

Inhouse or Outsourced Netting?

by EuroNetting Inc.

When it comes to setting up your netting system, one of the principal choices is whether to run the netting system in-house, or to outsource it to a bank or other provider. These two alternatives can each be a perfectly valid choice for different companies with different needs and resources. Here are some of the factors to consider:

Available manpower: running a netting system in-house certainly means you must have a number of man-days available each month to manage the netting center functions, but exactly how many? The answer is it depends on the number of participants you will be administering, how their netting data will get into the netting database (file transfer or remote entry?), and what other specialized functions such as hedging you will be incorporating into your netting procedure, however our many clients appear to average about 2 to 3 man-days per month at the netting center, split across a number of days within each month.

But does this manpower need evaporate if you choose to outsource the netting center function? Not really - you will still be required to review and approve preliminary netting results and of course you will be the one initiating changes in the static data used by the netting system such as participant lists, users and privileges, and settlement instructions. So you will very likely still be involved in the monthly process to a greater extent than you might expect - even more now that a web-based service makes it just as easy for you to make changes directly in the static tables without intervention from the outsourcing entity.

Cost: It's not always easy to compare in-house and outsourced netting costs. Not only is the explicit fee charged by an outsourcer often higher than the annual license cost for a service such as EuroNetting, but outsourced services generally include another cost that is not so apparent: outsourcers typically charge a built-in foreign exchange spread on the netting FX trades to earn the majority of their income. While this is an appropriate way for the outsourcer to recover its costs, you may be able to execute your netting trades at better rates by keeping the netting function in-house. Netting FX trade volumes have generally contracted with the Euro having removed much of FX volume from intra-European trade, and with FX spreads generally diminishing due to improved rate visibility, some bank outsourcers have found it necessary to either drop unprofitable clients, or raise the explicit outsourcing fees to compensate for the lost FX revenue.

Other outsourced treasury functions: If your company already outsources other treasury functions (for example via an IFSC) it would make perfect sense to hand over the netting function to the same provider, since the netting will very likely be integrated with other functions. But if netting is the only service being outsourced, there might not be much benefit.

Complexity: This can work both ways. Some of our most complex netting implementations are run very efficiently in-house by our clients, because they have taken the time to optimize their netting procedure and they make extensive use of automated data interfaces. These clients would gain nothing by handing over their carefully-tailored netting system to another party.

On the other hand a netting system involving hundreds of participants using an email-based remote entry process can be tough to manage, simply because it requires tracking the data input from so many people - it may be better to give this job over to an outsourcer who has the dedicated resources to deal with so many participants without the distractions you would have from your other treasury management obligations. Even so, this situation could be much more easily handled by an Internet-based system such as EuroNetting, that places the data entry responsibility directly into the hands of the participants. Without the need to track and import large numbers of small data files received by email, the data entry phase is much simpler to handle even for large numbers of participants.

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October 2007

