January/February 2015

# treasurytoday ASIA

research | insight | analysis

## Treasury priorities in 2015

Thinking about relocating your SSC this year? Or planning to introduce some innovative technology to the treasury department? Then you're not alone. We examine the priorities for treasurers operating in the APAC region over the next 12 months.

### The Corporate View

**Steven Wong**

Group Treasurer

**Neptune Orient Lines Group**

### Women in Treasury

**Dawn Chua**

Head of Capital and Treasury

**SGX**

### Financing

Private placements

### Trade

ASEAN: a new era

### Risk Management

Tackling political risk

### Back to Basics

Cash flow forecasting

# Treasury Today Asia App

**www.treasurytodayasia.com/app**

# Mobilising the APAC markets

The ascent of mobile is arguably the greatest innovation that the payments industry has seen in recent memory. Nowhere does the mobile revolution hold more promise than in Asia. After all, the region accounts for over half of the world's mobile devices. There is also a significant move towards m-commerce in APAC, with over 50% of all Asia-based online transactions in 2015 set to be made by mobile, according to Criteo.

Yet, as we frequently see in the region, there is great disparity between individual nations. This is not only as a result of varying levels of smartphone penetration, but also because of payment infrastructure challenges in rapidly growing markets, as well as certain cultural barriers.

Japan and South Korea are widely recognised as advanced markets for mobile shopping with Criteo reporting that over 45% of online retail transactions are made via mobile devices. In fact, Japanese e-commerce sites have mobile conversion rates that double those seen in the US. Australia is another mobile leader in the region, with impressive uptake of contactless payments.

Meanwhile, countries such as Singapore, Hong Kong and China – although possessing an infrastructure that is more than capable of supporting mobile payments – have yet to encourage widespread adoption. Others, such as Malaysia, remain largely cash-based societies.

While governments, national payments associations and internet providers are working furiously to increase mobile adoption, more must be done by banks and treasurers too. According to EY's recent global commercial banking survey, almost 70% of banks' commercial customers in Asia are using mobile banking channels each week. But when asked about the reasons for not using online and mobile channels more often, the most commonly cited obstacle in the region was security. This was closely followed by slow speed and poor functionality. In short, banks have some work to do in 2015 and beyond to provide security enhancements around their mobile solutions, as well as improved user experience.

Treasurers, on the other hand, should take the time to consider how mobile might provide growth and efficiency opportunities for their business. Mobile is not just for banking on the go, or a smart solution for merchants to improve consumer interaction. It can ultimately assist in improving your working capital metrics, whilst presenting many opportunities for cost-cutting too. So, in an ever-competitive market, mobile is surely worth a second look.


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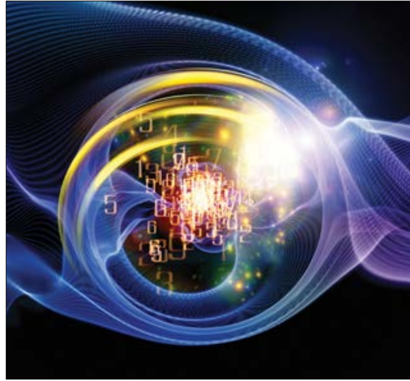

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### Steven Wong
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With over three decades' experience in the shipping and logistics industry, Steven Wong, Group Treasurer, Neptune Orient Lines Group, has guided the company through quite a few ups and downs in a cyclical sector. In more recent years Wong has applied his knowledge and understanding of philosophy to make some important changes not only to the treasury but to the business.


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## Peak flow

For any business, knowing how much money will be coming in and going out gives a better understanding of how much will be needed to keep operating and to enable growth. Treasury Today Asia goes 'back to basics' with cash flow forecasting and asks how businesses should best approach it.

**These pages contain edited versions of a few of the Treasury Insight pieces written in the last month. The full versions are posted on treasurytoday.com as they are ready. The Treasury Insights weekly email summarises the new pieces from that week plus other news relevant to treasury. You can register for this free service at treasurytodayasia.com**

## A baht time: is Thailand ready for treasury centres?

Growth in Asia has been well-documented in recent years. How can businesses make the most of their operational presence in such a dynamic environment? One way is to consolidate certain treasury functions in a well-placed treasury centre. From a finance perspective, attracting corporates has been relatively easy in some jurisdictions because the incentives have been offered by their governments who have been keen to promote the centralisation of treasury activities. In Singapore and Malaysia, for example, reduced or zero tax is applied to income from qualifying treasury services.

But what about Thailand, once the financial phenomenon of Asia? Thai treasury centres are few and far between; currently there are just four in the country. In recent years, Thailand has seen the commencement of a major overhaul of its financial sector as part of its Final Sector Master Plan (FSMP). This may go some way to creating the right environment, but as well as stringent foreign exchange controls the country has also faced labour shortages, natural disaster and political unrest, all of which undermine investor confidence.

Large MNCs operating in Thailand usually adopt a structure similar to those in other markets in the region but they will commonly operate from a regional treasury centre outside of Thailand, such as in Singapore or Hong Kong. A Singapore-based Citi spokesperson has argued that Thailand "currently doesn't offer the right incentives for corporate treasurers". Their view is informed by Thailand's imposition of capital controls on cross-border inter-company lending. There is also limited liquidity in foreign currencies locally which he feels may inhibit corporates operating their regional treasury out of Thailand. "I therefore don't foresee Thailand becoming a big treasury centre for multinationals in the near future," he says.

Despite the problems, the country is in many ways heading in the right direction. It has, for example, pushed forward within the ASEAN community, working towards integration with the region's capital markets. BoT is looking to entice new money but needs an act of parliament to do so which is a slow process.

At least the FSMP is aiming to making the sector more "efficient, competitive and transparent". It is a three-part plan. Phase one (completed in 2009) overhauled the commercial banking licence system leading to significant consolidation of the Thai banking sector. Phase two is ongoing and seeks to invest in infrastructure and technology, reduce operating costs and increase competition in the sector. The final phase is set to start soon and will evaluate the results of previous phases and build out recommendations accordingly.

## The rise of Chinese MMFs

Money Market Funds in China are a hot topic. The rise of retail funds such as Yu'e Bao Wow, owned by Chinese e-commerce giant Alibaba, is making headline news and causing seismic shifts in the Chinese financial system. In fact, statistics from May 2014 showed that Yu'e Bao Wow was the fourth largest (by assets) MMF in the world with $90 billion worth of assets. This is a third of the entire assets in the Chinese MMF market. Yet behind the headlines, corporate MMFs are also evolving in order to better meet corporate's short-term liquidity needs.

### Market development

Until last year, the corporate MMF market was dominated by next-day liquidity funds. According to Kheng Leong Cheah, Head of Sales, Global Liquidity, China at J.P. Morgan China, who distributes such a fund, they have proved popular amongst corporates. "Principal preservation has historically been the most important aspect for our investors, and these funds have met that need," he says. However, as the market has developed and corporates' needs have become more complex, other demands are starting to come to the fore. "The most frequent requirement we are seeing now is for liquidity, and the ability to access funds on demand."

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In order to meet the changing needs of investors, J.P. Morgan Asset Management's China joint venture, China International Fund Management (CIFM) has launched a same day liquidity fund, the first of its kind in the China market. "A product such as this hasn't existed before due to the infancy of the market," says Cheah. "Even today, MMFs are still regarded as equity style funds, which are more common in the local market."

## Corporate usage

"Corporates have been slowly but surely moving towards MMFs as the market has developed," says Cheah. Currently, the primary users are multinationals that are familiar with the products in their home markets. However, a growing number of local Chinese corporates are also turning to MMFs. "Corporates in China are beginning to accumulate more cash and are assessing their own investment policy, which is starting to include MMFs."

Moreover, Cheah indicates that corporates are moving away from alternative investment products in China, which offer greater yield but also greater risk. "Many companies are moving to a more conservative yield strategy as there is a growing awareness of the importance of risk versus return. As China and its businesses continue to grow, I expect this trend to accelerate and for the importance of MMFs to increase."

# Treasurers play a role in addressing disaster risk

Managing risk is at the heart of what the treasury function is all about. But while most treasurers devote significant time and energy to managing threats around interest rates or foreign exchange, reducing the risk of natural disasters – not just to the company, but globally – is unlikely to figure very prominently in the treasurer's priority list. After all, what has the private sector got to do with reducing disaster risk in the wider world? A great deal, apparently. Indeed, the United Nations (UN) feels it is virtually impossible to address the problem of disaster risk without the help of business. "Economic losses from disasters are out of control and can only be reduced in partnership with the private sector," according to Ban Ki-moon, Secretary-General of the UN.

Now the leaders of an initiative aimed at tackling disaster risk are calling out to corporates for their participation. R!SE is an initiative with the overall aim of ultimately making all investments risk-sensitive, by utilising both public and private sector resources and expertise to reduce disaster risk around the world. What's more, treasurers are a community that R!SE is looking to reach out to.

Launched in May 2014, R!SE has the ambitious (some would say impossible) objective of 'making investments risk sensitive' by 2020. Scott Williams, a Director at PwC who is one of the lead coordinators of the initiatives, accepts the timeline is very ambitious but counters that drastic action is necessary. "We had to set out with extraordinary ambition because the data, the currently largely invisible risk information, is showing us that if we continue to construct risk at the rate that we are, and at an accelerating rate, in terms of large infrastructure and other developments in emerging and developing fast-growth economies, then it may be too late by 2020. We have to bend the curve well and truly by 2020."

## Corporate impact

But, some corporates might still be asking, why should we be concerned with disaster risk? They should think back to Hurricane Sandy, which, in addition to killing at least 286 people and causing almost $70 billion of damage, also forced the closure of the New York Stock Exchange and NASDAQ. "It's fair to say we have been very lucky with the type of disasters that have happened – if Superstorm Sandy had continued at hurricane strength three or four as it made landfall and hit central New York with that sort of strength, then Wall Street could have been shut down for three or four months instead of two days."

He concludes that corporates need to wake up to the topic sooner rather than later. "The latent conditions for catastrophic disruption are already built in to our system. The fundamental mispricing of risk is endemic within our economic and financial systems because there is a disconnection between the price setting mechanism in those systems and the physical reality described by science." ■

**Longer versions of these articles are available at treasurytoday.com/treasury-insights**


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# This much I know

## Dawn Chua

### Head of Capital and Treasury

### What is the best piece of advice that you have been given in your career so far?

Very early in my career I was told that always having an eagerness to learn, a disciplined approach to doing things and working hard to follow things through, are very important qualities. Only through these can you gain the experience and exposure you need to progress. I have applied these qualities throughout my career, but I will leave the judgement on whether these are the right qualities for others to decide! In all seriousness, I truly believe that one should be willing to take on new tasks because you never know how doing them might enhance your skillset. I would encourage women to be forthcoming in this respect and to have more confidence and self-belief to take on new challenges.

### How much opportunity is there for career progression within your role?

Over the past couple of years there has been a distinct focus on increasing awareness around diversity of all types, including gender. There are initiatives to encourage females to enter the boardroom of companies and create more opportunity and motivation for women to succeed.

### Which regulatory initiative is currently the biggest concern for your treasury department?

Treasury always has to be aware of evolving regulations, and I wouldn't say that one is of particular concern because there are many that we need to comply with. It is a very dynamic area and one that has to be carefully managed; and, if necessary, changes have to be made in order to meet the regulatory requirements. It is a challenge but it is also something that makes the treasury role more interesting. Working in treasury means being able to adapt to the ever-changing environment and adopt it accordingly.

### If there was one tool that could help you to be an even better corporate treasurer, what would it be?

A magic lamp that would allow me to resolve all treasury issues instantaneously! But while I have been waiting for this magic to happen, technology has had an increasingly vital role to play in the treasury space and this will continue, allowing treasury to further enhance front, middle and back office operational efficiency. These developments have allowed for enhanced risk management and allowed the treasurer to spend more time engaging the business partners. A few hours extra in the day to balance everything would also be lovely.

### Finally, what is your motto in life, and your greatest inspiration?

A quote that has stuck with me since my teenage years is that 'a thought that one has will eventually become an action and through this action it will become habit. This habit will then shape our character which will then define our destiny.' I still believe in these four elements and therefore focus on being positive in everything I do.

I am inspired by continuously driving change in the treasury function, and seeing the department become an increasingly strategic player in the ecosystem of the organisation. For this to happen, we need people who are truly passionate about treasury to join the profession because being passionate about what you do brings happiness and motivation. Hopefully, this positive vibe can be caught on by others throughout the industry.

"Technology has had an increasingly vital role to play in the treasury space and this will continue, allowing treasury to further enhance front, middle and back office operational efficiency."

**ON THE WEB**

To read all the interviews in this series go to **treasurytoday.com/women-in-treasury**

Dawn Chua, who is Head of Capital and Treasury at the Singapore Exchange, entered the treasury profession following graduation from University. She found a job advertisement for a Treasury Executive role, and decided to take the plunge. Dawn quickly began to see how dynamic and challenging corporate treasury could be. "It was at this point I decided that this was the career path I wanted to follow," she says. "The dynamism and the challenge that the role presented ticked all the boxes for me and it was something that I became passionate about doing." Since then, she has never looked back and thoroughly enjoys her work.

This passion for the profession has seen Dawn stay in treasury her entire career and experience all the challenges it has to offer. "I have been very lucky in my roles and have been exposed to treasury on both the asset and liability front," she says. From this Dawn believes that she has acquired important treasury skills to give her a more holistic view of the treasury function, allowing her to develop a methodical approach to treasury tasks that offer benefits to the organisation. Very importantly, she is grateful for the opportunities that were given to her by the companies that she used to work for. In addition, she is also very thankful for the support that she has received from her external business counterparts, such as bankers and lawyers who have been very supportive throughout her time at the different organisations that she has been with.

In Dawn's view, being a value-add business partner is key and to achieve this, the treasury must operate harmoniously alongside the rest of the business. "Treasury is deeply integrated with the business in both operations and in facilitating any organic or inorganic growth plans that the organisation may have," says Dawn. She is acutely aware however that the importance of treasury sometimes needs to be re-emphasised to the C-suite. "Senior management are very busy with macro-level strategy and planning; sometimes they need a gentle reminder of the key role the treasury plays either from the department itself or from an outside source such as Treasury Today Asia."

Despite her experience Dawn is still very aware that in treasury no single person knows everything and she therefore has a strong belief in the importance of teamwork. "Working together in a team complements the individual strengths that each person brings to the department and allows us to develop more innovative solutions for the organisation," she says. For Dawn, treating people as individuals is vital, be they male or female. "In business, just as in everyday life, people shouldn't be seen as male or female – they should be seen as an individual and treated accordingly."

However, some sections of the business world, in Dawn's opinion, need to embrace modern ideas regarding balancing professional life and family life for females. "From my observations and conversations with friends and counterparts, there is a subtle and implicit expectation for women to be able to oversee their family life on top of their work responsibilities," she says. "Both men and women only have 24 hours in the day but in some cases women are implicitly expected to do more on the family front." What can be done to overcome this issue? "I believe that the business world needs to acknowledge that this is an issue so that it can then be managed accordingly," she says.

Dawn is already seeing some progress being made with a handful of companies offering flexible working hours and has been further encouraged by recent developments in Singapore, that have seen the creation of a Diversity Action Committee, a group tasked with building the representation of women in the boardroom. "SGX is embracing diversity, and our CEO Magnus Bocker is the chair of the committee," she says.

Indeed, throughout her career Dawn has already seen a growth in the presence of females in the industry. "In my current company I see a more balanced mixture of males and females and also when I go to events I see many more women than I did when I began my career," she says. True diversity is therefore an achievable goal in Dawn's opinion. "It will take a conscious effort from both the individuals in the workplace and the corporate world," she says. "But I adopt the philosophy that positive thoughts will prevail and I therefore believe this will happen in time." ■

Dawn Chua is the Head of Capital and Treasury of SGX. She is responsible for the effective management of the capital of SGX and managing Treasury strategies and policies. She has more than ten years experience in various Treasury functions spanning across the Manufacturing, Property, IT and Investment industries before she joined SGX.

Dawn holds a Bachelor of Business degree (Honours) from NTU and has obtained ACCA certification.

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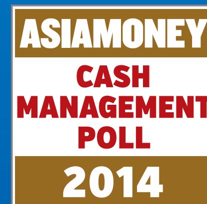


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# Best practice: IPOs

*With Alibaba making the headlines following their IPO, what do other companies who wish to follow suit need to know? Also what best practice tips can readers share on how the treasury function can add value to this process?*

## Max Loh, ASEAN and Singapore Managing Partner, EY:

The success of the Alibaba IPO is largely due to the potential that the company has and investors' appreciation of this. It was therefore a very considered choice for Alibaba to list in the US, as this market is home to many sophisticated investors who understand the complex business model of Alibaba.

Asian companies tend to list in either their home markets or two of the region's more established exchanges, namely Hong Kong and Singapore. Asian companies tend to do that as investors in the home or regional markets will be familiar with the company, its offerings and brand, and this helps in achieving better valuations. This is especially true for companies in the retail, consumer products and services sectors. The US, on the other hand, is seen by many as a preferred destination for e-commerce and technology companies, given greater investor knowledge and appreciation.

> To ensure the success of an IPO, the treasury function should be at the fore of the process alongside the business, given its understanding of the company's operations and how much cash it should look to raise and how it is to be deployed.

There are many other factors which influence the decision of where a company can or should list, as each exchange and domain market has its own differing set of criteria, regulations, adopted accounting standards and laws. It was widely reported that another key reason for Alibaba's listing in the US was the dual share structure the market offered. Otherwise, the differences are quite subtle and companies will often be flexible enough to accommodate and comply with the rules of the exchange of its choice.

Across Asia Pacific, countries are looking to build up their exchanges. Locations like Hong Kong and Singapore currently have the advantage of being international financial centres, with lots of depth and liquidity. They are also popular with foreign companies that view North Asia and South East Asia respectively as their key markets. Other exchanges in the region are more focused on attracting domestic companies.

### Role of the treasury

To ensure the success of an IPO, the treasury function should be at the fore of the process alongside the business, given its understanding of the company's operations and how much cash it should look to raise and how it is to be deployed.

> Following the IPO, the role of the treasury function shifts back to its more traditional role of investment appraisals and managing cash flow, liquidity and financial risks. This already vital function becomes more important as the success of the IPO will ultimately be judged by the financial metrics of the company.

In presenting the IPO story to investors, it is important to demonstrate how the proceeds raised will be put to good use. The treasury function has a key role in explaining this. During the IPO process, the treasury also needs to help build investor confidence by demonstrating that the company is adept at making both returns on their investment and managing financial risks.

Following the IPO, the role of the treasury function shifts back to its more traditional role of investment appraisals and managing cash flow, liquidity and financial risks. This already vital function becomes more important as the success of the IPO will ultimately be judged by the financial metrics of the company. Also, with the company now being public-listed, accountability, governance and transparency become more crucial and accordingly, the treasury function must ensure it steps up to the mark in this regard.

### Matt Emsley, Partner, Corporate, Herbert Smith Freehills:

Alibaba hit the headlines following its recent IPO, not just because of its large size, but because it decided to list in the US and not Hong Kong. Traditionally, Chinese companies see Hong Kong as the gateway to global capital markets and look to the Hong Kong market when launching an IPO. However, Alibaba went against this trend and highlighted reasons why some corporates from China may look to the US and not Hong Kong.

The primary reason for Alibaba's listing in the US rather than Hong Kong was because of the management and voting structure that Alibaba adopted. The current regulations in Hong Kong apply a one share, one vote policy. However, Alibaba wanted a structure that gave greater voting power to the key management, one that is permitted in the US market. Indeed, similar structures have been adopted by a number of Chinese companies seeking listing in the US, and in particular internet companies, in recent times.

The public debate in respect of the one share, one vote policy as a result of Alibaba's decision to list in the US has seen the Hong Kong Stock Exchange issue a conceptual consultation with the market, seeking views regarding the one share, one vote concept. The Hong Kong Stock Exchange has also, in recent years, clarified its approach to the listing of companies adopting variable interest (VIE) structures where the companies are in restricted industries. Such a structure allows the channelling of the economic benefits from the business to the listed group by way of contractual arrangements with a third party who actually owns the business and assets, for businesses where foreign ownership of the business is restricted under Chinese law. As a result, there have been a number of Hong Kong listings of Chinese internet businesses in recent years, where previously they may have sought a listing in the US.

One of the key requirements for a listing on the Main Board of the Hong Kong Stock Exchange is compliance with one of the three alternative financial tests. These require the applicant to meet specified thresholds for profit, revenue and market capitalisation or revenue, cash flow and market capitalisation. Companies are also generally required to have management and ownership continuity for the most recent three financial years and one year, respectively.

> Once the IPO is complete, treasury will finally be required to manage the FX risk and regulations when repatriating its proceeds. In order to carry out these roles efficiently, treasury should be introduced to the process as soon as possible.

Other items to be aware of during the listing process in Hong Kong are the Hong Kong regulators' expectations of sponsors and the level of due-diligence they conduct, that have become stricter since regulatory changes implemented in the last year. A further regulatory change was the adoption of a requirement that, with effect from April 2014, the application proof of the prospectus filed with the Hong Kong Stock Exchange be made publicly available on the Hong Kong Stock Exchange website upon filing. There were concerns that this may make the Hong Kong Stock Exchange more unattractive to some companies, though the market has quickly adapted to this requirement.

Outside of Hong Kong, Singapore has been a popular IPO destination over the last 12 months and has seen some large listings. The market receives a lot of interest from South East Asia based companies, while Chinese companies have tended to generally look to Hong Kong. This is primarily due to market valuation and familiarity of investors there with Chinese companies.

The treasury can have a key role to play during an IPO, especially around restructuring the organisation. For example, Chinese companies listing in Hong Kong will often reorganise their shareholding structure in advance of seeking a listing so that they are held by an offshore entity subject to compliance with PRC regulatory requirements. As part of this reorganisation, financing will often be required to fund the reorganisation that the treasury will manage, with such funding often provided through pre-IPO investments. Also, in Hong Kong the organisation is required to be financially independent of its controlling shareholders. To achieve this the treasury may need to restructure any loans from shareholders and bank loans where shareholders have provided guarantees in preparation for listing. The negotiations with the banks typically either remove shareholder guarantees completely or otherwise replace the shareholder guarantees upon listing with a guarantee from the listing vehicle. Once the IPO is complete, treasury will finally be required to manage the FX risk and regulations when repatriating its proceeds. In order to carry out these roles efficiently, treasury should be introduced to the process as soon as possible. ■

## The next question:

"The war for talent continues in Asia. What innovative approaches are treasury departments in the region taking to attract and retain talented individuals? Also, how can in-house talent be developed to add more value to the company?"

Please send your comments and responses to **qa@treasurytoday.com**

# APAC treasury in 2015: all change?

*Over the next 12 months, what will be the defining themes and projects for treasurers operating in the APAC region? Will we see treasury departments across the region increase in sophistication and utilise new technology and structures to reap benefits, for example? Or will regulation and the tough economic environment continue to stunt innovation? We talk to a handful of industry experts to get their take on these issues and reveal what your peers truly consider to be top priorities for the year ahead.*

The start of a new calendar year always comes with a wave of optimism and enthusiasm. In recent years, however, this has often been quickly extinguished as the reality of global conditions strikes home and corporates are faced with new and increasingly difficult challenges. Indeed, 2014 was full of economic, infrastructural and political developments that stretched the patience of treasurers in APAC.

One of the big stories was the slowdown in economic growth across many of the region's key economies, not least China and India. In China for example, the forecasted 7.4% growth rate, while still impressive, has raised certain questions around the reform agenda and its continued trajectory. With a geopolitical environment that looks increasingly uncertain, it's not difficult to imagine treasurers, ever watchful for signs of heightened volatility in financial markets, heading into 2015 with a slight sense of trepidation.

"I think the macroeconomic issues are the ones that most treasurers will wake up thinking about on 1st January," says Paul Taylor, Regional Sales Head, GTS EMEA at Bank of America Merrill Lynch. "We've heard talk in recent weeks about a cooling in the global economy; we've seen what's happened to the price of oil and what that has done to currencies globally, which has in turn had a knock-on impact upon currency valuations. I don't think anybody can ignore what is happening on that level at the moment."

Another topic that treasurers will no doubt be focused on as we head in to 2015 is the negative impact that regulation might have on their operations – and ultimately, on the company's bottom line. In APAC, the headache of regulation is of course exacerbated by the non-uniform approach across the region. There is hope, however, that plans to create an integrated ASEAN Economic Community (AEC) by the end of 2015 will solve this issue for a large portion of the region.

The creation of the AEC should also provide new impetus to trade among and with ASEAN communities, which can only be a positive development in what is proving to be a rather sluggish time for global trade (read more about this on page 28 of this issue where we look in depth at the new trade paradigm in ASEAN.)

## What matters to you?

Away from the macro view, treasurers will naturally be focused on making their day-to-day operations run as smoothly as

### Table 1

| Rank | Treasury department priorities 2013 | Treasury department priorities 2014 |
|---|---|---|
| 1. | Cash management/cash pooling structure. | Bank relationships and banking group organisation. |
| 2. | Working capital management. | Funding/credit lines. |
| 3. | Balance sheet optimisation. | Cash management/cash pooling structures. |
| 4. | Funding/credit lines. | Working capital management. |
| 5. | Foreign exchange risk management. | Improving cash flow forecasting. |
| 6. | Improving cash flow forecasting. | Balance sheet optimisation. |
| 7. | Compliance and regulations. | Foreign exchange risk management. |
| 8. | Banking relationships and banking group organisation. | Security and fraud. |
| 9. | Technology and systems. | Compliance and regulations. |
| 10. | Establishing a shared services centre (SSC). | Counterparty risk. |

*Source: Treasury Today Asia Pacific Corporate Treasury Benchmarking Study 2014*

possible. Nowhere is this more evident than in the results of the latest Treasury Today Asia Pacific Corporate Treasury Benchmarking Study, where treasurers in the region were asked to rank their treasury department priorities for 2015, with 1 being the most important (see Table 1).

## Cash and liquidity concerns

Although the top issues remain largely the same as the previous year's results, with an inevitable focus on working capital, funding and cash management, there are a number of nuances worth highlighting. For instance, does the fact that 'cash management/cash pooling structures' have dropped from being the top priority in the 2013 study to the third priority in the 2014 study reflect the fact that regulators in the region – notably China – have made significant moves to improve cross-border liquidity and therefore this will not be such an issue in 2015?

According to the experts, the answer is 'yes and no'. First of all, "It is important to note that any regulatory changes that have taken place at the end of 2014 in China will not truly be actioned by corporates until 2015," says Mahesh Kini, Asia Pacific Head of Cash Management Corporates at Deutsche Bank. "The move to allow cross-border RMB sweeping is a good example: all of the activity around designing and implementing solutions on the back of this will continue into 2015. In fact, the majority of the pipeline will be Q1 and Q2 2015, so this will be a large area of focus."

And as Amol Gupte, Region Head, Asia Pacific, Citi Transaction Services, adds: "When it comes to trapped cash, much progress has certainly been made by the regulators in China, but there is still a lot more that needs to happen before cash can flow freely across borders. For example, CNY and CNH are different currencies with different rates and yield curves, and the extent to which corporates can borrow offshore to name a few, these need to be standardised before we can truly see the end of trapped cash."

## Banking on change

Elsewhere, it is interesting to see that 'bank relationships' has jumped from being the eighth concern in 2013 to the top priority in 2014 – even above 'funding/credit lines'. This suggests that corporates in the region are now starting to be more strategic about their bank relationships, and having more open conversations around wallet share. In fact, 40% of respondents to the 2014 study said that their lead cash management bank receives between 30-50% of their total cash management wallet.

That said, we cannot ignore the impact – whether direct or indirect – of regulation on banking relationships. According to a speech at a recent conference by Alan Verschoyle-King, Executive Vice President and Global Head of Sales and Client Management for BNY Mellon's Treasury Services, "Global regulatory reform continues to be the largest driver of change and concern within Asia's banking industry, with many banks struggling to understand the impact of and meet the new requirements."

Moreover, it is not just APAC-specific regulations that matter. "Given the size and global reach of the US economy, US regulations, in particular OFAC (The Office of Foreign Assets Control), Dodd-Frank and FATCA (The Foreign Account Tax Compliance Act), have the most substantial direct impact on Asian bank operations, business development and their working relationship with partnership banks," he said.

### Top seven barriers to growth impacting Asia's banking sector in 2015

1. Information management and reporting challenges under new US regulations.
2. Regional market fragmentation.
3. Insufficient resources to meet client demand.
4. Balance sheet size of local banks.
5. Political tension within Asia.
6. Pace of global economic recovery.
7. Continuing concerns about China's outlook.

*Source: Verschoyle-King, BNY Mellon Treasury Services*

So how is this impacting the treasurer? Well, "To meet the new standards, banks are building higher capital and liquidity buffers, as well as re-evaluating their business models with many institutions choosing to focus on their core strengths and key markets. Others are under intense pressure to consolidate and streamline to position for future growth and, in some cases, survive. Whilst consolidation presents opportunities for stronger regional banks to emerge, the reality is many local banks within Asia Pacific remain too small to effectively compete on a local, regional or global scale."

In short, treasurers are having to carefully re-think their bank allegiances in light of a number of banks retrenching because of regulatory pressures. Domestic and regional legacy relationships are also being reviewed as these might not represent the optimal long-term play in the new regulatory environment, although this largely depends on each company's situation of course.

## Containing risk, leveraging technology

Going back to the treasury priorities list, the increased focus on risk is also worthy of note. Counterparty risk did not even feature in the 2013 list, nor did security and fraud. Both have risen up the corporate agenda, thanks to headline-hitting scandals. Furthermore, there is a growing global trend for both regulators and consumers to hold corporates accountable for the actions of the third parties that they choose to interact with – whether these be customers, suppliers, banks, or vendors.

In addition to introducing stricter due diligence processes and internal controls, many companies are revisiting their technology infrastructure – not only to plug any potential security gaps but also to leverage the benefits of straight through processing, analytical programmes, best execution platforms and trends such as big data.

"We believe that ongoing technological innovation and digitisation will be essential to help clients better adapt their operating models to the current trends and shifting market demands. The focus will be on developing treasury management e-solutions that deliver impactful results – making our products simpler, more convenient and flexible, and allowing companies to have improved visibility over their

treasury flows in ways that were not previously possible," notes Citi's Gupte.

It's about enabling treasurers to become much more efficient and getting instant access to information, as well as how to get better insights of data analytics to make better informed decisions, he explains.

### Table 2

| Rank | Technology issues 2014 |
|---|---|
| 1. | Cash flow forecasting solutions. |
| 2. | Improving visibility over the company's cash. |
| 3. | Choosing a Treasury Management System (TMS)/Corporate to bank connectivity/cash management portals. |
| 4. | FX portals. |
| 5. | Bank portals. |
| 6. | Migration from spreadsheets. |
| 7. | Choosing an Enterprise Resource Planning (ERP) system. |
| 8. | eBAM. |
| 9. | Bank dashboards. |
| 10. | Standards and formats. |
| 11. | Mobile banking. |
| 12. | Supply chain finance portals. |
| 13. | Big data. |
| 14. | Cloud technology. |
| 15. | Software-as-a-service (SaaS). |

*Source: Treasury Today Asia Pacific Corporate Treasury Benchmarking Study 2014*

It is not only treasurers who are taking advantage of evolving technology though – regional payments authorities and governments are too. "On the subject of technology, the region is migrating from paper to electronic payments," says Kini. "Corporates are increasingly transitioning their payment ecosystem to 'pay electronic' – even in countries that tend to use cheques. This is riding on the back of the new payments infrastructure that countries are introducing."

Despite these developments, it is worth noting that many APAC countries are still cash and cheque focused – India, Indonesia and Thailand are prime examples here. Currently, electronic payments and collections can only be carried out effectively in countries such as Japan, Singapore and Hong Kong. This is primarily because the government in these countries promote e-payments and have spent a lot of money developing their payments systems.

For treasurers, the benefits of this innovation will be far-reaching. As Kini notes: "The systems can now carry information that helps to identify who is paying, which then helps to reconcile at an invoice level. We believe that e-invoicing will therefore be an increasing priority for the finance function in 2015 and beyond. On the back of this, we are likely to see more 24/7 real-time clearing systems being built too."

## Shared service centre shifts

Another key trend in 2015 will be the continued march towards centralisation – and the establishment of shared service centres (SSCs) says Gupte. "Centralisation remains a key priority for corporates in the APAC region. As we see it, there are four stages to centralisation: operations; standardisation; balance sheet centralisation (funding centrally/pooling) and finally, the in-house bank. The majority of our clients are at the 'centralising balance sheet' stage and are looking to implement regional pooling structures and SSCs," he comments.

And some interesting geographical dynamics are happening in that SSC space. "With ASEAN Economic Community 2015 plans coming into effect, corporates will be looking for opportunities in the region, such as the relaxation of the rules around the movement of liquidity. We will also likely see certain ASEAN countries position themselves as sophisticated hubs to host treasury centres – such as Malaysia– or even to host cross-border structures, something that Hong Kong and Singapore have traditionally dominated," Kini notes.

"The Philippines is one place to watch," he adds. "It is an investment grade country, with a young, skilled population. It will increasingly develop into a business process outsourcing (BPO) location and we will see more and more corporates use it as an ASEAN hub."

Elsewhere, there has been a trend developing towards the near-shoring of SSCs by European and US MNCs. Indeed, a number of multinational companies are now looking to move their shared service centre (SSC) or treasury centre back to Europe or the US from China. The increase in cost of living and labour can be seen as two primary drivers of this trend.

## Embracing change

All of this gives treasurers much food for thought throughout the next 12 months but, unlike previous years, the tone heading into 2015 is largely positive. While the year ahead of us will undoubtedly challenge the profession at one point or another, the collaborative and more transparent environment that we are now operating in promotes proactivity.

So, rather than simply doing the minimum to meet necessary compliance project deadlines, or to ensure your data is secure, why not use such triggers as an incentive to review and improve existing practices, processes and policies instead. After all, being open to change is the best way to stay ahead. ■

# The world of private placements

*If governments want to help the flow of credit to mid-market companies, they need look no further than the US private placement (PP) market for inspiration. In the US, companies have long benefited from a PP market that is both large and liquid. Can a similar market emerge in Europe, and what are the private placement options for corporates in Asia?*

In a year where bank lending once again contracted and the ultra-low rate environment pushed investors still further out on the yield curve, it seemed inevitable that private placements would be one of the hot topics of 2014. And so it proved.

Corporates, wherever they are in the world, now need new options when it comes to financing the business. Accordingly, those companies for whom the public debt capital markets are not a feasible option, the private placement markets are becoming an increasingly popular alternative source of capital.

The trend can be seen worldwide although, as we will see, there are some important differences between, and even within, regions such as Asia and Western Europe.

## A turbulent decade

Asian capital market issuance is growing rapidly. Regulation has been one of the drivers. In recent years, there have been efforts in the region to improve access to public capital markets through the simplification of legal documentation and the investor base has widened substantially.

"Traditionally Asia has been a bit of bank loan market," says Vijay Chandler, Executive Director of the Asia Securities Industry and Financial Markets Association (ASIFMA). The bond market is typically smaller relative to the loan market, at least in terms of the total outstanding. Although this continues to be the case, there are signs that change is afoot.

"What has happened in recent years is that the banks have been pulling back from the syndicated loans market, largely as a result of the Basel III guidelines and other regulatory pressures. Bond issuance has really grown, as a result."

For a while, this proved a happy arrangement for all concerned. Investors bought up all the debt they could, providing companies with much needed financing, and secured very attractive yields in return.

There has been a change, also, in the type of debt being issued on Asia's capital markets. About a decade ago, private placements in Asia were – with the benefit of hindsight – moving into bubble territory. Western hedge and private-equity funds came to take advantage of the region's burgeoning growth, but soon found that there was little to purchase on Asia's underdeveloped capital markets. Some corporates in Asia, meanwhile, faced obstacles to issuing on the public capital markets. Thus each party ended up solving the other's problem, and the issuance of dollar-denominated debt boomed.

"This was before the financial crisis, remember, so everyone was gung-ho. You had the likes of Indonesian mining companies coming to the market looking for bridge finance prior to an initial public offering (IPO) or a public bond issue, and we had all these investors looking to invest in corporate bonds at a time when the public markets were pretty much full," notes Chandler.

For a while, this proved a happy arrangement for all concerned. Investors bought up all the debt they could, providing companies with much needed financing, and secured very attractive yields in return. Then, in the autumn of 2008, the music finally stopped.

According to Chandler, a very large percentage of the deals struck during those heady pre-crisis days had to be refinanced. "A lot of them were very short-tenor private transactions," says Chandler. "That meant that if your company's deal was priced in 2005-06 – or even as late as 2007 – by 2010, you needed to refinance either through an IPO or some sort of bond offering, both markets which were, of course, closed by that time."

The subsequent freeze in capital market lending didn't last long, however. Debts were successfully restructured, and sovereign wealth funds took up some of the remaining slack and now, remarkably, the capital markets are once again growing at a rapid pace, although the bulk of what is being issued, this time, is denominated in local currencies, not USD.

## Asia today

Asia is not a homogenous region, by any means. The split between public and private issuance still varies considerably across jurisdictions, therefore. Public placements now account for the lion's share of corporate bond issuance in a number of Asian countries such as China, Malaysia, the Philippines and South Korea. However, in other markets, like India, private placements have remained the primary form of bond issuance representing more than 80% of the corporate bonds issued domestically in 2012 and 2013.

The regional disparities are, of course, all a matter of pricing. "In many Asian markets, the costs of public issuance still exceeds those associated with private placement by a multiple," says Hannah Levinger, Analyst, Global Risk Analysis, at Deutsche Bank. "As a result, private placements are still a common issuance regime. Companies can tap longer-term financing with a few selected investors while saving on regulatory costs and requirements and avoiding lengthy and burdensome procedures."

Such features make private placements a very attractive proposition for some businesses, particularly smaller, fast-growing companies who need capital to finance their growth plans. Recognising this there have been initiatives in some countries, most notably China where obtaining capital is one of the biggest problems faced by SMEs, to help smaller companies execute private placements. A pilot initiative for SME bonds was launched by the Chinese regulator in 2012, which was followed up in 2013 by an announcement to extend private issuance to a wider region and companies registered at the "new third board" a nationwide share transfer platform for non-listed companies.

"The move was seen as both a measure to stimulate the development of the corporate bond market and reduce SME's reliance on bank loans," says Levinger. "As a result, private placements have seen steady growth in Asia."

## Luxury or necessity?

We have also seen a growing level of interest in private placements from companies in Europe – and similar initiatives encouraging firms to reduce their reliance on bank loans.

In autumn 2014, private placements – and specifically the question of whether a European PP market to rival the US will develop – was one of the most keenly discussed topics at the Loan Market Association's (LMA) annual Syndicated Loans Conference in London. On that question, the general sentiment was optimistic. A straw poll of the 850 delegates in attendance found that a sizable majority (78%) believe that such a market will become established within the next decade. In addition, just under half (49%) indicated their conviction that we will see one emerge within as little as five years.

Earlier in the session, a panel of fixed-income investors were asked if a Europe-wide market for private placements is even needed. After all, companies today can choose to issue a private placement in the US market denominated in dollars, before converting back into euros. In fact, a lot of companies these days are even finding investors in the US willing to lend to them in euros, thereby saving them the bother of executing the conversion themselves. Companies might also find the credit they need in one of Europe's local markets – the German Schuldschein sector, and the nascent French and UK markets – each of which has seen growing international interest from both investors and issuers in recent years.

However, the ability to issue private placements in a pan-European market would be a big advantage for borrowers, the panel insisted. "It would be much easier for companies to borrow locally in local currency," Calum Macphail, Head of Corporate Private Placements at M&G Investments, told

delegates. Investors, he explained, tend to extend their willingness to lend right across the yield curve when dealing with familiar, local companies.

A European market would also simplify the process enormously, especially on the legal side of things, he added. "If borrowers have the ability to use documentation that is familiar and consistent and cheapens the process – that has got to be beneficial as well."

> "Clearly there are challenges, but we've got to work together to overcome these challenges and help develop and grow the market,"
>
> Richard Waddington, Head of Loan Sales, Commerzbank

Investors would stand to benefit too, as Emmanuelle Nasse Bridier, Chief Credit Officer at the AXA Group, pointed out. It's no secret that institutional investors have felt the need to be a bit more adventurous with their portfolios of late. In the current ultra-low yield market, insurance and pension funds have found it all but necessary to diversify into new asset classes to secure some return on the amount of liquidity they are now holding. Developing a pan-European PP market would certainly help them in that respect.

"For us insurance companies a European private placements market would offer new opportunities that are not available on the public market, most of which are well organised and strongly performing corporates," she noted. "We are looking for new investment opportunities with that type of company."

## The need for consistency

Having agreed unanimously that building a private placement market in Europe would be a positive step, the panel then moved on to address the barriers that need to be overcome before that can become a reality. When the question was put to delegates earlier the answer was clear. Just under half (47%) said that the main thing that Europe needed to begin competing on equal terms with the USPP market was greater standardisation, particularly with respect to the legal documentation used across various jurisdictions.

Eliminating such inconsistencies is something that the LMA has itself taken a leading role in. In January 2014, the group announced that it is working with banks and law firms on developing a standardised template for use in private placement transactions. This is just the beginning, however; the investors on the panel were keen to emphasise that much more progress is needed in this space if Europe is ever to rival the USPP market. "Regulation is very different around Europe when it comes to credit markets," AXA Group's Bridier said. "I think if we had a European framework around investment regulation that would solve a lot of the problem."

## Come together

If the industry now joins forces to iron out the differences at local level then the liquidity should soon follow, the panel concurred. "We are seeing investors become increasingly interested in European private placements markets," asserted Richard Waddington, Head of Loan Sales at Commerzbank. "Clearly there are challenges, but we've got to work together to overcome these challenges and help develop and grow the market," he added. "There is most certainly demand from issuers, but it is about trying to match that demand with investor's requirements."

Achieving that match may take some time, but it is not beyond the industry's reach. In the end the panel arrived at the consensus that a pan-European market will emerge in time, albeit a segmented one. That is not as contradictory as it might first seem, M&G Investments' Macphail explained. If a company wants to raise a relatively small amount of funding – say €10m – then it may still be best served by its local market. But there are, of course, no shortage of companies who have larger requirements and, for them, tapping into larger pools of liquidity on a pan-European basis would be the more ideal option.

"If we are talking about a market for everyone, not just the happy few, then you need to have a different response depending on the requirement," he said. "For a small bilateral loan then local is great. However, we also need to cater for the needs of those larger companies who want to borrow Europe-wide. I think the market is flexible enough to accommodate both." ■

# Riding the waves of treasury

**Steven Wong**
Group Treasurer

With over three decades' experience in the shipping and logistics industry, Steven Wong, Group Treasurer, Neptune Orient Lines Group, has guided the company through quite a few ups and downs in a cyclical sector. In more recent years, Wong has applied his knowledge and understanding of philosophy to make some important changes not only to the treasury but to the business.

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*Singapore-based Neptune Orient Lines Group is one of the region's best-known names in transportation and logistics, with more than 11,000 staff across 331 offices in 112 countries. The company's brands include APL, the world's seventh-largest container carrier, and APL logistics, a global leader in providing supply chain management services. Originally formed by the Singaporean government to help develop the economy, the company now transports over three million FEUs (40-foot container equivalent units) of cargo.*

Having worked in the treasury department at Neptune Orient Lines (NOL) for 31 years, Group Treasurer Steven Wong is a 'walking historian for the company'. "To discuss my entire career it may take one day, not an hour," jokes Wong. Indeed, throughout his career, Wong has had to ride the waves of treasury in the notoriously cyclical shipping and logistics industry, navigate through multiple financial crises and also adapt to the changes that have transformed the treasury

profession. Drawing from his appreciation of history and philosophy, Wong applied some of these principles to guide the NOL treasury department throughout his tenure.

Following graduation from the National University of Singapore in 1983, where he obtained a degree in business administration, Wong joined NOL as a management trainee. "In this role I was meant to be given exposure to all areas of the organisation," says Wong. "However, I stayed on in my first rotation at the treasury department because the challenges were multi-faceted and interesting." Looking back, this was a blessing in disguise. "Although I didn't get the exposure to the other areas of business like I should have, I was put on a path within treasury that has allowed me to learn about all aspects of the business, rise up the ladder and head the department for nearly 20 years," recalls Wong. "This may not have been the case had I moved to the next rotation as first anticipated."

Recalling his early years in treasury, Wong is thankful to the people around him who helped him develop. "Back when I was at university, the treasury function was in its nascent stage and there was no treasury course. The closest I came to looking at treasury was learning about foreign exchange," recalls Wong. Supported by those around him Wong was able to learn on the job, and learning is something that still resonates within him today. "Thanks to spending my entire career in treasury I now have a deep knowledge of the profession," says Wong. "But I am never able to rest on my laurels as it is constantly evolving and there are always new things that need to be considered." For Wong this is part of the allure of the profession. "I can never say that I am bored – even half an hour ago I was still learning from my conversations with my bankers and I am sure tomorrow I will learn something new as well."

## Captain of the treasury

Wong manages an 11-strong treasury team based in Singapore, which is split into three areas: cash management, risk management and financing. The most important aspect of their daily work is the management of liquidity, what he calls 'the bloodstream of the business.' "NOL's business is capital-intensive and it is therefore vital that I don't make any errors in this department or have a situation where we can't meet our business requirements."

To ensure that the treasury is able to meet its expectations, Wong believes it is vital that treasury and finance are integrated with the rest of the business. "To achieve this, treasury and finance must be a cohesive team," says Wong. "One of the key roles of the team is to understand the company's vision, business strategies and plan the cash flow accordingly. It is important that we work together and don't ask the same questions and duplicate work. Thankfully at NOL we are like a big family and we work very closely together."

The reach of the treasury also extends to the boardroom. "Treasury issues are discussed in each board meeting (there are four each year)," says Wong. "We also have one sub-board meeting twice a year that focuses solely on enterprise risk management." In these meetings, treasury issues such as liquidity and counterparty risk are discussed in detail. "The board pays particular attention to this area so it is my role to ensure that they, and other business partners, are informed and understand the various risks and formulate the right policies accordingly." For Wong, it is important to have a clear business strategy supplemented by a clear treasury strategy to ensure that the company moves in the right direction.

## The philosophical approach

When building the treasury strategy, Wong calls on his many years' worth of experience, as well as his philosophical approach. "A lot of my time is spent thinking through problems and planning how these can be resolved," he says. "This is especially so since the financial crisis, which reiterated the importance of foresight." Following the crisis, Wong has looked to ensure that NOL is well protected against both external and internal shocks.

One such example is in the company's hedging policy. "The philosophy we have developed is to have a deep understanding of our own organisation – the strengths and weaknesses – and apply that to our treasury strategies. We are in the shipping industry and we make our money from the liner and logistics business. So any risks that are not directly related to these (for example foreign exchange, interest rate and even fuel) should be hedged away," explains Wong. Natural hedges, Wong has decided, are the most effective and cost-efficient first line of defence and the treasury has worked with the business to develop a number of these, including creating a natural fuel hedge.

> "Thanks to strategy changes we now own 70% of our ships, our capacity is the same, and many of these ships are modern, more fuel efficient and also well financed. So we are better off, in terms of cost per teu (twenty-foot container equivalent units), than we were a decade ago."

"As one would expect, in our industry we consume a lot of fuel," says Wong. Over the last few years, NOL has been aggressively finding ways to bring down its overall costs, particularly fuel cost. "The cost of any movement in fuel prices can have a dramatic impact on the earnings of NOL. The price volatility, coupled with the volume of consumption, means that sound risk management is an imperative," he says.

To mitigate this risk, Wong had worked with the rest of the business, applying his philosophy of a natural hedge, to implement a strategy that protects NOL from swings in fuel cost. "The price we now charge our customers reflects our fuel costs and floats accordingly," he says. "Through partnering with the business heads and explaining to our customers about this risk we have been able to on-board around 80% of our customers to pay a floating rate, naturally hedging away 80% of our fuel costs."

Interest rates are another area where Wong has used his philosophical approach and deep knowledge of the shipping industry to naturally hedge risk. As a company that is capital-intensive and a net borrower, the exposure to interest rate risk is high. "A rise in interest rates however, for our business, is not a bad thing," he says. "If rates are rising, this means that the global economy is buoyant and the demand for goods will increase and our business will therefore be good." Having a floating interest rate therefore offers NOL a natural hedge against this risk. "A buoyant economy and good business can easily generate enough revenue to pay our interest rate costs many times over."

"As the Group Treasurer it is my role to develop these strategies and then articulate them back to the business and for the board to decide upon," he says. "Once they are accepted, they are institutionalised across all levels of the organisation."

## Transferable skills

While Wong missed his chance to sample other areas of the business during his management trainee days, he has since had the chance to gain exposure in other areas. The most prominent of these was time spent working alongside the group's procurement department.

Historically, the procurement department has been run by the liner division, which made the strategic decisions of what ship size and which trade routes for the ships to be deployed. "In 2005, the board decided this was not necessarily the best way to do things from a financial perspective." Wong explains that during an up cycle, shipyards and ship lessors demand the highest costs and longest leases. To effectively manage these demands, the procurement department was 'decoupled' from the business.

When procuring a new ship there are lots of questions that need to be asked, including whether they are leased or bought outright, and how they will be financed. "There are pros and cons to these options and they need to be carefully considered from a finance point of view," says Wong.

Since the financial crisis, Wong has implemented some major changes as he has been involved in this side of the business. The biggest of these is arranging the financing of new ships in advance with no covenant in order to protect against any financing risk. This is something Wong admits required some frank conversations with his bankers, in order to secure financing for an as yet unknown ship. "I was upfront about this and helped by narrowing down the scope of the order, in terms of what size and yard we may purchase it from."

"Ensuring that financing is in place is now something we do for any big ticket items, not just ships," says Wong. The experience shows the value that treasury can add to the wider business when fully engaged and for Wong, "It allowed me to see the business directly rather than just through the lens of treasury. It has added more colour to my career and certainly allowed me to become a more effective treasurer and business partner."

## Upfront banking

"I have been very fortunate over the years to have worked with very good bankers and I appreciate what they have done for me," says Wong. "They help me think through my issues and develop solutions through teamwork – this is invaluable." With such high-held opinions of his bankers it is no surprise that Wong spends a great deal of time managing his banking relationships and ensuring that both the company and the banks benefit from the relationship.

"I am always transparent and upfront with my banks and look to adopt a mutually beneficial partnership model," says Wong. For example, when it comes to areas such as fees, Wong is acutely aware that banks want to charge more; he therefore looks to establish a win-win situation. "If a bank is not keen on lending, but is happy to take our cash management business, then we will be transparent and ask for the lending we want. If the bank is happy to lend then we will reward them with some fee-based business – it's then good business for me and it's good business for the banks."

For Wong, it is important to take time to understand their business in order to obtain the most out of relationships. "I work with local and global banks, depending on our requirements and their strengths. Local banks have very strong balance sheets and we are happy to use these for straightforward processes such as FX," he says. "When it comes to cash management, for example, we chose to work with a global bank because of their innovative solutions and network. The key is to optimise banking relationships based on their expertise." In doing so Wong is able to maintain balance of all the banking relationships.

> "Therefore it is always the best policy to be upfront and transparent and ensure that everyone is a winner."

In terms of technology and the services provided by banks, Wong looks to these in order to improve productivity and processes without increasing manpower or effort. "Banks are armed with so many skilful and knowledgeable people, so it is a source I am always looking to tap," he says. "But I always need to ensure that what I tap is useful to the business. It can be quite easy to get caught up when being shown shiny new toys that the banks have developed, but if it is no use to the business then I am ultimately not interested."

In a capital-intensive business that relies on bank borrowing, Wong is aware of the delicate nature of bank relationships. "Therefore it is always the best policy to be upfront and transparent and ensure that everyone is a winner."

## The next step

In Wong's opinion the biggest threat to the shipping industry is overcapacity. "There are a lot of ships that have been ordered over the last decade and they are getting bigger and bigger," he says. Despite this, with the treasury's help, NOL has positioned itself well to meet the challenges of the future. "Thanks to strategy changes we now own 70% of our ships, our capacity is the same, and many of these ships are modern, more fuel efficient and also well financed. So we are better off, in terms of cost per twenty-foot container equivalent units (TEU), than we were a decade ago."

In terms of more treasury-specific challenges, a liquidity crisis remains the biggest fear. "If there is a case that all the banks have to recall their loans and I need to raise capital urgently, this could be a nightmare." Wong and his treasury team have done all they can to minimise the risk of this ever happening and while it remains a nagging worry, he believes that even if the worst does happen, the industry has the capacity to adjust.

When Wong decides to head for shore, he wants to put his historical, philosophical and treasury knowledge to work and move into consulting or teaching. "I have a former colleague who joined the teaching profession and he sends students to me to talk about hedging every other year. I am very happy to do this and I find it very rewarding to share my knowledge, so it may be my next move as I would like to give something back." ■

# In SAFE hands

*China's foreign exchange controls have evolved significantly over the past few years. The overall trend has seen the State Administration of Foreign Exchange graduate from controlling the regime at a micro level to supervising it at a macro level. In this, the first of a new series for 2015, we look at the history and people behind the well-known institution.*

Based in Beijing, China's State Administration of Foreign Exchange (SAFE) has responsibility for monitoring the country's balance of payments and foreign exchange positions. Its duties include: participating in the drafting of laws concerning foreign exchange administration, monitoring external credit and debt and cross-border capital flows and managing the foreign exchange reserves, gold reserves and other foreign exchange assets belonging to the State.

## How the SAFE came into being

Until 35 years ago, there was no state authority specifically tasked with the management of foreign exchange in China. In fact, the Bank of China had for a long time looked after the country's foreign exchange management. But in the spirit of Chinese economic reform under Deng Xiaoping, in February 1979, the People's Bank of China (PBoC) put forward a reform programme for Bank of China that would see the creation of what we now know as the State Administration of Foreign Exchange.

The overall aim of Deng Xiaoping's economic reforms was to open the country up to the outside world and to reverse the Maoist commitment to the ideal of self-reliance (although many were opposed to this radical change in cultural values). China was keen to purchase foreign equipment and technology in order to modernise its economy, but this so-called 'opening up' also led to foreign exchange inflows through tourism, exports, and arms sales. The PBoC quickly recognised the importance of establishing an entity to deal with the new foreign currency flows the country would be exposed to and the decision was taken to create the State Administration of Exchange Control (renamed in 1996 to be the State Administration of Foreign Exchange) as a separate

## Major functions of the SAFE

1. To study and propose policy suggestions on the reform of the foreign exchange administration system, prevention of the balance of payments risks, and promotion of the balance of payments equilibrium; to study and implement policy measures for the gradual advancement of the convertibility of the RMB under the capital account and the cultivation and development of the foreign exchange market; to provide suggestions and a foundation for the People's Bank of China to formulate policy on RMB exchange rate.
2. To participate in the drafting of relevant laws, regulations, and departmental rules on foreign exchange administration, releasing standard documents related to the carrying out of responsibilities.
3. To oversee the statistics and monitoring of the balance of payments and the external credit and debt, releasing relevant information according to regulations and undertaking related work concerning the monitoring of cross-border capital flows.
4. To be responsible for the supervision and management of the foreign exchange market of the state; to undertake supervision and management of the settlement and sale of foreign exchange; to cultivate and develop the foreign exchange market.
5. To be responsible for supervising and checking the authenticity and legality of the receipt and payment of foreign exchange under the current account according to law; to be responsible for implementing foreign exchange administration under the capital account according to law, and to continuously improve management work in line with the convertibility process of the RMB under the capital account; and to regulate management of overseas and domestic foreign exchange accounts.
6. To be in charge of implementing supervision and checking of foreign exchange according to law, and punishing behaviours that violate the foreign exchange administration.
7. To undertake operations and management of foreign exchange reserves, gold reserves, and other foreign exchange assets of the state.
8. To arrange development planning, standards, and criteria for IT-based foreign exchange administration and organising relevant implementation; to realise supervision of information-sharing with the relevant administrative departments according to law.
9. To take part in relevant international financial activities.
10. To undertake other matters as assigned by the State Council and the People's Bank of China.

*Source: The State Administration of Foreign Exchange*

entity from the Bank of China, although both would still be part of the larger PBoC.

In March 1979, the Chinese authorities also introduced a foreign exchange retention system as a means of providing incentives to exporters. Under this system, domestic exporters were permitted to retain a certain portion of their foreign exchange earnings, which could be used to import goods over and above the state import plans. Nevertheless, the official exchange rate that the country operated under made exporting expensive, and it became clear that something needed to change.

Soon, the authorities introduced a RMB Internal Settlement Rate (ISR) effective from 1st January 1981. According to a paper by Lin Guijun, School of International Trade and Economics, University of International Business and Economics, Beijing and Fulbright Scholar, Department of Economics, Columbia University, New York, "The ISR would cover trade-related foreign exchange transactions. At the same time, the authorities also retained the more appreciated official exchange rate to cover mainly non-trade foreign exchange transactions such as overseas Chinese remittance, tourism, expenditure by foreign diplomatic and business representative offices in China and Chinese diplomatic and business offices abroad, foreign investments, and foreign trade transportation and insurance charges. The adjustments to the official exchange rate were determined by the changes in the value of a basket of currencies."

The ISR was operational until 1984, when the challenges caused by a dual exchange rate system became too much and the Chinese authorities gave in to pressure from the International Monetary Fund to abolish the ISR. This marked the beginning of the next round of reform, which although too wide-reaching to explain in this article, saw the establishment of a foreign exchange swap market in China.

A series of further reforms saw the country work towards current account convertibility, whilst also laying some of the groundwork for capital account convertibility. In 1994, for example, China reformed its foreign exchange system, combining the renminbi exchange rates, and launching the China Foreign Exchange Trading System (CEFTS) – a unified inter-bank foreign exchange market.

Then, on 1st December 1996, after a series of pilot schemes, as well as the promulgation of the "Regulation on Foreign Exchange Sale, Purchase and Payment," China formally accepted Article Eight of the IMF's Agreement on International Currencies and Funds, and realised the goal of current account convertibility. To mark this milestone and herald the beginning of a new era, the State Administration of Exchange Control was renamed the State Administration of Foreign Exchange.

Since then, we have seen a greater variety of financial businesses being established in China. New sub-sectors have also been introduced into the Chinese financial industry

such as consumer credit, securities investment funds and investments linked with insurance.

## Then and now

Today, the SAFE is a deputy-ministerial-level state administration. Apart from its Communist Party of China (CPC) Committee, the SAFE Head Office consists of eight functional departments. These are:

1. General Affairs Department (Policy and Regulation Department).
2. Balance of Payments Department.
3. Current Account Management Department.
4. Capital Account Management Department.
5. Supervision and Inspection Department.
6. Reserves Management Department.
7. Human Resources Department (Internal Auditing Department).
8. Science and Technology Department.

There are also four institutions affiliated with the SAFE, including the Central Foreign Exchange Business Centre, Information Centre, General Services Centre, and the Editorial Office of the Foreign Exchange of China journal.

## Branch network

According to its website, the SAFE sets up branches and administrative offices in different provinces, autonomous regions and municipalities either directly under the Central Government or with a vice-provincial status. In addition, the SAFE establishes a number of central sub-branches and sub-branches in some cities and counties across China. As of the end of 2013, the SAFE network consisted of the following:

| SAFE network | Number of institutions |
|---|---|
| Branches (administration offices) | 36 |
| Central sub-branches | 307 |
| Sub-branches | 519 |

Elsewhere, the SAFE has a subsidiary in Hong Kong called the SAFE Investment Company which was formed in 1997. Another avenue for managing the country's growing foreign currency reserves (see Chart 1), the fund is able to invest in a wide variety of instruments including foreign and domestic equities and fixed income securities.

SAFE also has subsidiaries in Singapore, London and New York. The newest of these is the US branch, which analysts believe invests mainly in private equity, real estate and other alternative asset classes.

## People behind the institution

In early 2014, the financial press was shocked to learn that Zhu Changhong, an American-trained fund manager who returned to his native China to help invest the world's largest foreign exchange reserves, had left his position as Chief Investment Officer at the Beijing office of the State Administration of Foreign Exchange.

One of Zhu's main tasks had been to assist with finding alternative investments that offered similar safety and security to US Treasuries. The Wall Street Journal, reporting on Zhu's departure, noted that "In June 2010, just after Zhu started at the agency, about 45% of China's reserves, or $1.11 trillion, were invested in US government bonds, according to an analysis by ChinaScope Financial, a provider of financial data. Since then, China's overall purchases of US debt increased, but Zhu steadily helped reduce the percentage devoted to Treasuries to about 35%, or $1.29 trillion, in September 2013, the most recent figures available."

Although both sides declined to comment on the departure, some analysts cited internal politics as a catalyst. And Yi Gang, Deputy Governor of the People's Bank of China (PBC) and Administrator of the State Administration of Foreign Exchange (SAFE), is no stranger to this. Professor Yi Gang has long argued that China should slow the growth of the country's foreign reserves or even reduce them. He has suggested allowing the market to play a bigger role in determining China's exchange rate, for example. But these suggestions have largely fallen on deaf ears.

Other key members of the SAFE'S Management Team include Deng Xianhong, Fang Shangpu, Wang Xiaoyi and Li Chao – all of whom have the title 'Deputy Administrator of the State Administration of Foreign Exchange (SAFE)'. Finally, Yang Guozhong is the Head of the Discipline Inspection Group of the CPC Leadership of the State Administration of Foreign Exchange. Their biographies (which can be found on the SAFE's website **www.safe.gov.cn**) certainly make for impressive reading.

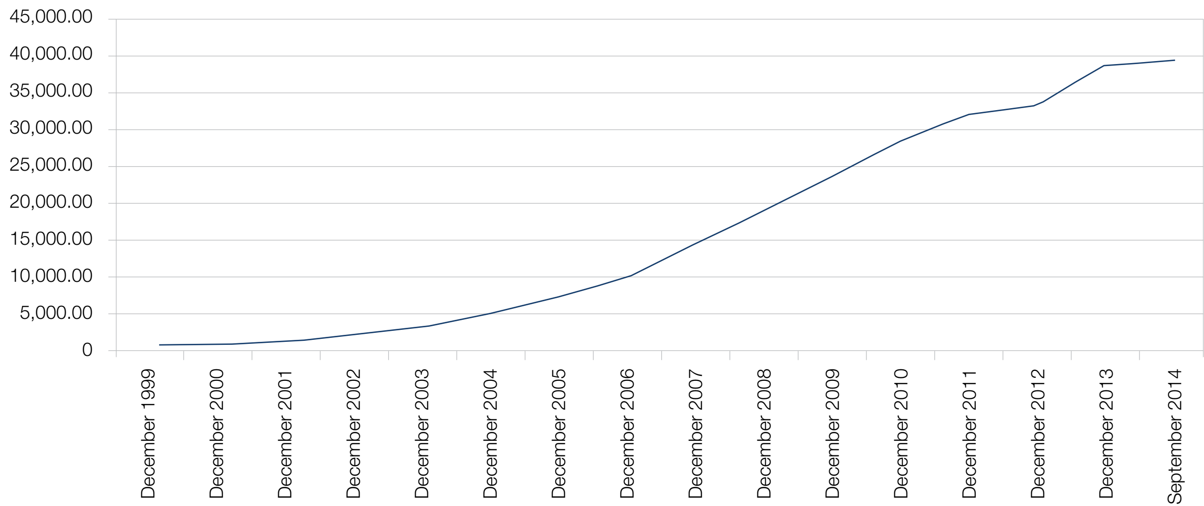
## Behind closed doors

What this management team discusses inside the SAFE is, unsurprisingly, largely secret. While the size of the country's foreign exchange reserves may be public knowledge, for example, analysts can only speculate on how they are invested. One area where there is a great deal of communication around the SAFE's activities, however, is on updates to often highly detailed rules and regulations. Treasurers operating the region will be more than familiar with the institution's circulars which inform them of the latest changes.

And in recent months, some of these changes have been extremely high profile. As of 1st June 2014, for instance, companies based anywhere in China can establish, with relative ease, centralised foreign currency cash management programmes. While MNCs who accumulate foreign currency onshore previously had the ability to perform two-way transactions independent of the Shanghai Free Trade Zone (SFTZ), the latest measures ease the documentary burdens that were limited to approved companies.

Now, there is no longer a need for each individual entity to submit supporting documents to the SAFE for each and every trade transaction. Instead, qualified multinationals in China can set up a payment-on-behalf-of (POBO) or receipt-on-behalf-of (ROBO) structure simply by filing a single request at their local SAFE branch. The local SAFE branch co-ordinates the filing with the SAFE HQ and certification process in the specified time frame.

### Chart 1: Scale of China's foreign exchange reserves ($100m)




*Source: PBoC website*

This easing of the rules was seen as a huge step forward – not only for the corporates, but also for the SAFE – which is often criticised for its slow and onerous procedures and for stretching the 'phase by phase' approach to deregulation too far. But in the SAFE's defence, with the significant burden of responsibility on its shoulders, it is understandable that the regulator wants to be thorough – and the detailed nature of the SAFE's rule changes is often easier for treasurers to follow than the somewhat 'grey' announcements from the PBoC.

Getting the most out of the SAFE therefore requires patience and understanding. It also requires a good relationship – the SAFE (and the PBoC for that matter) operates in consultation with banks and corporates. Therefore, having the right lines of communication, whether through your bank, or direct with the regulator, can be a significant advantage in building an effective treasury function in China.

As PWC says in its guide to doing business in the country, "Companies in good standing with SAFE may have better insight into managing the approval process and may be able to contribute to new policies as they are developed and introduced. In addition, as the government is inclined to experiment with new liberalisation policies, working closely with SAFE may provide some perspective, in assisting SAFE in its reform efforts, while also improving treasury's effectiveness." ■

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# Political risk: the impact on corporates

*Across the world, political risks are front-page news every day. But many corporates are in the dark about how these can affect their business. We look at the political dangers companies need to be aware of before starting operations abroad.*

Switch on the TV on any given day and you are likely to see the results of political instability around the world. From Argentina's debt crisis, to ongoing troubles in Ukraine, the past year has seen new political risks erupt that look set to rumble on throughout 2015. The question many corporates will be asking is, what is the knock-on effect on us?

"The impact of political risk on corporates is vast," says Charlotte Ingham, a Principal Political Risk Analyst at risk and strategic consulting firm Maplecroft. "This risk can be operational in nature, in terms of the physical security of their facilities and staff or the potential disruption to their logistics, or legal, if you look at things like corruption risk and the potential ramifications of violating the US Foreign Practices Act or the UK Bribery Act, as well as financial."

At the extreme end of the political risk scale is the forced expropriation or nationalisation of a company's assets in a country. While this is extremely rare, there have been cases of this occurring over the past century, including in Libya, Iraq and Venezuela. "This is the worst-case scenario for a corporate, where the company loses not just its profit, but its entire means of making money in that country – everything it's invested, everything on its balance sheet in that country, is taken away," says John Drake, Head of Intelligence and Risk Mitigation at AKE Group.

Wholesale expropriation of privately owned assets aside, there is a wide spectrum of less drastic ways political decisions can hit corporates. "Changing tax regulations and the revision of tax codes can significantly impact a company's bottom line. Similarly, if a country's government chooses to impose a tariff on certain commodities, this can make a big dent in profitability for foreign investors," says Drake.

Beyond the purely financial consequences, political risk can damage a corporate's image as well. "There are big potential reputational risks for corporates with operations in countries which have poor records on democratic governance, political violence, or human rights. There are a lot of challenges in these countries, but also lot of opportunities if the risks are managed well," says Maplecroft's Ingham.

## Business carries on

Often the highest-profile risks are not necessarily the most detrimental from a corporate perspective. Despite the awful human cost of terrorism, countries with a high incidence of terrorist activity are not necessarily no-go zones for corporates. "Terrorism generates a lot of headlines, but often the impact on companies might not be very significant if they are able to mitigate the risk. Many companies are still making a lot of money in Iraq, for example, especially in the oil and gas sector, despite some of the terrible atrocities that are going on in the country at the moment," adds Drake. "The political violence risks from terrorism, riots, and war can have a big impact on private companies, but not as much as full nationalisation, because if a country nationalises a whole sector without paying proper compensation, you lose everything. However, even in a war situation, you might not lose your assets in the longer term – you might be able to come back and reclaim them after a few years."

While political risks – in particular the risk of political violence – are often a significant deterrent to potential investors, with sound advice companies can successfully mitigate many of the risks. Implementing appropriate security measures, engaging with local communities, and selecting lower-risk parts of the country to do business in are just some ways corporates can cover themselves in higher-risk countries.

Beyond monitoring political risk hotspots, tell-tale macroeconomic signs – even in jurisdictions where political risk is not currently high – can help predict regions where problems may erupt in future. "We don't just look at risks and perils," explains AKE's Drake. "There are lots of indicators to look out for too, including macroeconomic developments. If there is a massive economic downturn, that usually raises the risk of political risk incidents occurring – it could lead to more unrest in the streets, it could lead to the government resorting to hostile and unpredictable actions in an effort to restore its control and authority."

Take the Eurozone, for instance. "We are seeing rising threats to the level of institutional stability which could have a knock-on effect on the investment climate," says Drake. "There is a major risk of deflation in the Eurozone over the coming years and this could have a huge impact on voting patterns, and the overall trajectory of EU and Eurozone evolution, with quite significant threats to the ongoing existence of the Eurozone and the European currency."

The Middle East also presents some interesting cases for the student of political risk. Political and social upheavals across the region have created challenges for corporates – some of which are easier to cope with than others, in this land of contrasts.

"Tunisia is a really good example of how a post-Arab Spring political system can evolve into what looks like an emerging

credible democracy, where governance is more stable and there is potential for development. However, right next door you have got a complete basket case – Libya, which is falling apart with virtually no institutional framework, and is totally lacking in the evolution of civil society," says AKE's Drake.

Yet even in Libya some corporates are finding opportunities. "Despite the political environment in Libya, the oil industry is continuing to function – albeit under major threat with lots of interruptions – these companies are still pumping oil out of the ground and generating revenue."

This goes to show that countries which appear to be disaster zones from the outside could still offer attractive opportunities to corporates. Lebanon is another example. "Throughout the civil war in Lebanon, the country's banking sector managed to function completely, and it's still regarded as one of the better run banking systems in emerging markets around the world."

## Enhancing reputation

Companies that do business in politically risky countries not only stand to get an advantage on competitors who refuse to take the risk. They can also help bring stability to the country in question. "Corporates could be playing a major role in the stabilisation of the world by going in and investing in countries that are seen as more hazardous because that investment will eventually provide job security and stability in a country," says AKE's Drake. "By helping companies do business in unstable regions, this helps build an economic framework and eventually assists the development of those countries into something less volatile. You can't build civic society without economic progress."

Furthermore, by investing in a country when times are hard, companies can establish crucial reputational benefits if and when stability improves. "If you invest when a country is unstable and provide jobs to a number of people in a community, when the situation starts to stabilise in the longer term and the market becomes more competitive with more companies moving in, provided you have managed to remain in that environment, your company will be at an advantage, because there will be local brand recognition," says Drake. "Investing in the local market during times of turbulence as opposed to leaving the country is likely to result in favourable treatment from local consumers, as well as the authorities, in the longer term."

Indeed, Drake says the 'three Ps' are crucial when investing in countries with high political risk: presence, patience and perseverance.

However, while investing in politically risky countries when they are not 'en vogue' can bring reputational benefits to a corporate, reputational damage can also arise if this investment is not carefully controlled. "When countries are unstable, there's more susceptibility to corruption – and the massive reputational risk that can result from this," warns Drake. "Signing contracts with illiberal governments brings a high risk of corruption, which could come back to haunt the company in the longer term. If you are going to invest in an emerging market with high political risk, you have got to know who the key players are, and be mindful of the reputational risks of doing business – especially of doing bad business."

In addition to the in-country risks of corrupt practices, many corporates are also subject to anti-corruption laws at home which extend to overseas operations. The UK Bribery Act, for example, has extra-territorial reach both for UK companies operating abroad and for overseas companies with a presence in the UK.

Corporate awareness of the political risks they are subject to varies widely. Given that they often operate in more unstable regions of the world, oil and energy companies typically have more sophisticated political risk monitoring capabilities. "In our experience, a number of corporates in the oil and gas sector have paved the way in terms of their knowledge, understanding and monitoring of these kinds of risks," says Maplecroft's Ingham. Shell, for instance, has a dedicated 'Scenarios Team' which is responsible for monitoring geopolitical shifts, as well as long-term trends in economics, energy supply and demand, and social change.

However, as supply chains become more and more internationally interconnected, corporates in other sectors are starting to pay more attention to political risk. "As a result of the increasing complexity of global supply chains, large corporates in several sectors are increasingly looking at the impact of political risk on their business in the way that companies such as some of those in the oil and gas sector have been doing for some time," adds Ingham. "Many companies, either directly through their own operations or through their supply chain, are going into territories they have not been in before, and an increasing number are using systematic, comparable ways of assessing this risk."

Maplecroft indexes the political risk of 197 countries across 52 indices. Its political risks include what it calls dynamic political risks, which focus on short-term challenges, such as rule of law, political violence, the macroeconomic environment, resource nationalism and regime stability, as well as structural long-term political risks, such as economic diversification, resource security, infrastructure quality, societal resilience and the human rights landscape.

In its 2014 Political Risk (Dynamic) Index, Somalia was ranked as the country with the highest political risk in the world, and was in the 'extreme' risk category, followed by Syria, Afghanistan, DR Congo, Sudan, the Central African Republic, Yemen, Libya, South Sudan, and Iraq (see Chart 1).

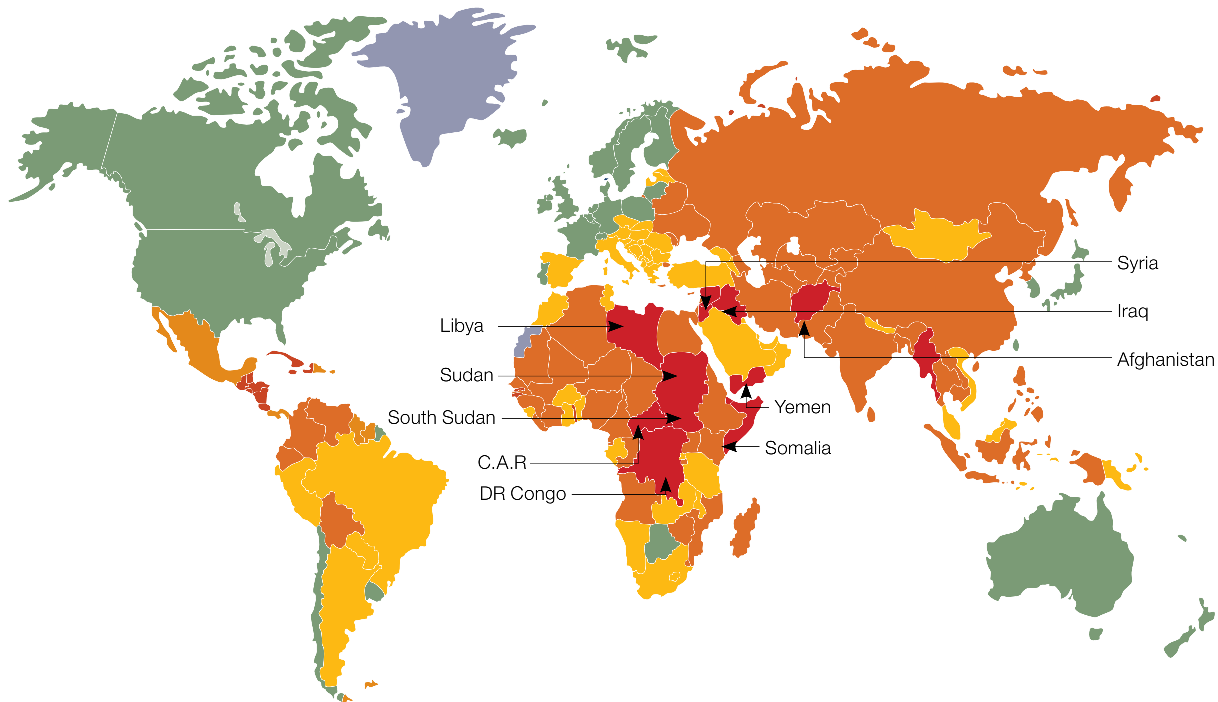
And according to Ingham, the world is getting riskier. "Since 2012, we have seen a notable increase in the number of countries that we would consider extreme and high risk," she says. "This category has gone from about 32.5% of countries in 2012 to 36.5% in 2014, and this growth has been driven by events in the Middle East and North Africa following the Arab Spring. Four out of our top ten riskiest countries are in the MENA region."

Furthermore, countries tend to deteriorate much more rapidly than they improve. "At the end of last year, Ukraine was medium risk by our dynamic risk assessment. We have done two updates since then, and it has now moved to the 36th highest risk in the world," explains Ingham. "The political violence level is the main driver behind that."

## Global fragmentation

But besides high-profile outbreaks of instability, such as that in Ukraine, why does political risk seem to be on the up in the longer-term? "There's now a general trend of fragmentation in the world at all different levels – on a global level, regional level, national level, supranational level, and individual level," says Andy Langenkamp, Global Political Analyst at financial research consultant ECR Research.

## Chart 1: Maplecroft's political risk (dynamic) index 2013




| Legend | Rank | Country | Rating | Rank | Country | Rating |
|---|---|---|---|---|---|---|
| **Extreme risk** | 1 | Somalia | Extreme | 6 | C.A.R | Extreme |
| **High risk** | 2 | Syria | Extreme | 7 | Yemen | Extreme |
| **Medium risk** | 3 | Afghanistan | Extreme | 8 | Libya | Extreme |
| **Low risk** | 4 | DR Congo | Extreme | 9 | South Sudan | Extreme |
| **No data** | 5 | Sudan | Extreme | 10 | Iraq | Extreme |

*Source: Maplecroft ™*

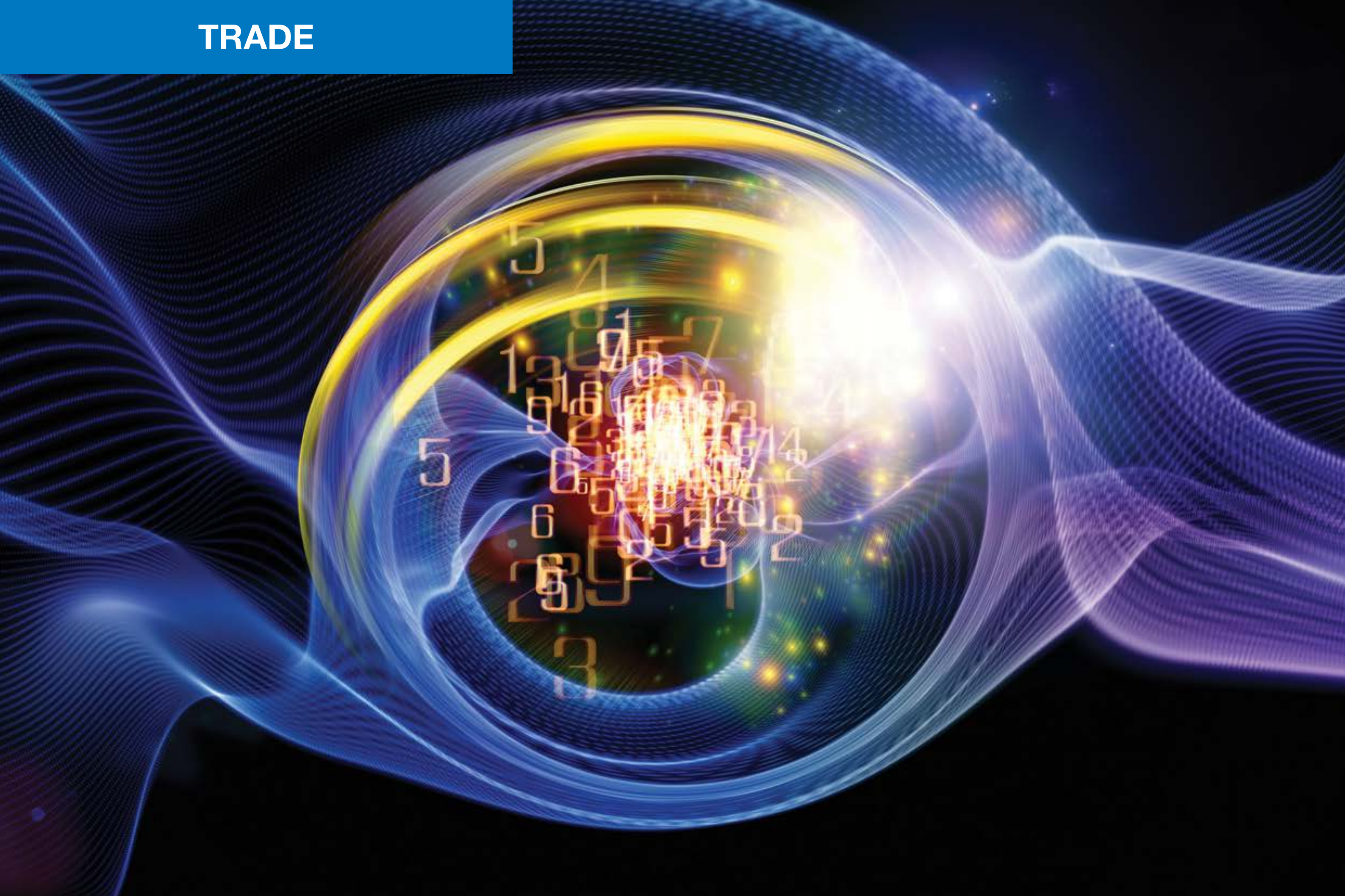
"The world is increasingly being divided into regional blocs. On the one hand this can be positive, because it encourages co-ordination and stability, but at the same time it undermines global corporates because these blocs are competing with each other. On a national level, there is increased nationalism – such as in India, Japan and Russia, and at the level below that there is a push for autonomy, as we have seen in Catalonia and Scotland recently. At the individual level it is much easier for people to contact like-minded citizens in other countries using the internet and mobile phones, which played a big part in events like the Arab Spring. This all goes to make the world much more unpredictable," adds Langenkamp.

Often companies – even ones operating on a global scale – integrate their political risk policy within their broader risk management policies and leave it at that. But AKE's Drake thinks many corporates could be doing more given the level of risk they face. "The potential losses in terms of assets, people, profits and reputational harm that can come about as a result of political risk is huge. Every company should have a board member who specialises in security and political risk, because something like the nationalisation of a company's operations – even though it doesn't happen very often – can wipe out your entire investment in a country," he says.

"Political risk needs to be addressed as part of an organisation's core culture if it wants to specialise in investing in challenging parts of the world – and these challenging parts of the world might not be that far away at all."

ECR's Langenkamp believes companies are waking up to the importance of the risk. "Geopolitics is a big part of the backdrop of financial markets," he says. "It is having a much bigger impact on financial markets and economies than it did five to ten years ago. Since the financial crisis, the corporate world has taken politics increasingly seriously as companies have started to notice that politics has a very big influence on their activity," he says.

Maplecroft's Ingham concludes that political risk per se should not deter corporates from entering a country. "We would never say to a company not to invest somewhere – it's just about fully understanding the risk profile, and then making sure that a very robust risk management policy is put in place," she says. "Continuity is important. It is not the particular level of risk, but uncertainty which creates the most challenges for corporates. If you know there is a high risk of political violence in a country, measures can be put in place to mitigate that – the challenge is if you don't properly assess the risk and plan for the possibility of a rapid deterioration." ■



# The new trade paradigm in ASEAN

*Here marks the beginning of a new dawn for companies trading in the ASEAN region. China may remain the dominant player across most markets in South East Asia – for now. But the upsurge in intra-ASEAN trade has been the biggest story in the region over the past few years. With the imminent arrival of ASEAN Economic Community, this trends looks to accelerate even further in the years to come. In this article, we ask what the new trade paradigm will mean for corporates and the demand for trade solutions in the region.*

Later this year there will be an economic shake-up the like of which has never been witnessed before in Asia. Yet, for all the excitement around the birth of the ASEAN Economic Community (AEC) and the prospect of greater intra-regional trade on the horizon, the economic data appears to indicate that this ambition will not be realised overnight.

Boosting intra-ASEAN trade is important, for obvious reasons. All countries that – like China and India – boast a high share of global trade have one thing in common. The share of business being done with countries in close proximity to them is considerably higher than their counterparts. In the European Union (EU) and the North American Trade Association (NAFTA), for example, intra-regional trade currently averages around 50%. In ASEAN, the figure is not even half that.

Speaking about the soon-to-be established AEC at a recent trade summit, the Singapore Foreign Affairs and Law Minister, K. Shanmugam acknowledged this reality, and called upon the region's leaders to step up to the challenge and make the elimination of trade barriers a priority of the new AEC in the coming years.

"What does [the AEC] mean for our people?" K. Shanmugam asked delegates. "It must increase trade. It must increase the economic relationship."

## Breaking down barriers

Although the ultimate goal is still some way off, recent ASEAN trade figures should make encouraging reading for K. Shanmugam. Ahead of the birth of the new AEC, an area which promises the freer flow of goods, services, investment and labour, trade between ASEAN economies has been rising. In fact, in recent years it has grown at a considerably faster rate than extra-ASEAN trade, boosted by the fact that the promise of integration has led a number of the region's large multinationals to establish offices in regional hubs to support their trading activities. Faster intra-regional growth can be seen as a positive sign, even if it's building, of course, from a much lower base.

"Countries in the ASEAN region seem to be buying and selling more to one another," says Sonal Priyanka, Regional Head of Trade for South East Asia, India and the Middle East at Societe Generale. "It is being driven partly by the promise of ASEAN integration under the Asean Economic Community and the consequent loosening of trade barriers in some of the markets."

## New trade flows

Economic integration is only part of the story however. To gain a better understanding of how and why ASEAN trade flows are changing, one must look at another macroeconomic trend taking place in the region; a shift in the types of goods being exported from ASEAN.

For much of the early part of the millennium, export of intermediate goods – products used in the eventual production of a finished good – was the dominant trade flow from ASEAN. This is now changing. "There is a lot more export of finished products from ASEAN now, as more and more multinationals (MNCs) are using ASEAN directly as part of their international supply chains," says Priyanka. And this is all leading, she explains, to "a shift from the sale of unfinished goods to finished goods."

Countries in South East Asia are no longer simply sub-contracting from main suppliers in China, sending their intermediate goods for final assembly in China. As China becomes less attractive to some MNCs as a supplier of finished products, these MNCs are looking for alternatives, and ASEAN is rising as an alternate low-cost producer to China.

This trend is part of the region's natural economic evolution, explains Simon Constantinides, Regional Head of Global Trade and Receivables Finance Asia Pacific at HSBC. "ASEAN is an economy with $2.4 trillion of GDP and 640 million people. It has vast natural resources and considerable manufacturing capacity. And now you've got good pricing from a labour cost perspective also," he says. "I think that is driving a lot of the activity we are seeing combined with certain government intervention to improve FDI opportunities and promote a more flexible environment for cross border trade. So I think it is the natural evolution and growth of the emerging markets within the ASEAN block."

As ASEAN's role in the international supply chain changes, new trade relationships are beginning to blossom. Japanese investment in South East Asia, which has boomed in recent years, is one example, explains Priyanka. It's been a remarkable resurgence. According to Dealogic, the value of mergers and acquisitions executed by Japanese companies –auto industry firms particularly – in ASEAN rose to $8.2 billion in 2013, a level not seen since the mid-1990s. "We are seeing growing Japanese interest in the region at the moment," she says. "A lot of Japanese corporates are now setting up their manufacturing operations here, away from the traditional manufacturing hub of China, due to cost and other reasons."

Despite the recent excitement around Japan, there is still only one economic powerhouse when it comes to trade in the region. ASEAN is now the fourth largest destination for outward investment from China, accounting for more than 60% of the country's foreign direct investment (FDI) volume. Given the structural changes being witnessed in both ASEAN and China the nature of the goods being exchanged has changed, but China's importance as a trading partner has never waned. On the contrary, increased trade flows can be seen in some countries. Trade flows between Malaysia and China, for example, grew from RMB 128 billion in 2009, to over RMB 203 billion in 2013. More broadly, annual bilateral trade between China and ASEAN's ten member states is expected to rise $1 trillion by 2020.

Banks know they cannot afford to stand still in the face of these big changes now transforming the region. The new trade paradigm that can be seen emerging is creating new demands for trade solutions in the region. To meet these demands, banks have had to respond with a range of new solutions using a broader range of currencies and new forms of financing aligned with new ways of settlement.

## New trade flows demand new solutions

In ASEAN, like in much of the rest of Asia and the world, there has been a pronounced shift from traditional instruments such as the Letter of Credit (LC) to Open Account settlement. "There has been a steady growth in the documentary trade business, with a rise in Open Account trade amongst Asian corporates," says George Fong, Asia Head of Trade Product Management and FI Advisory at J.P. Morgan.

Although this trend is not unique to ASEAN (80% of trade is now settled on Open Account globally), Fong believes it to be closely linked to recent developments on the ground, such as the growth in intra-ASEAN trade and the new financing needs this is generating amongst both Western and, increasingly, Asian multinationals. "We definitely see those local factors helping switch the terms of trade from instruments like the LC to Open Account or other negotiable trade instruments."

But despite the ongoing decline of the LC, one of the biggest impediments to intra-ASEAN trade remains paper documentation. Trade finance in ASEAN remains highly paper-intensive, something which obviously slows down the whole settlement process. Electronic trade solutions, meanwhile, can offer both better business flows and improved security for corporates in the ASEAN region.

In 2013, the announcement of new International Chamber of Commerce rules to govern the use of the Bank Payment Obligation (BPO) raised industry hopes that such archaic instruments may soon be consigned to the history books. However, almost two years on, it is clear that this was never going to happen overnight. For the time begin at least, the BPO is only being used by a select handful of large corporates – mostly in the commodities space – and for everyone else with trade finance needs, manual, paper-based processes remain very much the order of the day. "Paper-based trade most certainly dominates still," says HSBC's Contstantinides. "The BPO is not a widely adopted capability within ASEAN yet," he adds.

Why are electronic trade solutions such as the BPO finding it so difficult to get off the ground? Now that there is more legal certainty around the solution following the creation of the ICC rulebook, answers must be sought elsewhere.

Global banks have, on the whole, been very supportive of the BPO. That is all very well if you're a treasurer for a company that is banking with one of these large, sophisticated organisations. But that's far from the norm in ASEAN, MACT's Azmi Abdullah, Group Treasurer of Genting Bhd and Malaysian Association of Corporate Treasurers (MACT) committee member points out. "The regional banks that dominate the banking scene in ASEAN will have to step up their efforts to automate some of these trade finance solutions in the coming years," he says. "The global institutions, who are very selective in their clientele, still lead the business of providing trade solutions."

The dematerialisation is certainly an important issue for corporates in the region of all shapes and sizes and it's one which we will return to and explore in more depth in the next issue of Treasury Today Asia. Now, though, we will consider how trade in ASEAN is becoming less dollar-centric, shaped by China's supremacy in the region and the recent efforts of its regulators to gradually liberalise the renminbi (RMB).

## Rise of the redback

For any company doing business in China today – ASEAN domiciled or otherwise – settling trade transactions in RMB might make a lot of sense since it can reduce risk naturally, offering opportunities for hedging without having to go through a third currency.

It's not surprising then that, given the growing opportunities for corporates to move RMB in and out of China now, settling in RMB is becoming an increasingly popular option. This phenomenon is bigger than China, of course. Ask any treasurer in the world today and most will tell you that the RMB is assuming an ever greater role in trade settlement.

This anecdotal evidence is reinforced by recent data. The RMB now stands as the seventh-ranked global payments currency and accounted for 1.72% of global payments, an all-time record (see Chart 1). In September 2014 alone, the value of RMB global payments increased by 13.2%, well above the average 8.1% growth for all currencies.

ASEAN has been a part of the RMB's rise, as much as any other country. RMB usage by ASEAN countries has, according to data supplied by Bank of America Merrill Lynch, doubled (+103%) year-on-year with an estimated FY value close to RMB 2.6 billion. "This is a significant move in anyone's language and it shows that ASEAN trade is supporting RMB internationalisation confidently," says Kuresh Sarjan, Head of Trade and Supply Chain at BofA Merrill. "Overall, the RMB has consistently strengthened its position in a relatively short period of time," he adds.

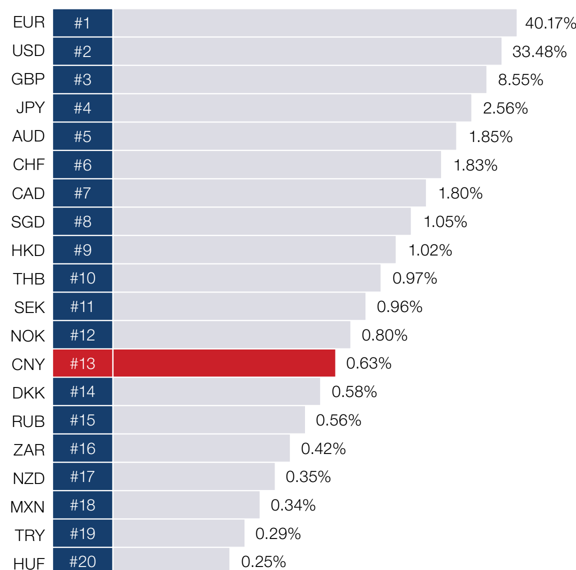
## Tomorrow's ASEAN

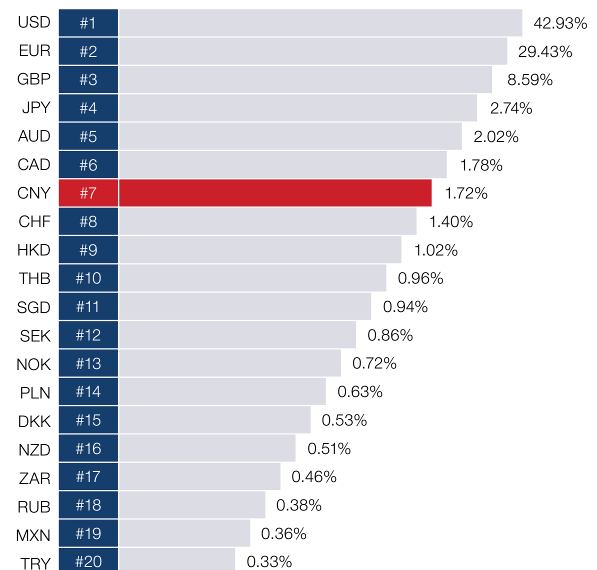
In less than 12 months' time, ASEAN will open a new chapter in the history of its economic development with the creation of the AEC. Significant obstacles still stand in the way of this ambition, however, with the region still notorious, of course, for economic protectionism and stringently regulated financial markets.

But the incentives for ASEAN nations to overcome these obstacles are truly enormous. If the promised AEC succeeds in accelerating recent growth in intra-regional trade, the benefits it will bring for businesses operating in the region will be very significant indeed. Recent analysis conducted by the McKinsey Global Institute (MGI), for example, found that greater integration could translate into productivity benefits worth up to up to 20% of the cost base for some ASEAN manufacturers.

Corporates, of course, will want to be prepared as much as possible for the new opportunities that will be coming their way after 2015, looking at how changing regulation might impact the currencies they can and cannot use and the trade solutions available to them. It's going to be a busy year for treasurers. ■

### Chart 1: RMB as world payments currency in value




*Source: SWIFT Watch*

## Adam Smith Awards ASIA 2014

# The real deal

*Celebrating the achievements of corporates from across the APAC region, the Adam Smith Awards Asia Gala Presentation Lunch which took place on 13th November 2014 saw 142 of the brightest thinkers in the industry come together in Singapore to share their stories of success.*

In Asia Pacific, as well as globally, the years following the global financial crisis have been immensely challenging. Yet, treasurers across the region have stepped into the spotlight to meet this test head-on, successfully guiding their companies through these difficult times. In doing so, corporates have shown great dedication, ingenuity and innovation, developing industry-leading solutions to solve a multitude of complex problems.

Recognising the extraordinary efforts of treasurers in the region, Treasury Today Asia introduced its Adam Smith Awards Asia programme to the market last year, building on the success of the global Adam Smith Awards programme. The judging panel was inundated with nominations from corporates across every industry sector and from countries including China, India, Singapore, Hong Kong, Malaysia, Thailand, Korea, Japan and Australia.

After much deliberation, well-deserved winners were selected in each of the 15 award categories, in addition to a number of highly commended projects that the judges felt also deserved recognition. And despite the wide geographical footprint of the corporate treasury departments honoured with an award, 142 corporates and their strategic business partners gathered at the Grand Hyatt hotel in Singapore on 13th November 2014 to take part in the inaugural Adam Smith Awards Asia Gala Presentation Lunch.

The event began with a welcome reception and the room was abuzz with the attendees acquainting themselves with peers and sharing stories of their award-winning projects. Following the reception, all guests were ushered through to the Grand Ballroom where Angela Berry, Publisher, Treasury Today, gave a welcoming speech. Lunch was then served, but not before the room was plunged into darkness as the kitchen was dramatically opened with much fanfare.

It was then time for the corporates to take centre stage as each Winner and Highly Commended corporate was invited

on stage to collect their award. The pride that accompanies such recognition was clearly visible on the face of each winner and images of their awards were quickly being shared with colleagues, friends and family via social media.

## Deserved recognition

"An event such as the Adam Smith Awards Asia is certainly overdue for a region that has been performing particularly well in recent years while many are still struggling," says Calvin Lee Manager, Asia Pacific Treasury Centre at LG Electronics Singapore. "Receiving an award gives great recognition to the journey the treasury team has been on in recent times."

This thought is echoed by David Gaythorpe, Finance Director SEA and Pacific at adidas Singapore who says; "It is great external recognition. The Adam Smith Awards have a great reputation in the treasury world."

For all corporates in attendance, receiving an Adam Smith Award was not only a huge honour but also motivation to go on and do other things. "Winning the Adam Smith Award is a great achievement for us," says Harjeet Kohli, Group Treasurer, Bharti Airtel, Winner, Treasury Today Asia's Top Treasury Team. "The team gets the right level of motivation and drive to continue to do better. I also think the accolade adds accountability to the team to continue to strive and raise the bar to retain such status – again a worthy motivation."

Another theme mentioned by attendees at the event is that winning an Adam Smith Award also sets a benchmark for the industry to work towards. "In a tough environment where all corporates are striving for efficiency, the Adam Smith Awards provide a great platform for companies to benchmark themselves against their peers, their competition and also companies in different industries," says Ashish Bhardwaj, Senior Credit Manager at Microsoft. "Thanks to the Adam Smith Awards Asia event, we have seen that there has been lots of innovation in the region and there is plenty of best practice. The challenge now is to learn from this and continue to innovate."

In the quest to find the most innovative solutions, the Adam Smith Awards Asia recognise that it is not always the large household name organisations such as Microsoft and LG Electronics who are doing great things. Take for example MSF Sugar, the integrated grower processor, marketer and exporter of raw sugar based in Gordonvale near Cairns in Australia, who received a Highly Commended award in the Best Risk Management Solution category. "It is great to receive recognition for what we have done," says Gunnar Andresen, Commercial Manager at MSF Sugar. "It is also fantastic to see what some of the largest companies in the world are doing and share our stories. We will take the award back to our company and share the success with our sugar cane grower suppliers and other stakeholders."

## Winners roll call

The diversity of companies honoured in this year's Gala Presentation Lunch reflects the range of nominations submitted to the judges – which totalled 162 nominations across the 15 categories. The full case studies of all winners and highly commended appear in the Treasury Today Adam Smith Awards Asia Yearbook, but in the meantime, here is a brief snapshot of the winners in each category and their solutions.

The headline award is the Top Treasury Team Asia award, which is open to any treasury team who have developed solutions to tackle a multitude of challenges, added real value to the overall organisation and raised the bar for treasury operations globally. The winner of this prestigious award in 2014 was Bharti Airtel, based in New Delhi, India.

Bharti Airtel's truly outstanding submission detailed a treasury transformation project across seven key pillars, covering that entire spectrum of the treasury function, which has delivered some impressive benefits. These include cost savings, KPI improvements and reduced risk. The submission raised the bar and demonstrated the innovation and ingenuity that the Awards represent.

The Best Cash Management Award is open to any company that demonstrates best practice and innovation in this important treasury discipline. Hitachi Data Systems Corporation led by Brian King was 2014's deserved winner. Hitachi transformed its cash management process through centralisation, consolidating its banking relationships and streamlining the overall process. The innovative use of host-to-host connectivity with its bank through its SSC centre ensured reduced touch points and delivered greater control.

## Setting the standard

Increasingly, corporates are turning to benchmarking in order to assess their performance, against both internal markers and

external companies. The award for Best in Class Benchmarking in 2014 went to Amway India Enterprises, whose project was carried out as a reaction to its growing business volumes across India and its banking complexities in the country. The internal and external benchmarking project focused on identifying the important benchmarks of success around multiple areas. The results of the project drove the implementation of India's first automated, multi-bank pooling structure proving that complex banking structures pose no barrier to achieving an efficient, centralised liquidity management model.

Australian beverage group, Treasury Wine Estates (TWE), was awarded the Best Card Solution. Its corporate card project not only provided a single global platform for all card payments but also connected it to Australia's common terms deed legal agreement. This unique and innovative solution has allowed TWE's corporate cards to integrate with its other core debt facilities, creating a value-add, working capital financing solution.

With the cash-based nature of many Asian economies, an efficient working capital solution is vital. For example, in India, where cash and cheques remain the predominant payment means, operating across a country of such geographical breadth makes the collection of cheques a challenge, especially in remote locations. In overcoming this challenge, METRO Cash & Carry India received the award for Best Working Capital Solution. Its image-based clearing solution has saved an average of two to five days on cheque processing times. Also, a supplier finance programme was developed that streamlined the process through simplified documentation and also saw the bills discounted and the proceeds remitted to suppliers on the day of request.

The winner of the Best Financing Solution is another India-based firm. Mahindra & Mahindra (M&M) the multinational automobile manufacturing organisation faced a number of issues around their long-term debt financing. Interest volatility meant its financing, completed with put and call options, hardly survived beyond ten years. The desired solution was to issue a 50 year bond with an interest rate of 9.55% p.a. with no put or call option. The M&M treasury team was able to successfully execute the deal and, in doing so, has created a new market instrument for that tenor in India. This means that Indian corporates can now look to the domestic as well as the global markets to raise long-term funds.

When expanding offshore, a company faces many new challenges, one of these being heightened FX risk. This was an issue for Best FX Solution winners Ingredion Incorporated, whose purchase of National Starch saw them become a truly global company. To overcome the FX challenges this presented, the company implemented a systems-based solution that would look to consolidate all the global currency and risk management processes in Asia Pacific. This was achieved using a single bank and currency platform that would be integrated with Ingredion's existing treasury technology across the region. The decentralised approach is unusual yet has offered increased FX benefits of $1m and a reduction in bank fees.

Over the past 12 months all eyes have been on China as its deregulation agenda has created a number of opportunities for corporates, not least where trapped cash is concerned. The sheer volume of nominations for the Adam Smith Awards Asia emanating from China and the innovative solutions that corporates had developed there meant that the country deserved its own award category. The winner of the Best Solution in China went to Bunge (Shanghai) Management. Utilising the SFTZ, Bunge has developed a two-way RMB cross-border sweeping structure, allowing for greater efficiency in the utilisation of its funds in China and moving trapped cash out of China. The innovative solution allows Bunge to make intercompany RMB loans from the Shanghai entity to the regional treasury centre (RTC) in Singapore, as well as from the RTC to the Shanghai entity, and daily sweeping is also possible.

## Full of promise

The winner of the One to Watch award, issued to companies who have ongoing projects that have the potential to create great benefits, was the Chinese National Petroleum Group (CNCP). The massive internationalisation of CNPC's business has meant that the treasury has had to evolve to ensure it can meet growth requirements and the additional complexity brought by operating worldwide. To ensure CNCP's treasury could step up to the plate, the department launched a re-engineering project. This involved the implementation of best practice solutions across the board and delivered significant efficiency improvements to the treasury function. Treasury Today Asia will certainly be watching further developments from this innovative treasury department.

As the technology that corporates are able to access in the region evolves, so do the opportunities to re-engineer treasury processes. Honeywell is one company that has taken full advantage of this opportunity by reducing the operational risk associated with having multiple users of its electronic banking

platform. The 'three instance approach' which Honeywell has deployed allows the treasury team to monitor and track the users of the company's electronic banking platform, ultimately reducing the risk of fraudulent activity occurring. This solution saw the Honeywell treasury team awarded the Best Process Re-engineering award.

Sometimes a solution can go beyond benefiting just the company, to benefit the economy of a country. This is the case for the Best Risk Management Solution winner, The Clearing Corporation of India. By adopting a settlement procedure similar to a CLS bank, it has been able to improve transaction settlement efficiency, mitigate risks, insulate the Indian financial system from operations-related shocks and undertake other activities that help to broaden and deepen the money, debt and FX markets in India. Thus, the solution has a direct positive impact on the Indian economy, which is one of the largest in the world.

## First class thinking

With centralisation firmly on the agenda of companies across the region, many treasurers are looking closely at their banking relationships. Blackstone is one such company and it was awarded the First Class Bank Relationship Management award. The company was looking to establish an Asian focused real estate fund that would allow it to target business opportunities across a number of different countries in the region. As part of this process, Blackstone revisited its banking requirements to help the company centralise cash management and FX execution in the region. The result was the use of a single bank across the region.

The Judges' Choice award recognises a team that develops a solution that is just that little bit different. This year, Larsen & Toubro led by Harish Barai, was awarded the accolade for their analysis of the economic and political landscape of India over the past two years. Through carrying out this analysis, the team was able to protect the company from instability in the country and its markets.

Finally, the Treasury Today Asia Women of the Year was Shirley Hiew, Global Cash Lead; Treasurer, Asia Pacific at DuPont. Described as having a unique combination of hands-on leadership and a great strategic vision around her areas of responsibility, she keeps raising the bar for herself and her team. Shirley was nominated by the Editorial Team here at Treasury Today Asia and our nomination has been endorsed by a number of senior contacts within the industry, including a number of Shirley's colleagues at DuPont.

## Your time to shine

Do you think you and your team can beat the class of 2014? Nominations for the Adam Smith Awards Asia 2015 open on 8th June 2015. We look forward to celebrating your success in Singapore in November 2015.

# Peak flow

*Cash flow forecasting is an important part of corporate financial life. So much can depend on getting it right and yet rarely, if ever, is it 100% accurate. Treasury Today Asia goes 'back to basics' with this essential function and asks how businesses should best approach it.*

For any business, knowing how much money will be coming in and going out gives a better understanding of how much will be needed to keep operating and to enable growth. The optimisation and most effective use of cash, in essence, is what cash flow forecasting is all about.

Whilst the fundamental principles and purposes of cash flow forecasting remain largely unchanged, the needs of the modern market have placed greater emphasis on accuracy and cash visibility. The full 100% minimum liquidity coverage ratio of Basel III (to be enforced in 2015) will change the liquidity landscape as banks – including Asian banks – place different values on the deposits sitting on their balance sheets. As corporates revisit their investment policies and risk appetites in this environment, and as structures such as in-house banks, payments-on-behalf of, collections-on-behalf of and payments factories continue to emerge as favoured models, visibility over cash becomes ever more vital. The aim is to be able to segment that cash into the most appropriate operational, reserve and strategic liquidity pools and, particularly in Asia, be able to navigate the regulatory diversity that characterises regional markets.

In achieving this goal, one of the key requirements now is for treasurers to better understand the needs of their business colleagues, and for those colleagues in other business functions to understand the needs of treasury and the function of liquidity. Even corporates that, by the nature of their business or sector, have not been best placed to deliver accurate forecasts should now be looking for a clearer all-round view. For an organisation, being sufficiently agile to get the best from its financial data is important; technology can play a part, but open communication is essential.

## Clear communication

The treasurer is typically charged with looking after the organisation's cash, ensuring it has appropriate liquidity and mitigating any risks and changes in business flow that may arise.

## Cash flow forecasting in practice: TRILUX Group

Case study

International lighting solutions provider, TRILUX Group, has more than 20 production and sales sites in Europe and Asia (including China, Hong Kong, Philippines and India). Its Group Management division operates a multi-layer five-year integrated budget and liquidity forecasting plan which includes an annual view of the Group's P&L, balance sheet and cash flow across all business units, covering some ten currencies in total. This, explains Oliver Thissen, Member of the Management Board, Finance/Legal, enables Group Management to draw up the budget and liquidity plans for the following financial year, which it does every September, the figures being based on refinement at multiple points in the year with reference to actuals.

To enable this, Thissen explains that the Group has a cash forecast and cash management plan running on a daily basis, using information generated by the import of SWIFT MT940s into its single SAP treasury management system (up to 90% of bank statement data from more than 150 accounts is loaded automatically, says Thissen). Each business unit is required to create a rolling four-month liquidity plan which is revised using actuals on a weekly basis. On a monthly basis the annual budget and liquidity plans can then be revised for each company within the Group. A comparison is made between monthly target and actual account statements with explanations sought for any variance. The revised results are fed back into the annual budget and liquidity plans as part of the continuing cycle of updating and improving.

The rolling data is in fact a series of five liquidity planning spreadsheets, notes Thissen. These cover the following data points: an overview of liquidity allocation; assumptions of tax (including VAT) and personnel expenses (such as social security payments); an estimation of financial status (external loans and deposits and those managed via TRILUX's in-house bank) and a consideration of payment terms (such as the posting of sales revenue versus customer payment data); estimated and actual opening balances (each business unit has the opportunity to enter and explain any manual adjustments). The fifth spreadsheet is the output of all companies, uploaded into the TMS and consolidated into one view which is used to produce annual budget and liquidity forecasting plans.

Collection of figures starts with actual budget figures from the previous month, output from SAP; the rolling budget forecasts for the next month are then added. Using what Thissen refers to as an "Excel bridge", data is transferred into the rolling forecast for cash flow. The entire process to this stage is carried out on a per company basis so the results uploaded into the TMS generate around 35 different cash flow forecasts within the system. With the help of TMS he explains that it is then possible then to consolidate all forecasts into a single view. This view is used to produce annual budget and liquidity forecasting plans – and the cycle continues.

But often the information related to these tasks resides in other business units and all too often these functions sit in siloes and communication is minimal. The calls from treasury for yet more financial data may not always be seen in a positive light if there is little understanding of why it is needed. This really becomes a problem when the other functions fail to recognise that the information they provide has to be current and accurate; rough approximations will lead to inaccurate forecasts and a subsequent incorrect assessment of cash needs by treasury. This is a major risk for the entire company.

If business units are held accountable for the determination of their own cash and liquidity needs and feeding that back into the cash flow forecasting process, it will encourage understanding. It will be beneficial, in terms of the accountability of the business units, for those units to be measured and monitored using KPIs to ensure that the task is carried out in a timely and accurate fashion. It will also be helpful for the treasurer to clearly explain to the business unit heads that the information provided will be used not just for liquidity planning but also possibly for interest rate planning and FX hedging, and that getting it significantly wrong is a serious risk event. Indeed, if the forecast is significantly wrong because the information provided was inaccurate or because the modelling was poor, the treasurer may be hedging a position that does not exist, exposing the business to trading and open positions that are not backed up by real business flows. Sizeable and unexpected losses may ensue.

## Timing

The frequency of forecasting depends on industry sector and, to an extent, the size of the business. A treasurer will often run a forecast off the back of a cash positioning process, used to determine elements such as current available balances, cash concentration and funding. The period depends on need: short-term cash forecasting is for overnights and investments into the market, whereas the longer forecast ensures cash is in the right place at the right time and in the right currency.

As with any process of prediction, the further out you go, accuracy will diminish. This is why frequent updates using actuals is essential and why known future financial events, such as debt repayments, must be incorporated. In considering the latter, it should be apparent that forecasting not only recognises cash events over a certain time horizon but also non-cash events such as repayments, covenants, interest rate and FX risk exposures and even hedging policies.

## Accuracy

Good quality information and a means of managing accuracy are vital elements of forecasting. This can be achieved with a 'look-back' process – sometimes known as variance analysis – to analyse and update previous forecasts using actual figures.

Attaining 100% accuracy in a forecast is unlikely, especially for the longer-term view. In fact, the Treasury Today 2014 Asia Pacific Corporate Treasury Benchmarking Study reveals that just 8% of treasurers in the region reach an accuracy level of more than 90% when comparing forecast versus actuals on volume of transactions; it slips to just 5% when comparing for value of transactions.

However, it is important to understand cause and effect to eke out incremental improvements in the managing, monitoring and

provision of data. If it is understood why something happened it may be possible to prevent or replicate that scenario as required. The more the treasurer is in charge of what flows are going to look like, the better the forecast will be.

## Methods and models

When generating a forecast, it is important to have access to an historical database of actuals that show how the business needs and uses cash over time. But data is just data until it is cross-referenced and interpreted; only then does it become usable information. By bringing it all together, it is possible to apply relatively simple statistical analysis to produce a forecast (it is also possible to apply highly complex mathematical models, explanations of which can be found elsewhere). Obviously it is important to consider whether the business has changed in any significant way (a major change of sales model or product line, for example) before using previous forecasts and actuals to influence results, but by looking at the database of cash actuals relative to projections, any variance will be apparent.

There are two basic types of variance analysis: 'common cause variation', or the ebbs and flows found in the normal course of business; and 'special cause variation' which reflects abnormal events likely to result in a negative or positive 'spike' in forecast performance. It should be possible in the analysis of 'actual versus expectation' to place any variance either in the realm of common or special cause. If the spike was 'special cause' and thus not predictable, it will be beneficial for future forecasting to try to put in place an early indicator of such events occurring again; learning from the past is a key part of forecasting.

## The role of technology

According to a 2013 survey of APAC treasurers carried out by SunGard and Bank of America Merrill Lynch, 67% of respondents do not use any form of forecasting tool for cash and of those that do, 69% rely on spreadsheets. The survey also showed that of those respondents that did not use any cash flow forecasting tools, just 10% were 'very satisfied' with their processes, the vast majority (52%) claiming to be just 'moderately satisfied'. The Treasury Today 2014 Asia Pacific Corporate Treasury Benchmarking Study further reveals that implementing a cash flow forecasting solution is the top technology issue and that cash flow forecasting is the number one area in need of improvement for those with an existing TMS.

It is clear that connected systems on a widely distributed network are the ideal when collating forecasting data. A TMS or ERP that is accessible via the web by the various business units, regardless of geography or time zone will afford direct input of their element of the cash flow forecasting data, this either being used as a continuous update or allowing the treasurer to collate, analyse and present the data relatively easily.

But business units that sit outside of an otherwise connected business can present data for manual entry, even if that means emailing a spreadsheet to the treasurer or picking up the phone. Despite the 'shock, horror' headlines of the APAC survey, a formally dedicated spreadsheet is a suitably flexible tool for the job and can be used with an ERP or TMS (see case study, opposite). However, as with all spreadsheets, care must be taken around version control, incorrect formulae and input error.

With the centralisation of treasury, the rise of in-house banking structures and the increased use of connected technologies and analytical tools, there is an opportunity to have better visibility over cash and cash flows. For those that choose to take advantage of these technologies, it means the ability to forecast is improving too. The models used by proprietary solutions may be far more complex than common spreadsheet formulae, but they do signify a reduction in reliance on the 'best effort' of an individual and a shift of emphasis towards more accurate and timely information and data support.

Linked with the ability to electronically move cash around the globe to optimise balances and make rapid transfers (using a pooling structure, for example), technology could play an increasingly important part in cash flow forecasting over the next few years. However, the value of significant relevant forecasting experience and an in-depth understanding of the company and the sector in which it operates should never be underestimated. It is thus advisable to consider proper 'succession planning', fully documenting all processes; if only one person has the knowledge, it will disappear if they leave the company.

## Banking role

As banks increasingly play a role around cash application, they are in a position to provide more data flows to clients related to the receipt of cash payments and the application of those payments to account balances. Some 25% of the APAC treasury survey respondents said improving cash visibility was top of their agenda.

But as bank products are commoditised, the banks themselves are seeking more of an advisory role to cement their relationships with their corporate clients. APAC is a complex region for treasurers not least because the diverse tax and regulatory environment makes cash optimisation challenging, especially where currency controls exist. If understanding the rules is difficult and cash visibility is an issue, in passing on their accumulated experience and understanding of integration, processes, systems and organisational structures, the larger banks with regional presence are in a position to genuinely add value to the cash forecasting process.

## Cost/benefit

That said, banks continue to have a more traditional role to fulfil. To ensure an organisation has the right level of cash and liquidity it may set up either an uncommitted or a committed facility with a bank. If, on the basis of solid forecasting, the business is reasonably confident of its cash positions going forward it may feel able to meet its liabilities in a given period. In such a case it may not need to put in place or call upon its facilities at all. However, with poor quality forecasting or in an unpredictable or volatile financial environment, there may be a need to seek bank cooperation.

A committed facility will cost more than an uncommitted facility, but with an uncommitted facility, if the need for cash arises simultaneously with many other businesses, bank funding may not be available. Of course, financial derivatives exist to hedge against unfavourable movements but there is a cost here too, depending on the kind of programme used. Hedging using FX forwards is cheaper than using options and can help predictability by smoothing the curve of FX variability through the neutralising effect of any gains and losses (options are better suited for those seeking the upside whilst mitigating the downside, but they attract a premium). It is all a matter of confidence in the forecast. ■

# Cash management: best practice (part one)

*People often ask our treasury insider what constitutes best practice in cash management. His normal reply is that it depends on the company. There is no one size fits all, he explains in the first of this two-part article. Nonetheless, there are some themes that stand out – such as efficient processes, optimal use of cash, and risk minimisation – that drive clear trends.*

Cash management exists in a context; therefore optimising cash management must be contextual. The context is the business and its risk profile, as well as management's risk appetite.

My working assumption is that the goal of treasury is cost effective risk reduction (CERR). Most of us want to reduce costs, especially since treasury is non-core to corporates. Likewise, we want to reduce treasury risks – but crucially not at any cost. No risk equals no reward. Nevertheless, we want to reduce treasury risks to maximise the risk capacity that can be deployed in the core business.

Treasury can only optimise CERR, and by extension cash management, if the risk profile is clear and agreed by management. This is not rocket science, just simple things like: how much cash should we hold? What is acceptable leverage? And so on.

## Cash management

At its core, cash management comprises flows and balances. Flows are about moving money into, out of, and around the business – payments, collections, and intercompany settlements. Balances are what end up on different bank accounts around the business.

Optimising flows is primarily about cost reduction and managing operational risks. Optimising balances may require more work on the CERR balance. For example, to one business, zero-balancing subsidiaries may seem cost effective; to another it might seem too risky.

"To one business, zero-balancing subsidiaries may seem cost effective; to another it might seem too risky."

## Managing flows

The key to efficient flow management is to minimise both the internal and the external costs. This requires efficient processes – for example manual processing is expensive both internally and externally at banks – so straight through processing (STP) must be the goal. And the wider the STP, the higher the efficiency. Happily, STP is a no brainer from a CERR perspective, since STP reduces costs and risks (humans are expensive and error prone).

STP is often understood simply to mean 'avoiding manual repair of payments by banks'. My meaning is much wider. I mean STP throughout the purchase-to-pay (P2P) and order-to-cash (O2C) processes. In direct procurement, the purchase decision can be made by the material requirements planning (MRP) software directly without manual intervention. In indirect procurement, procurement workflow can capture initial request, management approval, delivery, and then automate invoice matching and payment when due. In O2C, where customers order electronically, the workflow can be fully automated through to reconciliation of collected cash.

I hope it will be clear that best practice goes far beyond the treasury department and the banks. Best practice involves optimising CERR holistically across business processes. This is not 'pie in the sky' either – I know plenty of corporates that operate as described above, and have neither (particularly) simple, nor purely virtual, businesses.

That said, the integration described above may not suit all businesses or may not be accessible to all treasuries. There are a wide variety of solutions between writing

cheques and full electronic integration that can suit diverse corporate needs.

## Optimising payments

Here are some more specific observations that flow from the above.

Approving payments is nonsense. It is too late anyway. The moment for key controls is when the legal obligation is created – for example, a purchase order (PO) for commercial transactions and entering into a deal for treasury transactions. If the purchase was legally valid and the seller has delivered as contracted, withholding payment will only lead to court.

And if the payment approval is intended to verify that the seller's banking information is correct, then manual approval is a lousy way to check this kind of data. It's time to get a decent ERP and TMS, and secure them correctly. The key control points here are changes to the vendor master data (especially banking details – or, for treasury, the SSIs standing settlement instructions) and initial contracting (POs for commercial transactions and deals for treasury transactions).

Depressingly, I frequently hear things like "But my FD likes to sign the telegraphic transfer form." In any material business, the FD or CFO cannot possibly know the details of every payment, and signing payments cannot be a productive use of senior management time. Furthermore, despite all the current excitement about spying and data security, paper is – by any reasonable measure – a much more dangerous medium than electronic. In short, this predilection massively increases CERR by raising costs and pumping up risks.

Since the PO is the critical legal document of the business' obligation, it makes sense to pin the P2P process to it. Many CFOs have the mantra of "No PO, no pay", in other words if an invoice comes in without the PO number on it, it is returned to sender forthwith. With that number connecting PO, delivery, and invoice, it becomes easy to build efficient P2P processes that are both safe and cheap.

On the external cost side of payments, best practice includes ensuring lowest-cost routing, which generally means making payments locally. This in turn implies paying on behalf of (OBO) – ie treasury (or SSC) has accounts in each country so that it can make payments locally on behalf of subsidiaries anywhere in the world. Of course, it is also good practice to code payment instructions in your ERP and TMS so that they avoid manual repair at banks.

Best practice in OBO is when subsidiaries have no bank account at all. Many multinationals have consolidated all payments and collections to IHB (or payment factory), in other words 100% of flows are handled through IHB accounts on behalf of subsidiaries so the subsidiaries have no bank accounts at all. This results in one bank account per country owned by IHB.

Note that none of the above is about squeezing service providers and banks – it is about improving internal processes. None the less, there is no point in paying more than necessary for payments. As a guideline, local low value payments should be free or cents, and international payments should be $5-10. Percentage based fees are not acceptable, especially since they normally have minimum floors. Market practice is not a justification for abusively high fees. There should be no float or compensating balances (unless you have transparency over pricing and are able to calculate the benefit precisely). ■

***In the second part of this article in the next issue, we will continue our look at best practice, covering everything from visibility over balances to cash pooling.***

### David Blair, Managing Director

Twenty five years of management and treasury experience in global companies. David Blair was formerly Vice-President Treasury at Huawei where he drove a treasury transformation for this fast-growing Chinese infocomm equipment supplier. Before that Blair was Group Treasurer of Nokia, where he built one of the most respected treasury organisations in the world. He has previous experience with ABB, PriceWaterhouse and Cargill. Blair has extensive experience managing global and diverse treasury teams, as well as playing a leading role in e-commerce standard development and in professional associations. He has counselled corporations and banks as well as governments. He trains treasury teams around the world and serves as a preferred tutor to the EuroFinance treasury and risk management training curriculum.

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*The views and opinions expressed in this article are those of the authors*

INSIGHT AND ANALYSIS

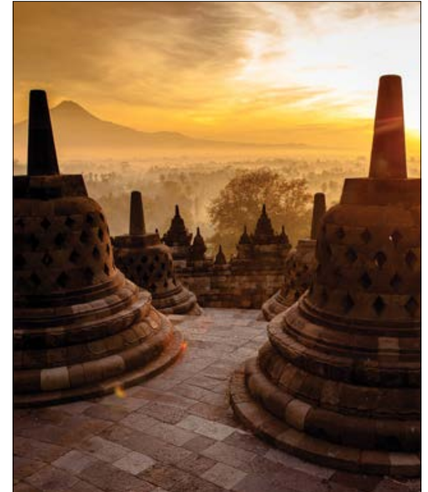
## Smart investment solutions

Following the crisis corporate investment shifted from being focused on yield to being focus on preservation of principle. Eight years on the tide is beginning to turn and corporates are tentatively beginning to seek yield once again. What smart investment solutions are open to corporates in the Asia Pacific region, Treasury Today Asia investigates.

TECHNOLOGY

## Treasury Management Systems

For the modern treasury department managing the financial activities of a business manually with spreadsheets can be an extremely risk-laden and time-consuming task. Investing in a treasury management system (TMS) is one option that could help corporates meet such challenges. Treasury Today Asia analyses what is under the hood of a TMS and what corporates should look out for.



KNOW THE REGION

## Central Asia

The financial press tends to focus heavily on Asian countries such as China, Japan and Singapore, but what about the Central Asian nations? In this new series, we examine the history behind the Central Asia region and examine the local business environment, highlighting points of interest for treasurers. We also look at developments in the region that are making it an increasingly attractive business location.

**We always speak to a number of industry figures for background research on our articles. Among them this month:**

**Azmi Abdullah**, Group Treasurer, Genting Bhd; **Faisal Ameen**, Head of Treasury Management Product, Global Transaction Services, Asia Pacific, Bank of America Merrill Lynch; **Gunnar Andresen**, Commercial Manager, MSF Sugar; **Ashish Bhardwaj**, Senior Credit Manager, Microsoft; **Vijay Chander**, Executive Director for Fixed Income, ASIFMA; **Dawn Chua**, Head of Capital and Treasury, SGX; **Simon Constantinides**, Regional Head of Global Trade & Receivables Finance Asia-Pacific, HSBC; **John Drake**, Head of Intelligence and Risk Mitigation, AKE Group; **Matt Emsley**, Partner, Corporate, Herbert Smith Freehills; **George Fong**, Asia Head of Trade Product Management and FI Advisory, J.P. Morgan; **David Gaythorpe**, Finance Director SEA and Pacific, Adidas Singapore; **Amol Gupte**, Region Head, Asia Pacific, Citi Transaction Services; **Charlotte Ingham**, Principal Political Risk Analyst, Maplecroft; **Mahesh Kini**, Asia Pacific Head of Cash Management Corporates, Deutsche Bank; **Harjeet Kohli**, Group Treasurer, Bharti Airtel; **Andy Langenkamp**, Global Political Analyst, ECR Research; **Calvin Lee**, Manager, Asia Pacific Treasury Centre, LG Electronics Singapore; **Hannah Levinger**, Analyst, Deutsche Bank; **Patricia Lim**, Head of Cash Management, Asia Pacific, RBS; **Max Loh**, ASEAN and Singapore Managing Partner, EY; **Calum Macphail**, Head of Corporate Private Placements, M&G Investments; **Emmanuelle Nasse Bridier**, Chief Credit Officer, AXA Group; **Sonal Priyanka**, Regional Head of Trade for South East Asia, India and the Middle East, Société Générale; **Kuresh Sarjan**, Head of Trade and Supply Chain, Bank of America Merrill Lynch; **Oliver Thissen**, Head of Finance, TRILUX Group; **Richard Waddington**, Head of Loan Sales, Commerzbank; **Steven Wong**, Group Treasurer, NOL.

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