

J.P.Morgan

Third-Party Money: What it means, and why it matters



In the embedded payments era, corporate treasurers are uncovering a new opportunity: Managing other people's money safely and effectively – while harnessing the benefits for their own business.

The time-honored role of a corporate treasurer (CT) is to take care of their company's cash. They're concerned with working capital as it pertains to their own businesses including addressing the funding, deployment and risk management needs of the enterprise.

With the advent of modern technology and greater regulatory freedom, many corporations are discovering that embedding payments and financial services into their business can create stickier relationships and new revenue sources with buyers, suppliers, employees, etc... While engaging in financial transactions with these parties was commonplace, handling money or payment activities belonging to them has historically not been their concern.

The challenge? To take advantage of new business models, businesses must now must embrace new financial responsibilities unrelated to their own assets and liabilities. [This is third-party money \(3PM\)](#), and it is a trend that is growing in uptake every day.

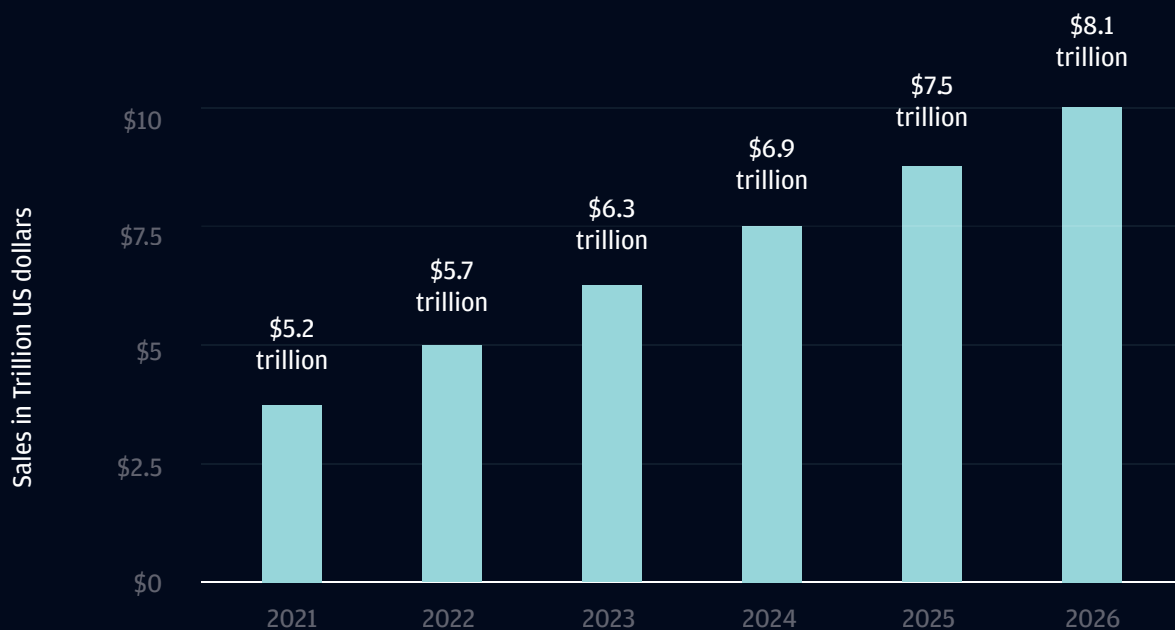
3PM represents an exciting new frontier for treasurers. So, what do corporate treasurers need to know about this fast-evolving space?

What is 3PM?

Third-party money (3PM) is fundamentally different to the funds associated with traditional day-to-day working capital, or company earnings. It is the cash and payment obligations that the business does not own and instead supports on behalf of other organizations (e.g. clients, vendors, employees or supplier). This requires different structures and processes in order to manage this money and meet all obligations and regulatory requirements.

Being able to process 3PM efficiently is so compelling because it allows businesses to better monetize their existing infrastructure and platforms and tap into new opportunities. For example, they can start offering additional goods and services from 3rd party players, such as through an online marketplace. Or they can facilitate payments quickly and efficiently to suppliers, which is useful for services like ride-hailing, which use large pools of gig workers. Companies are also increasingly offering [digital wallets](#), which may involve them storing funds on behalf of their customers. These services are linked to the growing digitalization of business operations as well as the continuing expansion of e-commerce. In 2021, retail e-commerce sales amounted to approximately 5.2 trillion U.S. dollars worldwide. This figure is forecast to grow by 56 percent over the next years, reaching about 8.1 trillion dollars by 2026.¹

Global e-commerce Sales 2021-2026



Source: eMarketer

3PM in practice

Let's look at some real-world scenarios which demonstrate how 3PM plays out in practice.

- Take the example of a major sports retailer that decides to drive sales by launching an online marketplace of curated sportswear made up of its most popular brands. The sports store hosts multiple individual sports clothing businesses on this digital marketplace, handling sales and payments for each brand. Importantly, the sports retailer is not the seller of record and does not own the inventory. As a result, there is cash moving through the marketplace that is not destined for the sport's stores own accounts; instead, this is cash that is due and owed to each brand. This is third-party money.
- Ride-hailing apps are another key example of third-party money. By creating integrated services - not just the ability to order a trip home on-demand, but adding the ability to pay for the trip, split payments with friends, order food, and to hold a payments wallet all within the same seamless smartphone-based ecosystem is highly attractive to users, driving customer loyalty - and generates a wealth of valuable data for the business in question. In this scenario, funds may need to go to the driver, the food outlet, the payments provider, and to the ride-hailing app itself.

Rise of super-apps and online marketplaces

The breadth and scope of 3PM will only grow in the coming years. The super-app model described above, involves making a huge array of different services available in a single platform, with a single embedded payment system. [According to J.P. Morgan](#), super-apps already account for \$36 trillion in global payments volumes, and are expanding rapidly around the world.

Meanwhile, online marketplaces are continuing to grow in influence, moving away from areas like consumer goods, travel and clothing to encompass trades, real estate and vehicle purchases. By 2025, it is estimated that online marketplaces will overtake 1st party e-commerce channel in many categories. Brands and businesses will start trying to replicate elements of this model in order to compete, making 3PM solutions vital.

For example, a haircare company may have previously supplied its client base of hairdressers through traditional distribution channels. Now, it's primary model is an online platform that allows hairdressers to buy products and renew orders at the click of a button. However, because they have such a wide network of customers, the corporate can also use that platform to offer other adjacent products and services, sourced from different suppliers. They do not own all the products on the marketplace but will be collecting and holding cash that they will need to pay onwards. By taking a cut of the transaction value, they can generate a lucrative extra revenue stream.

Online market-places - Average cut of transaction value

Category	Percentage take of transaction
Ticketing	30-35%
Clothing	20-25%
Travel	20-25%
Food Delivery	15-20%
Single Category Ecommerce	14-15%
Multi-Category Ecommerce	10-15%

Source: OSC Strategy

A trend that is not just about consumers – but infiltrating the B2B world too

This highlights another crucial point, which is the evolution towards 3PM is not just happening in the business-to-consumer (B2C) and direct-to-consumer (D2C) spaces. In the business-to-business (B2B) world, businesses are increasingly calling on their partners to provide speedy, almost instant execution of ordering, sales and payment within a single ecosystem.

*Super-apps
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volumes*

J.P. Morgan Payments



Considerations for corporate treasurers

On a practical level, there is much for the corporate treasurer to consider in order to meet these changes. For large industrial corporates moving into this style of doing business, its demands can come as a surprise. Previously key performance indicators (KPIs) have been centered around driving down the number of accounts required, centralizing cash into an in-house bank or regional treasury center and managing cash buffers to be as low as possible. Yet when a business is now tasked with managing a flow of funds destined for different end receivers, corporate treasurers may need to now think about:



Setting-up more accounts to take care of divergent fund flows. The current trend towards highly centralized liquidity structures may have to be adapted as payments become more complex. It could involve setting up [virtual accounts](#) and also transacting in more currencies than previously.



Paying out cash to multiple external businesses - which may mean special accounts are required separate to the corporate's own cash, to ensure that the third-party money is secure under any kind of solvency scenario.



If cash is due and owed to the end consumer, different licensing or business models will be required. New regulations may also apply, which did not have to be adhered to under existing ways of working. Safeguarding regulations can change significantly depending on the country.



Treasurers need to find a way to maintain separation of the fund types, without sacrificing efficiency or visibility across both. This will require new tools and greater use of automation. At the same time, they have to work within the structures of their organization, there may be limits.

As a result of these challenges many large corporates opt to outsource their 3PM functionalities to a partner bank. One model involves creating a dedicated center to manage seller or supplier onboarding, which includes trade-screening and know your customer (KYC) checks. This helps to mitigate potential fraud, which can be a major challenge with high volumes of 3PM. Through this center the partner bank can then handle the payment transfers, ensuring the correct revenue share percentage goes to the corporate and the seller.

To do this, the bank creates segregated accounts, which are used only for 3PM payments, with the accrued money managed as a liability on the corporate's books. Other banking services can also be offered such as embedded trade financing. The seller can also log into the center for reporting, payout status and disputes. By outsourcing, the corporate gets the advantage of an efficient turn-key solution, while still being able to manage the seller relationships and access the data.



Major opportunities for 3PM

The corporate treasurer's role is to ensure the financial stability of the corporate, limit financial exposures and to make sure that access to funding is available as required. As business development teams come up with strategies to expand the company's distribution channels and their service lines, there will be a greater reliance on 3PM.

What this means is that corporate treasury will have to move much closer to the business development teams and become a strategic partner, helping to put in place the financial structures which will enable a host of innovative new business lines. If they can get this right, then there are many exciting possibilities. We explore some below.



Treasury optimization

Treasury optimization and 3PM go hand in hand and can have wide ranging impacts for the business. For example, to enable 3PM a company may leverage a number of Treasury solutions from its banking partner, such as cash concentration, notional pooling or virtual accounts. Automated cash concentration allows companies to mobilize funds across accounts, borders and banks, so they can access same-day liquidity on a global basis. As well as being important for 3PM, this can help companies optimize their liquidity management and deploy cash more efficiently, helping their overall business operations.

By moving to multi-currency notional pooling, companies can pool multiple currencies as a single net position. This reduces the need for inter-company loans and supports cost-effective FX hedging. It is also important for 3PM as funds may be owed to companies in different locations around the world. Virtual accounts are also a valuable tool, as they eliminate the need for physical cash sweeps and allow both greater transparency and easier reconciliation across different corporate or third-party entities.



Payments as a service

Whether it's cross-border transfers, cross-currency transfers or higher value transactions, there are a myriad of payment services that would have been a cost but can now be monetized and turned into a profit center. In addition, there is the opportunity to add additional embedded financial services, to further maximize revenue. For example, offering customers 'buy now, pay later options,' or lending or credit options to other merchants that are using their platform, based on analysis of their sales.³ Increasingly, some corporates are turning their payments offering into a separate entity and providing it as a service to other customers. So, if they have a curated marketplace, they can offer their payment functionality to suppliers, or even to companies working in different industries.

"Payments as a service is forecast to reach \$16.7bn in value by 2024."²





Loyalty and rewards

From a treasury perspective, any customer cash that is held in a wallet has to be carefully managed and safeguarded. But it also opens up the opportunity to offer additional products and services, maximizing share of wallet. Take a company like Singapore's Grab, which started in ride-hailing, and now also offers food and grocery deliveries, as well as financial services like insurance and payments, all accessible from a single digital wallet. The goal is to create an environment whereby consumers wish to repeatedly come back because it's easy to use, adds value and because they're already holding cash in the ecosystem.

This can be made even more powerful with targeted loyalty programs and rewards that are based on customer preferences and are delivered digitally or through push notifications. According to recent research digital loyalty program memberships will reach 32 billion globally by 2025, representing growth of a third.⁴ Common digital reward schemes involve offering loyalty points for every dollar spent, that can then be redeemed and discounted. Starbucks's digital rewards scheme is so successful that it now accounts for 53% of in-store spending.⁵ But it also includes non-monetary benefits, like allowing customers to skip the queue in a store.



Big data, bigger impact

The key to unlocking the value of 3PM is through the collection of data, which allows the creation of more efficient services and engaging, personalized offers. As well as keeping customers in the ecosystem, this information can be used for better forecasting, superior product planning and supply chain management.

This will only increase as companies digitize and automate the whole purchasing chain. J.P. Morgan's research identifies different stages of digital maturity (see below). The **Discovery Phase** mainly involves the shift from manual to digital processing.

In the **Transformation Stage** the focus is on synthesizing existing data and using it to generate deep insights. By contrast, companies in the **Visionary Stage** have end-to-end automation and are leveraging technologies like AI and machine learning to apply predictive decision making. In this scenario, data is not merely an area of additional value, it is the driving force of the company's success. We believe that 3PM, and the customer data it will provide, can be a key contributor to a company's digital progression, providing the right structures are in place to manage it efficiently.



Digital maturity stages

Discovery ⁶	Transformation ⁷	Visionary ⁸
Accelerating digitalization across the organization	Fill gaps and build structures to succeed	Digital forward leadership
Paper to electronic/online processes	Integrated/embedded payments	Hyper automation
Data collection	Synthesizing data available and translating into analytics and insights	Predictive decision making and insights through usage of data using emerging technology techniques

Conclusion

As 3PM becomes more important the role of corporate treasury will continue to evolve from a primary focus on areas like multi-currency management and risk management to encompass settlement optimization, frictionless payments and complex new account structures. Whereas once treasurers were only tasked with looking after the corporate's money, now they are warehousing other people's cash, with the responsibilities and safeguarding that comes with that. Those that get this right, will facilitate the development of exciting new opportunities for their companies.

Call to action

JP Morgan has an in-depth knowledge of 3PM, extracting its benefits and navigating its challenges with our partner clients daily. We are constantly seeking growth. Alongside existing liquidity products, we are actively developing exciting new 3PM solutions to meet our clients' demands for better payments and digitization experiences.

Are you a corporate treasurer looking to onboard this new aspect of your role effectively? Contact your local J.P. Morgan representative to learn how J.P. Morgan can partner with your company.

- ¹ Statista, September 2022. "Retail E-commerce Sales Worldwide from 2014 to 2026." Available at: <https://www.statista.com/statistics/379046/worldwide-retail-e-commerce-sales/>. Accessed July 2022.
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- ³ Finextra, February 2022. 'How Embedded Finance Helps Businesses Generate Revenue and Increase Loyalty.' Available at: <https://www.finextra.com/blogposting/21785/how-embedded-finance-helps-businesses-generate-revenue-and-increase-loyalty>. Accessed July 2022.
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- ⁶ McKinsey, October 2020, 'How COVID-19 has pushed companies over the technology tipping point—and transformed business forever'. Available at: <https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/how-covid-19-has-pushed-companies-over-the-technology-tipping-point-and-transformed-business-forever>. Accessed July 2022.
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- ⁸ Retail DIVE, February 2021, 'Top 7 trends in retail digital transformation and innovation for 2021'. Available at: <https://www.retaildive.com/news/top-7-trends-in-retail-digital-transformation-and-innovation-for-2021/595486/>. Accessed July 2022.

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