GLOBAL CASH REPORT

DEALING WITH RISING INTEREST RATES

THE END OF THE CASH OFFICE

CAN CASH STRIKE BACK?

CASH UNDER THREAT

It's time to get your head out of the sand

EDITORIAL

Cash is being assailed from all sides. Card networks looking to extend their dominance into low value payments, technology companies trying to disrupt the payments industry and banks trying to reduce costs of 'non-core' activities. All share a common goal to eradicate cash as a viable payments instrument. Governments and central banks appear, at best, ambivalent to these attacks and at worst, complicit, as they blame cash for fueling tax avoidance, money laundering and a whole range of other social ills.

The response of many in the cash industry has been to bury their heads in the sand. I lose track of the amount of "cash is king" claims and disparaging comments about the integrity and desirability of the technology behind cash alternatives. I fear that this approach is detracting from the real need for the industry to face the truth; cash is in peril.

Yes, I know that international circulation figures have shown consistently rising volumes of cash since the financial crisis. However, look underneath these figures and a different story starts to emerge; Cash transactions in many countries are falling, even as cash in circulation rises. The difference is down to hoarding due to a number of factors, some long term (for example, demographics) but others short term and easily reversible (low interest rates).

In March this year, card transaction volumes will overtake cash transactions for the first time ever in the UK - a leading payments market. Contactless payments are eating into cash volumes and values, especially at low value merchant outlets, such as quick service restaurants (QSRs), where cash takings are falling year on year. Furthermore, this process is accelerating as the distribution of contactless cards increases and the availability of contactless-ready terminals grows.

As cash values drop, along with transaction volumes, there is a need for the industry to adapt. Currently, too many cash industry costs are fixed, meaning that cash will become more and more expensive compared to alternatives. Investment in technology to improve productivity is patchy to say the least, with vaults potentially grasping the issue but merchant outlets still skeptical of the investment. This creates a vicious cycle for merchants in choosing which payment methods to accept. The management of cash throughout the industry is too commoditized, often using spreadsheets or forecasting software that hasn't been properly upgraded for decades.

In this issue we highlight how a number of forward thinking organizations are gaining competitive advantage by investing time and money in techniques to increase flexibility, streamline processes and improve productivity. It is imperative that the cash supply industry wakes up and acts to encourage innovation in the retail sector. These techniques deliver competitive advantage under normal circumstances, but in a declining cash market will ensure the survival of the fittest.

Best wishes,

Brendan Doyle
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IN THIS ISSUE

THE RISING THREAT TO CASH

The threat on cash is real - it's time to accept it.

Believe it or not, the cash industry has been basking in the good years recently. Much of this has been powered by ever increasing volumes of notes in circulation. Indeed, many western economies have been experiencing volume increases of 6% or more per year **(see figure 1 – US Dollars in circulation)**. Capacity has risen to meet this demand. For example, by 2012 the number of ATMs in EMEA had risen to 760,000. Speaking at the recent ICCOS conference in Milan, Ron Delnevo, Executive Director for the ATM Industry Association (ATMIA) Europe stated "cash is one of the most successful technologies ever invented, being history's longest-lasting, most resilient form of money".

However, all is not as it would seem. Look 5 years ahead and there is evidence to suggest that this rise in cash volumes is a temporary phenomenon and worse still, that other, underlying, structural changes are coming together to create a systemic shock. In this changed landscape, a smaller, consolidated industry will emerge and the reaction of key players today will determine how the industry will look in 2020. Four fundamental factors are influencing cash demand; interest rates, alternative payments, demographics and political pressure.

1. Low interest rates have acted like a steroid on cash volumes, but this will unwind when the cycle turns.

Interestingly, although cash circulation volumes are rising at 6%, transaction values & volumes are falling year on year **(see figure 1: The conflicting trends of cash circulation and usage in the United States)**. The difference may be put down to cash hoarding. In the Europe alone, the amount of cash hoarded is now estimated at €400bn, some 40% of the cash in circulation and almost equivalent to the GDP of Austria. There may be a number of factors behind this, but the main driver is seen as low interest rates. With some commercial banks now charging nil or even negative interest rates, there is little economic incentive to keep money in bank accounts. It is therefore reasonable to conclude that once inflation and interest rates turn, some of this hoarding will unwind and the result will be a significant reduction of cash in circulation with impacts on ATM and bank branch withdrawals.

2. The rise in alternative payments is reducing the appetite for cash from consumers and merchants alike.

Card networks such as Visa and MasterCard have long aimed to replace cash as the primary means of payment. Retailers have traditionally supported cash as a low cost option. However recent regulatory changes have tilted the balance towards cards. The Durbin Amendment in the US has reduced card interchange fees paid by retailers by $10 billion a year and perhaps the boldest move yet is forthcoming European legislation designed to make the cost of accepting payment by card or cash, neutral. **(see figure 2: Current average transaction cost to a UK retailer by payment instrument)**.

Figure 1: The conflicting trends of cash circulation and usage in the United States.

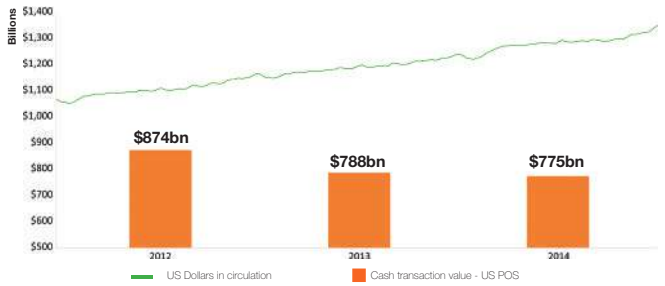

Figure 1: The conflicting trends of cash circulation and usage in the United States. While cash circulation has increased year on year, cash transacted at US POS has decreased. Both trends are set to continue on their current path under the existing conditions, however the extent of cash circulation's artificial high will become clearer following interest rate rises.

Sources: US Federal Reserve; Javelin Strategy & Research

Figure 2: Current average transaction cost to a UK retailer by payment instrument.

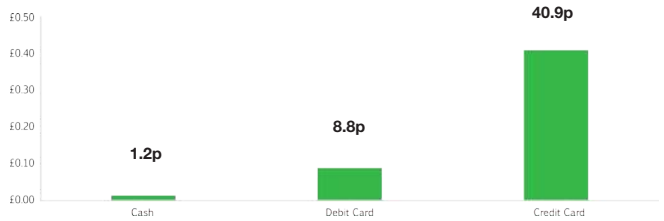

Figure 2: Average transaction cost to a UK retailer by payment instrument. For UK retailers, cards remain materially more expensive for a retailer to handle than cash, with the average credit card transaction costing the retailer over 3000% more. Future European legislation and regulation from other regions appear to indicate that this differential will reduce increasing the desirability of cards for retailers and potentially harming sentiment for cash.

Source: BRC - British Retail Consortium

One barrier against card payments has traditionally been low value transactions. Despite inroads elsewhere, cash has remained the primary payment method of choice for transactions under $25. Card schemes have been working hard to find a viable alternative and with the roll out of contactless cards, using NFC technology, they appear to have finally succeeded. By setting the cost of acceptance far lower than standard cards and by demonstrating a speedier, more efficient payment process at the point of sale, the card networks are making inroads at last. In the UK there has been an explosion in the issuance of contactless cards and transaction volumes are rising exponentially **(see figure 3: Issuance and transaction volume of contactless debit and credit cards in the UK)**. Many merchants with a low average transaction value, such as quick service restaurants, are seeing volumes rise to as much as 40% of total payment value. While much of this is cannibalization of existing card payments, there is a discernible reduction in cash volumes despite overall sales growth. We expect this growth to continue.

Figure 3: Issuance and transaction volume of contactless debit and credit cards in the UK (2008-2014)

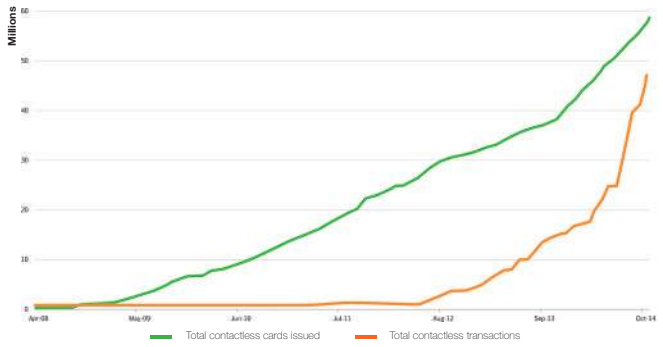

Figure 3: Issuance and transaction volume of contactless cards in the UK. Since the introduction of contactless cards in the UK in 2008, issuance has steadily increased to 58 million cards by December 2014. Monthly transaction volumes did not experience the same levels of growth initally, however since 2012 growth has been exponential with over 45 million transactions by December 2014.

Source: The UK Cards Association

Merchants remain keen to cut back-office costs and a growing number are already making the option to pay by cash more difficult. For example, international fast food chains, long dominated by cash transactions, are now introducing ordering terminals that don't accept cash at all. In any case, growth in non-cash transaction volumes have accelerated to more than 10% per year in recent years as consumers move towards the web and contactless and, with innovations such as Apple Pay & Zapp on the horizon, this trend will continue. By one means or another, the retail sector, once a powerful advocate for cash, will first turn neutral, and then negative towards cash and options to pay by cash will inevitably reduce, impacting demand.

3. Demographic changes may see cash reduced to the "margins" of society.

When former Australia Reserve Bank official, Peter Mair, criticized senior citizens for hoarding cash, Michael O'Neill, CEO of National Seniors Australia agreed that senior citizens "still have an attachment to the folding stuff". The inference is that this is not the case with younger generations. So far, there is little statistical evidence to back these anecdotal claims and restrictions on the use of certain alternative payment types by younger people have acted as a barrier to adoption. These barriers are now being overcome **(see above section, 'The rise of alternative payments...')** and there is a fear that cash is becoming ever more concentrated in older, poorer demographic groups, with weaker political and economic power.

4. Increasing political attacks on cash are encouraging limitations on the supply and acceptance of cash.

In some circles, cash is seen as a major villain in the current tax avoidance/evasion debates across many western economies. There is no doubt that this is having an effect on policy and from a traditionally neutral position, central banks are taking an increasingly negative stance towards cash. This is creating an easier environment for banks to limit supply and move payments from a costly, commoditized, anonymized paper based system that they find difficult to control to low cost, high margin, electronic systems with appetizing opportunities to track and manipulate customer behavior. In the Netherlands for example, Banks have reduced the number of ATMs by 15% over the last 5 years. The Dutch central bank has encouraged increased consolidation despite the impact on costs of cash for merchants. With reduced supply and rising costs, it is not surprising to see that cash transactions fell by 14% in the Netherlands in the three years to 2013. We have seen in sections 2 & 3 above, how powerful interest groups such as retailers have a reduced interest in promoting cash. If central banks, retailers and the young continue to abandon cash, while Banks and networks continue to heavily promote alternatives, then an accelerated decline in cash volumes can be expected.

Author

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BOTTOM LINE

Each of the four factors will have a differential impact over time but taken together they represent the most dangerous threat to cash yet. There is no doubt that cash volumes are being impacted already and this trend is set to continue and gain pace.

Author

Tracy Jeffries, VP & Head of ATMS
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CASH PROCESSING

A technological revolution has produced radical increases in productivity but end users still aren't benefiting.

The days when cash centers consisted of masses of cashiers sitting with desktop machines spending all day counting cash have long gone. The cash processing industry has been through a transformation over the last decade and the resultant productivity improvements have led to notes being counted 100x faster. The three main drivers of this revolution have been economies of scale, regulation and significant advancements in technology.

This industrialization of cash processing has seen a rationalization in cash centers in many developed economies. This has allowed greater concentration on efficiency and an ability to deal with much larger volumes of cash throughout. This concentration has been aided by a phenomenal improvement in cash processing technology and robotics with fewer, larger machines counting evermore cash more accurately. Globally, staff employed in cash centers has dropped by over 50% since 2000 and efficiency has increased by 400%.

Japan and China are leading the way towards people-less cash centers, with a greater automation across all processes, whereas traditional models would see 67% of employees in a typical cash center allocated to note processing.

Central banks are encouraging concentration by raising barriers to entry through increased regulation. In the UK, The Bank of England Note Circulation Scheme (NCS) is notoriously difficult to join as ever-increasing regulations are discouraging new entrants and leading to re-evaluation amongst current participants. Hence, a market that once had 11 competitors is now dominated by 2 processors, Vaultex and G4S. **(See figure 1: UK cash processing market)**

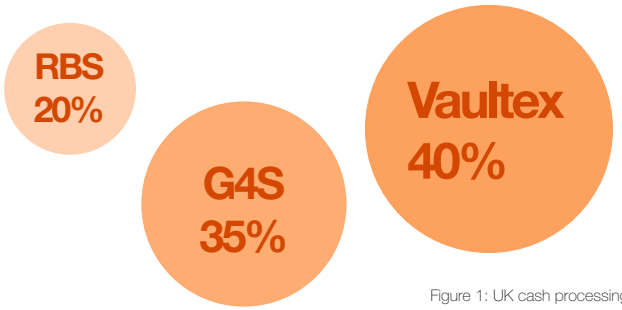


Figure 1: UK cash processing market

In the Netherlands, the country's three largest banks (with a combined market share of >90%) created Geldservice Nederland (GSN), a cash processing logistics business, with the support of the central bank of the Netherlands.

For retailers, merchants, retail banks & ATM deployers, these developments should be good news. The increasing productivity in the industry has reignited interest in outsourcing cash counting to the supply chain. Eliminating the need to count cash repetitively. New methods mean that outsourced cash processing can be reconciled back to the checkout – a stumbling block that, historically always undermined the case. Furthermore, outsourcing allows retail finance to remove fixed costs so that the cost of cash becomes variable with levels of cash usage.

However, the trend towards concentration in the industry presents potential threats. There is no doubt that many of the benefits achieved over the last decade have not been passed onto retailers, merchants & ATM deployers but rather to enhance profitability in the supply chain. If increasing concentration is allowed to continue, there is no reason to think that this will change.

BOTTOM LINE

Efficiencies in the cash processing industry will continue as the concept of a people-less cash center becomes more prevalent. The improvements made so far have transformed the way cash is processed and with it, the margins of processors. However subsequent benefits have yet to be passed down the supply chain to end users.

THE ARMORED TRANSPORT INDUSTRY

New thinking is successfully challenging a conservative industry.

As the nervous system of the cash industry, the Armored Transport (AT) sector is under no illusion about the consequences of a diminishing cash environment. Pressured margins **(figure 1 – UK Armored Transport industry average operating margin)** have already led to a scramble for additional revenue streams, cost reductions and a new, lean philosophy.

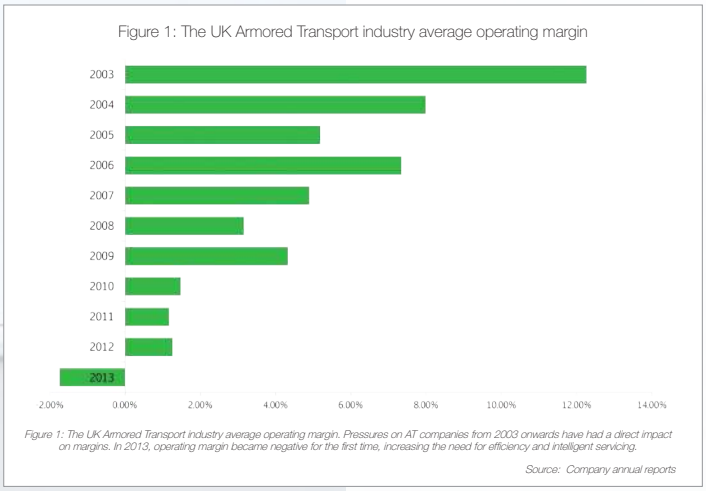
Driving efficiencies

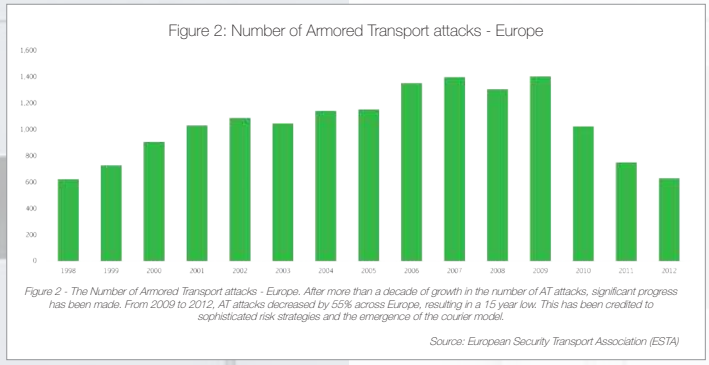
With interest rates at record lows, the demand for AT services has plummeted as the trade-off between the cost of moving and holding cash has shifted in favor of the latter. For example, average weekly scheduled services for major UK retailers have halved since 2005 and in the US, a number of AT companies have put limits on the number of days allowed between ATM replenishments to artificially maintain schedules and limit the impact on revenues. This drop in demand has been compounded by reductions in main street sites as many retailers and banks reduce their networks.

The resultant excess capacity in the industry has brought significant spotlight on high fixed and operational cost bases. In response, AT companies have taken action to reduce the variable operational costs of their businesses by seeking efficiency gains and investing in technology. New, more flexible labor contracts have opened up opportunities to extend hours and reduce crew levels on vans. With labor traditionally comprising 50% of costs, this has had a major impact. A movement away from armor and towards technology has seen reductions of 30% or more in the capital cost of vans while improving security. This is part of a more sophisticated risk strategy that has seen major reductions in attacks. **(See figure 2 – Armored Transport attacks in Europe)**.

Transitioning from Security Firm to Cash Courier

New technology is finally allowing the industry to move away from a security firm, hard armor and "guns" mind-set towards a modernized "cash courier" concept. Across Europe, several AT companies are transitioning by diverting capital away from the vehicle shell and towards more advanced technology in cassettes and casings. Hence, traditional armored trucks are being swapped for more standardized vans loaded with storage racks. The security aspects of drivers' roles (now often the sole person aboard vehicles) have also reduced with access to cases prohibited and responsibility for reconciliation shifted to the cash center. The courier model has had a significant impact on efficiency and profitability, with Scandinavia leading the evolution. The model is now standard across Sweden, Denmark and Finland where few vehicles leave depots with more than one person aboard.





New income streams

There has been a drive to decommoditize the industry in order to build profit and the search for alternative, higher-margin revenue streams has been a priority. AT companies have vertically integrated into cash processing services and encouraged banks to outsource vaults. This has worked particularly well where central banks have introduced note circulation schemes that encourage economies of scale, such as in the UK and South Africa. Benefits from this have also been achieved in the commercial sector. In 2014, Bank of America outsourced all its vaults to GardaWorld in a $1.4 billion, 12 year deal.

End-to-end services involving the use of cash office technology has proved particularly popular in the US quick service industry, where cash counting safes that provide better reconciliation, save time and provide quicker value can be rented from the AT provider by the merchant. This option is starting to gain traction in the United States, with Loomis currently renting nearly 10,000 smart safes to US retailers and 100 financial institutions providing credit to the retailer for cash held in the safe.

As interest rates rise & the cost of technology falls, these solutions will become more viable for other merchant sectors. Innovative solutions see the AT provider involved further up the supply chain. In Spain for example, Prosegur is encouraging banks to outsource bank teller staffing to themselves. Concepts such as mobile cash offices are also being tested.

Meeting the challenge

Efficiencies created within traditional AT models and through the emergence of the courier model show that the industry is meeting the challenge and a turnaround has begun. In 2010, Loomis set a target to achieve a full-year operating margin of greater than 10% no later than 2014. In 2014 this was achieved for the first time with a margin of 10.1% due to a combination of cost cutting, extended service offering and the addition of tailored large-scale contracts. However, there is a long way to go as there remains a deeply conservative, security focused mindset in many traditional markets. For example, Italy may have recently halved the number of AT suppliers, but there are still 58 in operation.

> ***"So let's call it bank branch outsourcing, ATM, estate management... we have that capability and that's something we are going to be working on."***
>
> Ashley Almanza, CEO - G4S

BOTTOM LINE

The financial crisis forced the AT industry to make difficult structural changes. Innovative cost reduction strategies, investment in technology and a creative approach to the cash supply chain has produced a much leaner, flexible industry better able to cope with the challenges of falling cash demand.

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CASH UNDER THREAT

RETAIL CASH OPERATIONS

The traditional cash office is disappearing.

Traditional retailing has been transformed over the last decade. The rise of online shopping and the impact on the main street of the Great Recession has transformed the payment landscape for merchants. It is therefore not surprising to see the beginnings of a decline in cash transaction levels, a trend that is gathering pace as new technology comes to fruition and the cost of alternative payment methods begins to fall. Many retailers have high fixed costs associated with cash, meaning that the cost of cash payments will rise as volumes decline. To meet this threat, a number of merchants are following innovative strategies.

Outsourcing

While a number of major retailers outsourced cash counting to third parties in the late 1990's, the movement towards such 'prime count' solutions lost momentum due to poor service quality, high losses, challenges around reconciliation and rising prices. However, recent improvements in technology allowing speedy, automated, low cost reconciliation to checkout level, has changed the cost benefit model and made outsourcing an attractive alternative. As charges tend to be on a price-per-note basis, outsourcing is sensitive to changes in cash volumes, transforming cash processing from a fixed to a variable cost so that declining volumes will mean falling costs.

BOTTOM LINE

The decline of cash increases the imperative for retailers to seek efficiencies in cash operations and move from fixed to variable cost models. A combination of outsourcing and cash technology solutions will become normal practice for larger retailers as the interest rate cycle changes and technology costs reduce.

Cash Office Technology

Same day value through 'provisional credit', removal of liability once cash is counted and deposited, immediate checkout operator reconciliation, transparency and labor savings. What's not to like about cash counting safes? Interestingly, adoption of this technology has been slow so far, with the exception of the quick service restaurants sector. Obstacles have included upfront capital investment for non-front of house solutions and low interest rates, limiting the attractiveness of provisional credit. Success has therefore been confined to high labor cost markets such as France.

However, declining technology costs and a turn in the interest rate cycle will remove these barriers. Armored Transport (AT) companies have tried to develop rental strategies to provide end-to-end cash management solutions and, as the underlying attraction of this technology improves, we expect merchants to show increased interest. However, concerns remain that merchants could become 'locked-in' to long term contracts at high prices, while AT companies gain all the value from reduced technology costs, scheduling efficiencies and high exit barriers.

Case Study: Car park Operators

It isn't just traditional retail merchants that are adjusting their operations due to lower cash volumes. The transport industry has seen significant transformation. For example, Transport for London has recently transitioned to cashless on buses. Behind the scenes, less transparent but equally radical changes are occurring.

Large-scale car park operators have significantly streamlined cash operations. Operators traditionally staffed each car park with at least one individual that, among other tasks, would be responsible for replenishment, maintenance and reconciliation of payment machines. The cash was often then physically transfered to a hub employing cashiers and low-tech machinery to process cash into bulk for onward delivery to the bank. Today, all these functions are outsourced to AT providers. Charges are levied on a per note/visit basis meaning that costs are now variable rather than fixed. Besides reduced costs, this new operating model has also improved cash flow as cash is banked, on average, three days earlier. Internal loses are reduced and reconciliation improved.

STRATEGIES TO UNLOCK VALUE

Merchants and ATM deployers have a number of options to deal with the decline of cash.

The Armored Transport (AT) industry is reaping the rewards of lower capital costs, increased labor productivity, improved technology, reduced attacks and reduced fuel charges. Yet merchants and ATM deployers have seen little reduction in prices over recent years and some AT providers still impose fuel and insurance related surcharges.

Meanwhile cash processors have reaped the rewards of consolidation, high barriers to entry and vastly improved technology, with many reducing staffing levels by two thirds in the process. However, cash deposit and withdrawal pricing has remained stagnant. What can merchants and ATM deployers do to divert some of these benefits to themselves?

1. Outsource

Economies of scale, rapidly changing technology, security and knowledge all point towards outsourcing of cash activities. AT services, by their nature, require intensity of service to be productive. Very few retailers or deployers have the geographical intensity required to make an in-house AT service financially viable. Historically, reasons to insource armored transportation have rested on service quality and high supplier pricing, but these reasons are just a reflection of inefficient servicing & procurement. Supply chain performance and service quality in the industry has improved significantly over the last decade due to improved vehicles, newer technology and flexible working. Reconciliation presented a major barrier to outsourcing cash processing but again technology has resolved these issues. Outsourcing cash processing at a (typical) large retail chain can reduce costs of cash by 25%.

2. Innovate

Cash counting safes and recycling machines have reduced in cost over recent years as the technology improves. As interest rates rise, the attraction of provisional credit & improved cash flow will grow and better reconciliation, improved productivity and the removal of risk make these machines a "no brainer" in the quick service restaurant (QSRs) sector. Capital costs have yet to reduce to the extent that large retailers can choose this option over outsourcing, but this is only a matter of time and as labor costs continue to increase relative to capital, these options will become more attractive.

3. Radicalize your supply chain

So far, scheduling cash replenishments/collections has been conducted within the prism of traditional weekly patterns. However, cash flow does not take such a structured path. In recent years, CMS has worked with a number of clients to make the cash supply chain more responsive to the day-to-day needs of their businesses. Flexibility is key and, by working with suppliers, savings of as much as 20-30% in cash management budgets can be achieved without the need to reduce collection/ replenishment charges or threaten service quality/cash availability.

4. Encourage competitive markets

It's time for retailers & deployers to raise the issue of ever increasing concentration in cash markets with central banks & governments through industry associations. Retailers in the UK recently succeeded in getting card interchange fees included in the remit of the new payments regulator. There is a strong case that cash be included too. Central banks have a different agenda and it would be dangerous to entrust your business interests and those of your customers to them.

Author

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AN ALTERNATIVE VIEW: CASH IS STILL KING

Distrust of digital payments offers an opportunity for a cash renaissance.

Mobile payments, e-wallets and related security are blitzing the headlines. What is the impact of these surging digital payment initiatives on the cash needs of the general public, back dropped against their desire to use cash in the wake of repeated card and data breaches? How damaged is the consumers' comfort with using digital payments? Does this heighten the need and opportunity for deployers to increase security behind the ATM platform and take advantage of the dent in consumer card confidence?

Cash's unique position

Boss: "When will cash go away?"
Me: "Well, after the plastics have."

We'll see if I am right someday.

Plastics and mobile devices swim in the same digital pool - they overlap one another for usage. Cards and mobile are lopsided twins in a digital realm that is becoming extremely homogeneous. On the other hand, cash is used for payments outside of the compromised fiber optic payments expressway. It remains the alternative for payments when technology breaks down, is unavailable or loses the trust of the consumer.

For decades we've heard the same mantra of today: 'Cash is going away.' 'Cash is obsolete.' 'Digital is the future.' Yet, ATMs continue to proliferate globally. The level of cash deposits at local ATMs alone has increased 29% since the explosion of deposit automation in 2009. Local January ATM cash withdrawals have marginally fluctuated between $6.6 and $6.9 million for three years despite a reported 'decrease' in ATM usage. That's millions changing hands in cash between consumers and to the merchants and banks for payments, savings, daily expenses or just dinner out. And we all thought they said cash was "going away".

Guest Columnist

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Cash vs cards – a local business' unwavering outlook

In college I worked at Bob's Comic Shop. Bob's carried everything any loyal comic geek could ever want and was busy all week. Bob's had it, would find it or knew how to get it. As long as you paid in cash.

Honestly, Bob would accept, "checks, rolled coins, gold bullion, or pre-ban ivory." But no cards. NO cards. He wasn't in some backwoods, ramshackle shop. This was a nice store in a busy strip mall, at the center of suburban yuppyville. Plenty of money and lots of plastic.

Sales would walk out the door because they couldn't swipe to make their purchase. Bob refused to take cards. "If they want it they will come back with cash." Many times he just said, "There's an ATM just up the sidewalk." Bob was a businessman with lean margins, and he was not going to pay fees charged by the brands for accepting cards.

I'm 42 now, and Bob's is still open. A new generation is buying comics. The old manager is still chastising kids for misbehaving. Bob does not take debit cards nor is he rushing towards the surging digital payments. His economic reasoning still stands but there is a new twist. More customers show up ready to pay cash and fewer complain when he tells them, "no debit cards." He looked into accepting cards in 2008, but when the bottom crashed, he saw resurgence in cash sales. When he relinquished to credit cards after 2011, the usage still paled to checks and cash. He's been asked by online fans about Bitcoin, though he hasn't lost a sale because he wasn't accepting it. The number of online customers that still mail in cash, checks and money orders for payment is staggering.

An ATM opportunity?

This brings us back to the question, "does the current state of consumer distrust with digital and card payments offer an opportunity for ATM operators and cash renaissance?" I believe the answer is yes, if we improve the confidence level in the ATM channel security as a reliable means of purchasing power.

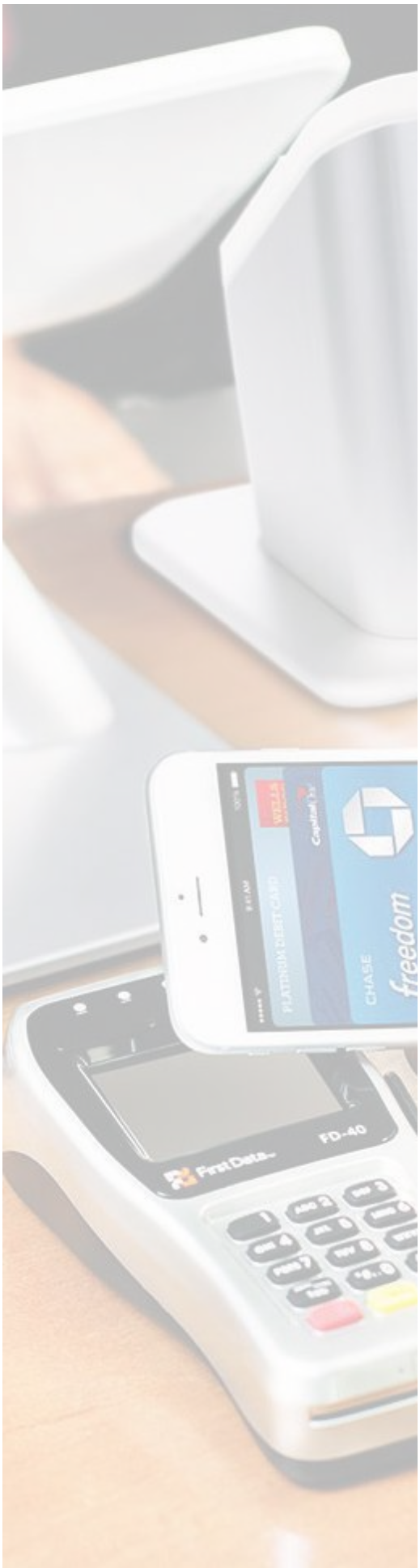
Deployers should thrust themselves ahead of the retail POS merchants by publicly embracing new security for validation at ATMs and in-transit. Deployers must leverage mobile for cash access, as well as P2P movement of cash between mobile wallets that bypasses the security porous payments pipeline that is being hacked at will. Done right, the operational engine of ATMs is, or can be, inherently more secure than the retail POS. This will be down to the more stringent federal, network and brand regulatory guidelines that ATMs have existed under since 2001. But everyone has to be on board. The FIs are being pushed there by regulation. Our ISO ATM brethren, need to embrace a streamlined and secure cash dispensing platform that will survive and evolve with technology. Too many deployers want a handout to offset the expense of EMV. It's not coming; and by waiting for one they are only hastening their own demise. Bite the bullet now, spend the money to secure the channel – albeit at a considerably lower overhead than the financial institutions that have been forced to keep pace all along.

Still the king

Cash is still king because the king can be spent anywhere and is accepted everywhere. Power or no power. At a theater or at the carnival. To purchase a candy bar or pay off a car loan. Over regulation, Durbin and payment system compromises have beaten down the traditional payment platform, and eroded the trust of the American consumer. But as long as I can find an ATM, as long as I have cash, I can get by. Even if the power is out, and all seems lost, I know that I did listen to my father when he said to always, "keep some cash on you."

BOTTOM LINE

ATM deployers are in a unique position to make cash the victor, rather than the victim, of digital payments. Through ensuring the security of the ATM channel – which digital payment vehicles have struggled with – deployers can leverage the benefits of cash against alternative methods.



INTEREST RATES: THE TIME-BOMB TICKS ON

A five-step plan to deal with rising interest rates.

The previous issue of the Global Cash Report was dedicated to the growing threat of a cyclical rise in interest rates. While interest rates have been at record lows in the US, the UK and other major economies, benign conditions have been created for ATM deployers. The cash management trade-off between holding cash and delivering cash has been heavily weighted in favor of holding cash. As interest rates rise, this will rapidly change.

While the exact timing of interest rate rises are not known, it is widely expected that the initial rise will occur this year in the US – with low inflation being the only major metric that appears to be standing in the way. While rates will only increase in incremental amounts it is important that each rise is factored into an ATM deployers' operations and cash management trade-off, as operational costs will rise. The speed and extent to which rates rise will influence the result on a deployer's bottom line. However, with the Federal Reserve's latest Federal Open Market Committee "dot plot" signalling some members' intentions for rates to be around the 4% mark by the end of 2016 **(figure 1)**, the negative impact has the potential to be significant over a short space of time.

Preparation and action needs to be taken. Here is a three-step guide offering practical advice for ATM deployers' cash management to navigate the upcoming rate rises with minimal consequence.

Figure 1: The Federal Reserve's Federal Open Market Committee (FOMC) "dot plot" from the Dec 2014 committee meeting

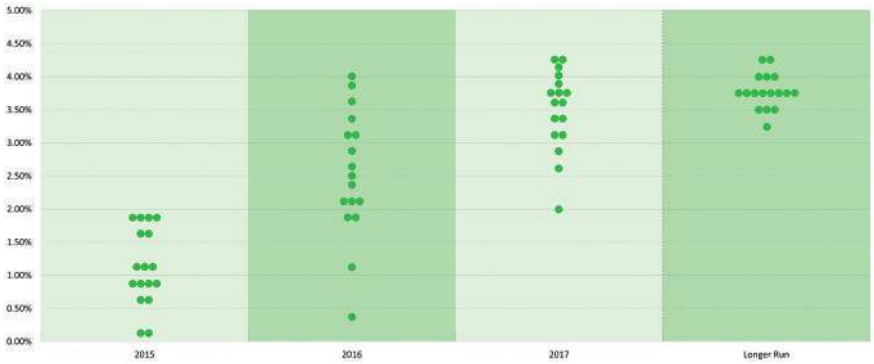


Figure 1: The Federal Reserve's Federal Open Market Committee (FOMC) "dot plot" from the December 2014 committee meeting. Each dot represents the interest rate that a committee member's deemed an appropriate Federal Funds Rate target for that time period. At the end of 2016, targets range to 4% - if interest rates were to reach this level it would signal a sixteen-fold increase on the current rate.

Source: US Federal Reserve FOMC

BOTTOM LINE

Due to the extent of the impact that increased interest rates will have, preparation becomes key. While over the past six years, effective cash management has meant the difference between certain levels of profitability, in the near future it will determine whether you are profitable at all.

Step 1: Optimize cash now

Don't sleep-walk yourself into trouble. While conditions are still benign, it is important that you don't get lulled into a false sense of security. Immediately reacting when rates do rise is too late, it is best to optimize your cash management now - it will begin to pay dividends today with the benefits only growing over time.

Step 2: Stress-test your cash management processes

While your cash management practices may be operating well as external conditions are relatively nonthreatening, it is important to see how they hold up in other conditions. Simulations can be used to forecast the effect of changing interest rate environments and other external scenarios on your cash management. Prepare yourself for a shock as small increases in interest rates will have a relatively greater negative impact on your bottom line!

Step 3: Ensure supplier contracts are flexible and efficient

Too often, contract negotiations can lead to an inability to react effectively to scenarios such as interest rate changes. While price is important, ensure it does not come at the expense of operational efficiency. Furthermore there is often too little forethought on the future, SLAs are often too loose and escalation procedures too vague. If predictions are correct, all elements of the cost of cash will rise over the medium term. Hence, just like your mortgage, it may make sense to fix prices and service levels long term. Pressure on service quality due to increased demand may lead to tightening operational flexibility and so, first movers will receive the best terms – make sure you're one of them!

Step 4: Prepare for operational impact

Expect increased pressure on resources as you order more often. For example, the armored transport industry may not have the capacity it did in 2007 when interest rates were at higher levels. Therefore, you should expect to see poorer supplier performance and experience a higher cost of failure - at least in the short term - as demand picks up. Automation of your decision making process is vital as your productivity levels will be challenged by increased workloads and weaker supply chain management.

Step 5: Outsourcing

Finally, take a look at the benefits of outsourcing - it can make sense to outsource as you gain from economies of scale, knowledge and experience – factors which will become ever more beneficial when conditions are more threatening.

> ***"I would rather the Federal Open Market Committee raise rates early and gradually than late and steeply."***
>
> Richard Fisher, President - Dallas Federal Reserve Bank

Author

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> ***"I think we have to move now, or soon, in order to be in the right position as the economy evolves."***
>
> James Bullard, President and CEO
> Reserve Bank of St Loius

Why are interest rates a concern?

Interest rates will lead to cost increases across your network – no matter how well you manage them.

The "cash management trade-off" is impacted. In other words, the cash inside your machines, on its way to the machine and on the way back to the bank, will begin to cost you more and in turn it will be more efficient to increase the number of loads.

More orders, more loads.

Are you ready for the impact on your P&L?

Are you ready for increased operational stress?

The Global Cash Report Q4 2014 edition featured a special report on the "ATM Industry's Ticking Time-bomb: Rising Interest Rates". Available online at www.cms-cashmanagement.com

CASH CALENDAR

Upcoming important dates

April 2015

7th | Reserve Bank of Australia interest rate decision and statement, Sydney, Australia

9th | Bank of England Monetary Policy Committee meeting, London, UK

15th | ECB Governing Council monetary policy meeting, statement and press conference, Frankfurt, Germany

Bank of Canada interest rate announcement and Monetary Policy Report, Ottawa, Canada

17th-18th | US Federal Reserve Federal Open Market Committee (FOMC) meeting, Washington D.C., USA

29th | Reserve Bank of New Zealand Official Cash Rate (OCR) decision, Wellington, New Zealand

May 2015

5th | Reserve Bank of Australia interest rate decision and statement, Sydney, Australia

7th | United Kingdom General Election

8th | Bank of England Monetary Policy Committee meeting, London, UK

10th | The Currency Conference, Vancouver, Canada

13th | Bank of England Inflation Report publication, London, UK

17th-20th | CUNA CFO Council Conference, New Orleans, Louisiana, USA

27th | Bank of Canada interest rate announcement, Ottawa, Canada

June 2015

2nd | Reserve Bank of Australia interest rate decision and statement, Sydney, Australia

3rd | ECB Governing Council monetary policy meeting, statement and press conference, Frankfurt, Germany

4th | Bank of England Monetary Policy Committee meeting, London, UK

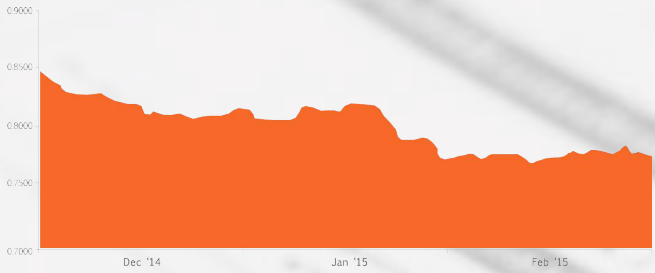
10th | Reserve Bank of New Zealand Official Cash Rate (OCR) decision, Wellington, New Zealand

16th-17th | ATM Industry Association (ATMIA) European ATMs Conference, London, UK

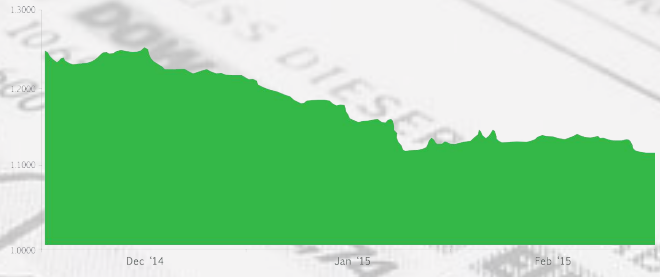
US Federal Reserve Federal Open Market Committee (FOMC) meeting, Summary of Economic Projections and press conference by Federal Reserve Chair Janet Yellen, Washington D.C., USA

EXCHANGE RATES

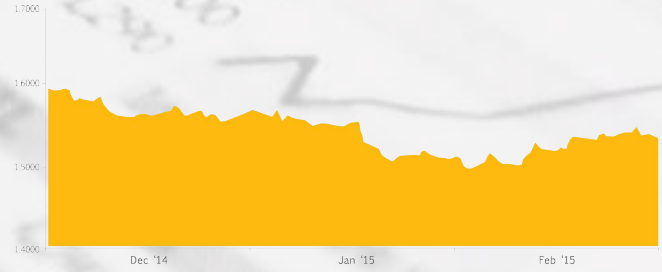
AUD - 1 AUD in USD



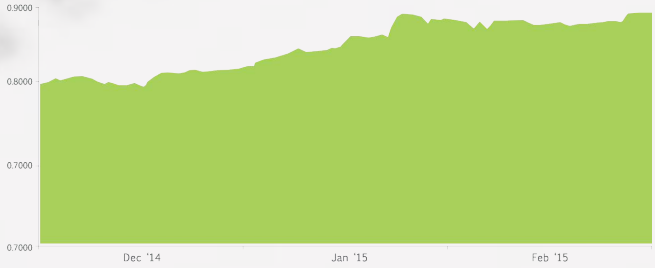
EUR - 1 EUR in USD



GBP - 1 GBP in USD



USD - 1 USD in EUR



CASH STATS THIS QUARTER

Contactless makes major inroads.

As alternative payment methods jockey for position, no clear market leader has yet to come to the surface. However, in certain markets, it appears that contactless cards may be taking the early lead. Now, the cash industry is left wondering if a payment method that it thought would only cannibalize itself – card usage – will be cash's biggest threat?

There are three factors which position contactless to continue taking market share away from cash and, as an industry, it's time to take notice.

Key Findings

User adoption has been staggering

It could be argued that contactless cards have a much better starting platform than the other alternative payment methods due to the extensive use of debit and credit cards. However, a change in consumer behavior still has to be made. Contactless cards appear to be overcoming this. In the UK, a leading payments economy, £302.7m was spent using contactless in November 2014. This represents growth in value of 275.5% year on year, as shown in **figure 1.**

Merchants are getting behind it

Many payment alternatives are hampered by a lack of adoption from merchants, either due to the additional equipment required or resistance to yet another untried payment process. Contactless has overcome these merchant concerns. The costs of additional equipment are relatively low and are often subsidized by card schemes. Furthermore, the process utilizes the pre-existing card acceptance system. This has led to strong merchant support, and there is pressure for maximum transaction limits. This has already occurred in some markets such as Australia and New Zealand. **Figure 2** shows the transaction limit for seven countries across the world, indexed to the US Dollar.

It's underdeveloped in some major markets

Despite looking like the early favorite, contactless still has a lot of mileage left. There are some major markets, namely the United States, where contactless cards are still in their infancy due to the lack of EMV migration. This gives contactless significant potential for sustained growth into the future as once certain markets mature others will be experiencing major growth rates. **Figure 3** shows the estimated geographic distribution of the 249 million contactless cards issued as of 2014.

Figure 1: Value transacted using contactless card (UK)

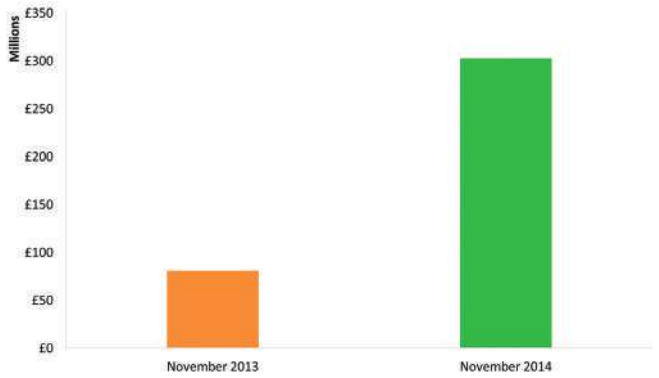


Figure 2: Contactless transaction limit (indexed to USD)

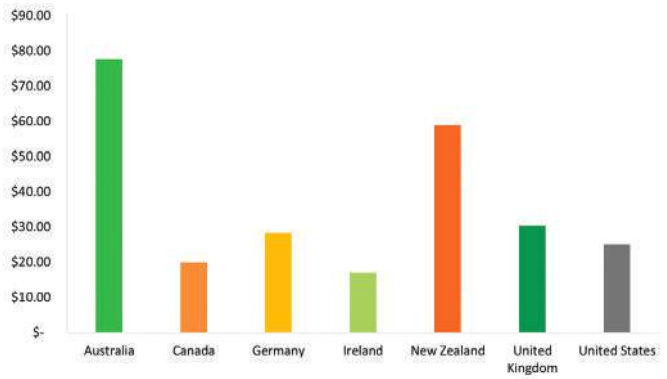
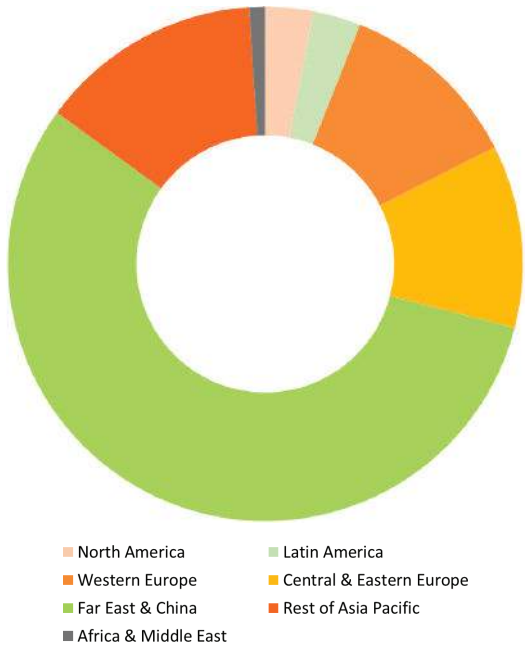


Figure 3: Contactless cards issued as of 2014 by geographic distribution



Sources:

Figure 1: UK Cards Association.
Figure 2: Visa/MasterCard; Exchange rate at 04/02/2015.
Figure 3: Juniper Research.

Global Cash Management Experts

Cash Management Solutions (CMS) is dedicated to optimizing the management of coins and notes. Our cash management consultancy and fully managed services are used by a diverse range of companies globally including financial institutions, ATM deployers and FX retailers.

CMS is completely independent and rather than rely on standard forecasting techniques or basic software, we combine advanced site-by-site modeling with our team of highly qualified mathematical analysts to create maximum value throughout the supply chain.

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