest cost possible.

How do prepaid cards and the unbanked complicate cash management?

Prepaid debit cards are another growing phenomenon. Student loans and government benefits such as unemployment and federal aid are being paid out with prepaid debit cards that can be used to access cash. Cash suppliers are reeling from

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costly outages and scrambling as ATMs are being hit with unprecedented withdrawal amounts. With high unemployment and massive deficits looming over the economy, this trend is expected to rise as businesses and governments turn to paperless technologies to tighten their belts and minimise costs.

Financial institutions must develop an ATM strategy that addresses the increasing popularity of prepaid debit cards. Rather than pushing cash levels up across the network, banks need to focus on pockets of high prepaid debit card distribution and usage. Identifying and segmenting the unbanked or under-banked offers opportunities to reach potential new customers and generate much-needed new revenue.

What currency management solutions and forecasting methodologies can help?

Financial institutions are looking for methods to streamline and automate the cash management process. Some are turning to automated cash forecasting software to optimise cash levels by balancing holding costs against transportation costs and constraints.

Many cash forecasting tools rely on the assumption that past experiences are replicated in the future. Linear regression forecasting models in the market today rely on this assumption to identify sequential repeating patterns of usage or use sophisticated averages to predict future cash demand. This may work well in some instances, but the way people save and spend is influenced by not only past experiences but also current events.

Using non-linear methods, which employ forward-looking reasoning based on past experience and factors that have influenced cash requirements, is a better way to forecast the need for cash. The goal of cash forecasting is to identify the complex relationships between the amount of deposits and withdrawals, current events and point-in-time demand, including day-of-week, day-of-month and week-of-month.

One of the barriers to accurate cash forecasting is the fact that cash data can be very dirty, containing errors and discontinuous extreme values. A truly robust, non-linear and highly dynamic forecasting engine can overcome this issue and recognise complex customer cash usage patterns and make sense of them to confidently predict future demand.

How should financial institutions develop a cash management strategy?

Banks need to clearly define their cash management goals, considering internal operational implications and external factors driving customer demand and cash handling costs. Software solutions can automate the cash forecasting, optimisation and management process to minimise cost and increase efficiency. But software alone can't solve all the problems. Implementing a successful cash management strategy requires direction from executive management, retail buy-in, and cooperation from internal and external stakeholders. Successful management of cash and currency requires:

- **People and processes:** Organisations should work to break down internal barriers and define roles and processes to centrally manage cash for greater control and visibility across the enterprise.
- **Performance metrics and reporting:** Measurements help organisations assess cash management progress against plan. Tools, such as business analytics, empower an organisation to quickly identify and turn around problem areas.
- **Technology, integration and scalability:** Technology solutions need to be flexible to integrate into internal and external systems and robust to support future growth. Software as a service, for example, offers unique opportunities for financial institutions to quickly implement powerful cash management solutions without shelling out capital investments, and for saving on internal IT costs.

What's the reward?

Cash is a big part of our society and these uncertain economic times are influencing both supply and demand. Managing and maintaining the right amount of cash to meet ever-changing customer needs is not cheap, and getting it right directly impacts the bottom line. Reduction in excess cash inventories minimises cash handling costs across the board, freeing up capital and putting what would otherwise be non-earning assets to work. Getting it right also leads to higher cash availability, greater customer satisfaction, and maximised surcharge revenue. As financial institutions are forces with increased capital requirements and fee revenues are squeezed tighter, it is imperative to find cost-saving and revenue-generating opportunities. ■



Increased capital requirements and squeezed fee revenues make it imperative for banks to find cost-saving and revenue generating opportunities

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