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June 2013

Will cash ever die?

Cash transactions persist despite a score of business reasons why we should do away with them. However, the global volume of non-cash payments has continued to show healthy growth, with the largest gains in volumes occurring in developing markets.

Women in Treasury

Yera Hagopian

Global Head of Liquidity Product
Barclays

The Corporate View

Peter Schädelbauer

Head of Group Treasury
Lindner Group

FX portals
e-Portals make their mark

Corporate fraud
A perennial problem

Back to basics
The benefits of netting

Tax and treasury
Taxing times ahead in Asia


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transform
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A tale of two cities

Miami and Singapore: two very different cities in two very different regions. Yet there were a number of common themes running through the EuroFinance conferences held in these cities in May.

First, as the global financial crisis reaches its fifth anniversary (commonly dated from when Lehman Brothers went down for the count), there seems to be no end in sight regardless of which side of the globe you reside. In Miami's opening plenary, Omar Sharif, US Economist, RBS Securities, raised the spectre of the US federal debt ceiling, pointed to the decreasing estimates of trend growth (currently at 1.9%) and said quite plainly "it doesn't feel like a boom time".

In Singapore, the mood was slightly gloomier for a change – in a straw poll of the participants, just over half (54%) felt more confident about their business prospects in the coming year, whereas in Miami the figure was 60%. This may have been the result of a flurry of negative news around economic data turning sour, the risk of a hard landing in China and a downturn in exports, but in his keynote speech Frederic Neumann, Co-Head of Asian Economic Research and Managing Director, HSBC, was quick to dispel these stories as just "noise". Yet the Asian markets took another tumble in the last week of May, which has caused more anxiety to creep into market sentiment. An interesting take-away from Neumann's session was how closely intertwined the growth story in Asia is with the quantitative easing (QE) policies of the West, which begs the question, as the governments in the West begin to unravel their QE packages, will the Eastern economies start to falter?

The second theme is interconnectedness. Despite some economists still floating the idea of a 'decoupling' between the emerging and developed markets, the interrelated nature of global finance and business was nowhere more apparent than at the EuroFinance conferences. The global multinational treasury operations are increasingly integrated and 'joined up', as illustrated by leading lights in treasury such as AkzoNobel, Microsoft, Yum!, IATA and Omnicom. Presenting in both cities with different treasury team members, their contributions showcased their skill in creating a uniform vision of processes, procedures and technology across the globe.

The third theme is treasury transformation. The vast majority of the conference presentations, as well as the entries from the Adam Smith Awards winners, told impressive transformative stories – whether that was through changing the culture of the organisation, driving rationalisation and centralisation, improving working capital cycles, or implementing innovative supply chain finance programmes. Despite tough times – or maybe because of them – a new breed of treasurer is coming to the fore. Not content to just fight their corner and maintain the status quo, these treasurers are coming out swinging and effectively taking the professional to the next level through a complete re-engineering process.

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Robert Murray

Managing Director
Richard Parkinson

Switchboard	+44 (0)13 0462 9000
Publisher	+44 (0)13 0462 9012
Subscriptions	+44 (0)13 0462 9002
Advertising	+44 (0)13 0462 9018
Editorial	+44 (0)13 0462 9004
Production	+44 (0)13 0462 9013
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Cash remains king – and even more so since the onset of the global financial crisis. However, the cost of moving cash around is an area under scrutiny as corporates look to cut overheads. Today, there are new technologies in the marketplace that can significantly reduce the cost of handling cash.

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Global Head of Liquidity Product

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BUSINESS BRIEFING


treasurytoday Business Briefing

How do you manage inflation uncertainty?

How do you manage inflation uncertainty?

As central banks across the world try in different ways to manipulate inflation in their favour, now is the time for treasurers to consider the bigger picture, take stock of the relative uncertainty and chart a strategy to defend against inflationary pressure.

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BENCHMARKING 34

Corporate Treasury Benchmarking

Compare your business against others and be part of the programme to create industry-wide best practice. Treasury Today first introduced Corporate Treasury Benchmarking in 2009 and your response has been amazing – almost 3,000 respondents across five regions since our first study.

What's yours is mine

Despite numerous measures, including controls around passwords, clear-desk policies, and implementing banking processes that require multiple approvals, fraudulent activity never goes away. All businesses need to be able to answer a very basic question: who are the employees in the company, particularly in the finance teams?

Taxing times in Asia

According to the World Bank, Hong Kong and Singapore are the fourth and fifth easiest places in the world to pay tax based on the number of payments, time and total tax rates. However, things are not as easy elsewhere in the region. Transfer pricing and general anti-avoidance rules (GAAR) are two areas of contention.

Peter Schädelbauer
Head of Group Treasury, Lindner Group and Managing Director, Lindner Finanz

Lindner

Highly Commended in the 2012 Adam Smith Awards, Peter Schädelbauer re-engineered Lindner's treasury so that it is capable of delivering the level of oversight and control necessary for survival in the worst of economic times.

Deal or no deal: anatomy of an FX portal

For a treasurer, the choice between single or multi-bank platform seems obvious at face value. Why wouldn't they sign up for a multi-bank FX portal and get the lowest price at the click of a button? Certainly the multi-bank portal's arrival was seen as the death knell for single-bank platforms.

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 treasurytoday.com

"And the winner is..."

The winners of the Adam Smith Awards 2013 have been announced. We are now looking forward to the prestigious Awards Lunch at Plaisterers' Hall in the City of London on 20th June.

Yet again 2013 has seen a record number of nominations and the standards were higher than ever. The judges found it a very challenging task to shortlist the best applications and decide on the winners. Our expectations were exceeded in terms of the number and sheer quality of entries submitted – 214 nominations from 25 different countries. Our thanks go to all those nominated and to our sponsor Bank of America Merrill Lynch.

This year's programme attracted entries from some of the world's largest organisations, along with a strong representation from the MME/SME universe. One of the major trends we are seeing this year is the increasing use of various technology solutions from simple connectivity, integration projects and TMS/ERP upgrades to full-blown treasury transformation programmes. Furthermore, around half of all entries received stated they were global, again illustrating the ever increasing remit of the corporate treasurer.

The winners and those highly commended will be profiled in the 2013 Awards Handbook which will be published in July and distributed to all subscribers. This will provide a fascinating insight into some of the best practice solutions corporates have been implementing over the last year.

What do corporates want from banks?

As corporates face new and continual challenges due to the sluggish global economy, their banking needs are evolving – and so are their expectations as to what banks should deliver in order to support their business. Much of this expectation is also driven by rapid technological innovation.

During a SWIFT Business Forum in London, Anne Coghlan, Head of Group Treasury at Dyson, which designs and manufactures vacuum cleaners, hand dryers, bladeless fans and heaters, outlined two levels to the bank interface. Firstly, there is the "bread and butter" of day-to-day treasury transactions, such as payments and cash management. She voiced her surprise that many banks do not offer a "health checklist" to assess how a corporate is functioning in the basic areas. Secondly, there are the new tools, such as helping corporates achieve better market penetration with their goods.

At present, the company has six transaction banks, with almost 80% of activity going through just three of them. Coghlan wants to consolidate still more but admitted that one bank is too few (reflecting a consensus most corporates reached after the recent financial crisis), whereas six is too many. "Today we are putting in place the building blocks that will help us achieve Nirvana – which is greater efficiency," she said.

At the end of the day, Coghlan wants two things from her banks:

1. To know that the solution she chose after a request for proposal (RFP) process and put in place is actually doing what it is supposed to be doing.
2. To have confidence that they will come to the regular six-month meeting with targeted suggestions as to how to improve Dyson's business.

The Asian growth story: can it continue?

The 19th EuroFinance in Singapore, held from 15th-17th May with more than 450 delegates, kicked off with an economic overview of the Asian situation. Any corporate operating in the emerging Asian markets – whether global multinational or domestic dynamo – is well aware of the complexity that comes with the territory, but the region's rapid growth story over the past seven years has been hard to ignore. However, in the past few weeks doubt has begun to creep in, with talk of economic data turning sour, the risk of a hard landing in China and a downturn in exports.

"Don't worry too much about this in the near term," says Frederic Neumann, Co-Head of Asia Economic Research and Managing Director, HSBC, Hong Kong, speaking in the opening plenary. Starting from the global economic situation, one important area to look at is the level of industrial production: emerging Asia has reached a level 47.1% above its pre-crisis peak, whereas the level of industrial production in the US is -1.7% and Europe is -13.4% compared with previous peaks. This shows that some form of decoupling is happening, according to Neumann, as the increase in Asian output has occurred despite the West not reaching its previous levels.

The other important area to consider is the Western central banks' response to the global financial crisis. There is a rule of thumb amongst economists that after a recession central banks only start to tighten monetary policy when output is 10% above the previous peak, mainly because only at that point will unemployment rates start to drop and inflation re-emerge. "Continuing with the current recovery rate in the US, to reach 10% above the previous peak will take another two years or so," says Neumann. "Therefore, there is no need to worry about the Federal Reserve withdrawing quantitative easing (QE) despite the recent media hype."

In Europe, the European Central Bank (ECB) should do much more to support economic growth, believes Neumann. The ECB cut interest rates but it will have to turn to QE to arrest the decline. This response is important for Asia because the monetary easing policies in the West are partly responsible for the increase in the East's output. "Financially the Asian recovery is closely linked to the stimulus coming from the West, and its continuance will allow Asia to grow for another two years," he states.

Emerging risks

The large injections of liquidity into the Asian markets has generated many questions about the effects and sustainability of the stimulus packages, East and West, raising the spectre of the Asian crisis in 1997.

Neumann warns that there are imbalances building up. What can be a trigger for this whole process to unravel? Neumann came up with three possible scenarios that would prick the Asian debt bubble:

1. Higher global interest rates.
2. Exploding local inflation that undermines financial confidence.
3. Some sort of financial scandal or crisis that again undermines financial confidence, such as a Ponzi scheme, a European bank getting into trouble at the level of a Lehman Brothers or a "Chinese Bernie Madoff" appearing.

The road less travelled

Between 2016 and 2020, impressive trade growth is expected for the markets of Vietnam, Malaysia, Bangladesh, Japan and Singapore. Economists are also predicting that trade and capital flows between emerging markets (EMs) could jump ten-fold in the next four decades. The International Monetary Fund (IMF) predicts that the 80/20 split between advanced and emerging economies in terms of share of world GDP in 2004 will, by next year, be more like 60/40.

As the competition gathers pace, international companies are expanding their trading activities into new regions. The practical implications of supply chain management when moving into these territories, especially the EMs, were brought to light at the ACT's Annual Conference held in Liverpool at the beginning of May.

The shift of labour

Carl Pate is Group Finance Director of Quantum Clothing Group, a UK-headquartered supplier to retailer, Marks & Spencer. It has no exposure to sales beyond UK but owns 70% of its production with facilities in Sri Lanka, India and Cambodia, and joint ventures (JVs) in China and sourcing in Vietnam, Indonesia and Bangladesh. "The reason we will place units in a particular location is due to fabric and labour availability," he states.

Indeed, Charles Barlow, Group Treasurer of Coats, a 250-year old industrial thread and textile crafts business, says that the textile business has pretty much all shifted to EMs as companies look to find the cheapest sources of labour. In China, most of its production goes into the export market; but as the Chinese economy grows and the people become wealthier, he anticipates that the company will be able to shift more to selling local production in China rather than for export.

The company, which is present in more than 70 countries across six continents, has been operating in EMs for many years, says Barlow (it was a Coats employee who introduced football to Brazil). Even with operations in emergent economies such as Cambodia and Vietnam, it too has been forced into a labour contingency mode. "If we look at where the next pool of cheap labour is available for making textiles, then Africa is the place," he comments.

The spirit of an EM

"The EMs are a very important area for us and we look to place a subsidiary in every market into which we can sell our products," states Craig Williams, Assistant Treasurer, FX, Markets Execution at Diageo, a premium-brand spirits, beer and wine company with a turnover of £12 billion. Before 2011, Diageo, which operates in 180 countries, derived less than a third of its turnover from EMs. "As of December last year it was 42% and our CEO has set a target of 50% by February 2016." This will be achieved through a mix of organic growth and acquisitions.

Diageo's Asia Pacific business serves the established markets of Korea, Japan and Australia and the EMs of China, India and Southeast Asia (Thailand, Malaysia, Indonesia, Philippines, Singapore and Vietnam). In China, for example, it invests locally and has been in the country since 1995 and has a long-standing JV – MHD – with Moët Hennessy. This relationship has enabled Diageo to build what it calls "brand extensions", including the opening in Shanghai and Beijing of what it describes as "ultimate luxury space for high net worth Chinese consumers". These, it claims, are its "most successful experiment in marketing and commercial innovation in Asia to date". ■

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

This much I know

Yera Hagopian

Global Head of Liquidity Product

BARCLAYS

What is your career-defining moment?

When I was seconded to what was at that time the Beecham Group, a British pharmaceutical company, as Assistant Treasurer Operations from 1987-1989. I consider it to be a defining moment because I still use the experience I gained there as a reference point almost on a daily basis.

What is the secret to your success?

Two things: curiosity and sheer persistence. I am quite stubborn (determined, if you are being kind) but also very curious – I want to know how things work. I have applied my training as a linguist (which is someone that likes to break down the code of a language and find out how it works) to my banking career.

What is the biggest challenge you are facing just now?

The biggest challenge is to bring the benefit of my experience to the business, while maintaining all the good things that already exist. That's the challenge of being a new person on the job and wanting to make changes, while also valuing the good things that are already in place – and there are many of them.

What couldn't you manage without?

Human contact would certainly be high on my list – the time to talk to people in order to really understand where they are coming from and their point of view. I also need time to think – to stand back from everything and take a more strategic view.

What is your next major objective?

After being away from Barclays for 14 years, I would like to settle in so well that people forget that I had left. I also want to start making a difference. Within the first 100 days I hope to have a broad understanding of the business, have met key people and our customers and formulated my initial view of where I should take the business.

What advice would you give to other women in treasury?

My advice is to take every opportunity open to you to learn and acquire the broadest experience possible. If you are working in product management, then work in sales; if you work in sales, try your hand in operations. You may not be good at everything but the breadth of experience that it will give you is invaluable. I believe it's good to take an unconventional path when progressing your career.

> "I think I was made to be a product manager because it is so multifaceted and takes a range of skills."

ON THE WEB

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

Yera Hagopian recently returned to Barclays as Global Head of Liquidity Product within its cash management team after a 14-year absence. She first joined the bank in 1980 on a management development programme straight out of university and stayed 19 years before leaving for a stint first at HSBC (11 years) and then just under three years at J.P. Morgan. "The different organisations have played an instrumental role in contributing to my understanding of cash management in different geographies, customer segments and product lines," she says.

For the initial 15 years of her banking, she was what she terms a "generalist". Her early career development focused on credit and risk, with a fair amount of relationship management and some treasury experience. "I am glad that I got to spend time in these areas early in my career because I think they are fundamental to a bank's business," Hagopian explains. During this time she also spent two years working abroad in the US: one year with a relationship team in Chicago and a year in New York in the treasury function.

In what she describes as a career-defining moment, Hagopian was seconded to the Beecham Group as Assistant Treasurer Operations from 1987-1989. Although it was meant to be just a three-month secondment, she was there for just over a year and a half. "That was a fascinating period because it coincided with a major treasury centralisation programme. This gave me insight into the practicalities and challenges of running a corporate treasury," she says. Almost daily she still uses the experience gained during this time as a reference point. "Whenever I am putting together something for a customer or thinking about a new service, I always find myself calibrating with what I learned during this period."

Her turn as a generalist ended after leaving the Beecham Group to go on maternity leave. "I took two years out," she explains, adding that some people still raise their eyebrows when she tells them this. Her husband's job transfer took them to Dusseldorf. It was exciting to be in Germany during reunification, but it was also quite challenging, especially learning German from scratch with a baby in tow. It was the second time in her life where Hagopian had the experience of going to a country where she didn't speak the language: her family moved to the UK when she was five years old and didn't speak a word of English.

When she moved back to the UK in 1989, not only had the world changed but the banking industry had changed as well. Still with Barclays, her first foray into the world of cash management entailed building a small specialist sales team and then she moved into managing a suite of products, including electronic banking. With the first taste of product management, Hagopian was hooked. "I think I was made to be a product manager," she says, "because it takes a range of skills. It is very multifaceted: you need to understand marketing but also technology; you have to be able to do detailed pricing and also have influencing and people management skills. It takes a specialist but you also have to be a generalist."

Hagopian describes another career-defining moment, which came early on when she worked on the liquidity product management side, but which is more akin to an epiphany than a moment. It was when she realised that she was "it": the person that colleagues completely relied on for critical liquidity management advice. "It is quite a wake-up call for a young product manager to realise that a lot of people trust and depend on your knowledge and ability to deal with a situation," she explains. "You have to assume that mantle of responsibility and bravery, which is the point at which you mature in your professional life."

Although hard-pressed to uncover anything that she would have done differently in her career, the one thing that Hagopian identifies is that she wished she could have spent more time working in corporate treasury. "Although it wasn't convenient in terms of my personal life at the time – I went on maternity leave – if there had been opportunities to repeat that experience regularly throughout my career, I think that would have been very valuable."

She believes that a combination of formal education and on-the-job training is needed, but the latter should come first. "Formal education does a number of things, in particular ensuring that there are no glaring gaps in your knowledge, such as a lack of credit experience when working in cash management," she says. "But I also believe that training is something you should do throughout your career. It is a time to stand back, reflect and reconsider if what you are doing is the best way to do it and whether there are other angles that you haven't thought about. Often that comes from meeting peers on training courses and being able to discuss topics in a more abstract way than the job allows on a day-to-day basis." ■

Yera Hagopian is Global Head of Liquidity Product within the Cash Management team at Barclays. She is responsible for driving the delivery of Barclays liquidity product set globally and providing integrated liquidity solutions to the corporate, financial institutions and non-bank financial institutions clients. Hagopian has a wealth of experience in global liquidity management. She recently joined Barclays from J.P. Morgan, where she was EMEA Head of Liquidity. Prior to that, she was responsible for Liquidity Services at HSBC for 11 years, a role which involved the co-ordination and development of HSBC's global liquidity management. Hagopian is a graduate of Brasenose College, Oxford.

In charge of IT

Tapping our collective knowledge to get better information

Who should be in charge of IT in treasury?

Joerg Wiemer, CEO and Co-Founder of TIS:

Today a high performing treasury team is a business partner, a value-adding change agent and a thought leader. Over the coming years, a treasurer will also need to further intensify collaboration with colleagues in shared service centres (SSCs) and lines of business in order to optimise, standardise and automate, especially the order-to-cash (O2C) and purchase-to-pay (P2P) cycles.

In my experience, a treasurer should establish highly scalable, flexible, standardised, automated and ERP integrated treasury and payment processes across the company. In addition, a quick return on investment (ROI) in terms of IT is crucial for a treasury's success.

This is a huge challenge for internal IT teams. During my time as treasurer I had several projects with excellent business cases, including high ROIs. However, many projects were slowed down because in-house IT resources were not available or the IT team did not have the expert knowledge required to make payment processes more efficient and secure. IT departments are often uninterested in taking on responsibility for treasury's technology for a good reason: most IT organisations spend 80% on maintenance and only 20% on innovation which directly supports the lines of business. By reducing the high maintenance costs for treasury IT, resources (money and people) can be freed up for innovation and improvement, which can help the organisation be more competitive and better achieve its ambitious growth targets.

Buying treasury IT as a service has become an attractive option for treasurers, CFOs and CIOs. The cloud computing/software-as-a-service (SaaS) trend in payments and treasury is moving faster than many may think. Compared to SaaS, a typical traditional on-premise solution is a painful road to take, with time-consuming and costly hardware and software installations, followed by lengthy and apprehensive IT projects that tend to take an enormous amount of treasury and IT resources.

Jayakumar Venkataraman, Partner, Financial Service Consulting Practice, Infosys:

The global financial crisis in 2007 and economic downturn led to a sharp reduction in the lending activities by the banks and thus made access to credit extremely difficult and costly. The complexities of working capital and liquidity management were compounded by fluctuations in interest rates and commodity prices and new regulations. This has created a high level of uncertainty in assessing the financial position within the corporates and the potential impact on profitability. The role of the CFO and corporate treasurer in the management of funds has therefore become extremely challenging. Within this context, technology plays a crucial role in helping the CFOs run an effective treasury function.

There is no doubt that the person in charge needs a sound head for technology. Whether it is re-engineering accounts receivable (AR) and accounts payable (AP) processes to release idle cash from within operations, or implementing liquidity management tools to reduce reliance on bank credit and implementation of SSCs, IT is central to any successful treasury management programme.

In many businesses, it means the CFO is often the best person to take on this responsibility. Not only do they have visibility of the company's financial and business strategy, but they also have control of many of the technology tools already in place being used to make effective treasury decisions, such as information reporting and cash flow forecasting tools. By harnessing these technologies and closely aligning them with corporate goals, the CFO can be the primary driver for internal change initiatives and ensure a healthy pot of funds for the business.

New additions to the CFO's arsenal include mobility and big data tools which help provide real-time reporting and analytics. These enable the CFO to monitor and better understand treasury activity and requirements, as well as harness data from the rest of the business to make more effective decisions. This can be particularly useful for liquidity management where a holistic, real-time view can provide the CFO with a better understanding of liquidity and risk positions across asset classes, geographies and currencies. Furthermore, these technologies can provide the CFO with the right financial tools to forecast their cash flows, understand their working capital needs based on the cash flows, benchmark their business metrics against industry peers and drive operational improvements.

David Whelan, Director, Capita International Financial Services:

IT is central to the operational requirements of corporate treasury. The problem is that the information held and used on these systems is so important, confidential and market sensitive that it needs to be kept under strict control. That does not mean that treasury can function without the support of IT, but overall control needs to remain with treasury.

Treasury is an area where there is a limited number of operational staff, so IT can be invaluable in achieving effective segregation of duties, to cover access and control. However, the input of transactions and data and authorisation need to be separate from each other, to minimise the risk of errors and fraud.

Companies using ERP systems will often expect treasury to conform to a corporate systems policy to use a particular supplier, even though their specific treasury capability may be of limited value. Providers of systems usually try to absolve themselves of any responsibility for losses incurred as a result of using their systems. Therefore, IT should manage the systems – but they don't have the capability or experience to understand the exceptional risks which exist in treasury operations. Treasury must be accountable for errors and losses that might occur and should remain in overall charge of all its IT.

Bob Stark, Vice President of Strategy, Kyriba:

Treasury should be in charge of everything treasury, including IT responsibilities such as application support, performance monitoring, and disaster recovery. The obvious question of course arises: how is this possible?

The answer is simple: while treasury should be responsible for the support of their systems, they enable this by leveraging the cloud and an ecosystem of cloud solution providers that provide SaaS for treasury.

There are a number of important reasons why this should be the case:

- **Internal IT resources are scarce.** Treasury has specific and on-demand service levels, including high system availability and above-industry-standard business continuity requirements, no matter what the disaster. IT departments are not staffed to meet these needs, so treasury must turn to external providers.
- **Security.** Hardware and data controls are rarely sufficient when systems are hosted internally within an organisation, especially when treasury information is concerned. Therefore, greater safeguards are needed. IT resources are often insufficient to protect treasury's interests to the level that is mandated or recommended by internal or external auditors.
- **Cost.** Treasury's budget is usually quite low in comparison to other teams. To offer the service levels and security that the treasury requires unfortunately consume a disproportionate amount of budget compared with other teams. Cloud providers – offering better service levels and disaster recovery metrics – cost less than installing software in-house and, as a result, offer better value to the treasury team. This also frees up budget for other projects; never a bad thing for an aspiring treasurer.

The nice thing is that this isn't a tug of war between IT and treasury. IT doesn't want to be in the business of installing software and troubleshooting software conflicts; instead it wants to be much more focused on technology projects that deliver business value for the organisation. This means that treasury's shift to the cloud is completely aligned to IT's objective. ■

The next question:

"How do treasurers determine share of wallet with their banks?"

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

Are safe haven currencies back in vogue?

Five years into the financial crisis and many governments are still implementing monetary easing policies to help their countries out of recessionary cycles, most notably the European Central Bank (ECB). What impact will such actions have on 'safe haven' currencies?

In the weeks leading up to mid-May, the traditional safe haven currencies – the Swiss franc (CHF) and Japanese yen (JPY) – have declined against the euro (EUR) and the US dollar (USD). This movement was unsurprising for those watching the market. While Eurozone tensions are receding and US growth prospects are improving, the extremely low yields on Swiss and Japanese money products have nothing to offer to yield hungry investors. Yet, these safe haven currencies are expected to regain their appeal, particularly against the euro.

EUR/CHF

With its interest rate cut at the start of May, the European Central Bank (ECB) has begun a monetary easing cycle. Speculation on further rate cuts (including expectation that deposit rates will turn negative) and a predicted rise in Eurozone tensions later this year will cause EUR/CHF to drop towards 1.20.

Many German banks, in particular, have large liquidity surpluses and are presently placing most of this money with the ECB. Once they need to pay for the privilege, the German banks themselves will probably offer lower interest rates on deposits. Recently, many savers shifted their capital from the weak Eurozone countries to the German banks whenever Eurozone tensions took a turn for the worse. This reaction was mainly because these tensions could have triggered a euro collapse, in which case, savings – if left in a peripheral bank – would be denominated in a currency with a much lower value than the euro.

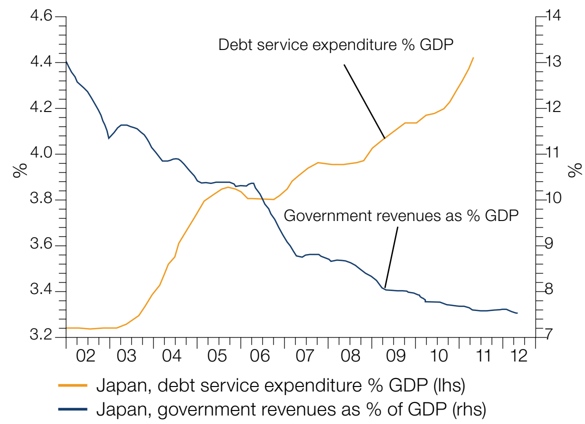
Depositing money with a Swiss bank is a sound alternative to placing it with German banks, even if a number of Swiss banks (intend to) apply a negative interest rate to foreign account holders. Such a disadvantage will become less significant once the ECB cuts its deposit rate below zero. This signals that any rally in EUR/CHF above 1.25 – 1.265 would be a good time to buy francs, particularly for investors who anticipate growing Eurozone tensions in the not-too-distant future.

And there is a real chance of the latter. Clearly, the Eurozone focus is shifting from reorganising public finances towards less fiscal austerity and more growth-boosting measures. The problem is that fiscal stimulus is no longer an option mainly because it costs too much; whereas a monetary impulse that is strong enough to accelerate growth is unlikely especially as Germany could well oppose this, even though it has reluctantly agreed to gradual monetary easing. In that case, mediocre growth prospects and large (and/or expanding) budget deficits in many weak Eurozone countries is a foreseeable outcome. All of this could whip up Eurozone tensions even further and lead to a drop in EUR/CHF (to 1.20) over the coming months.

The Swiss central bank, Swiss National Bank (SNB), will probably manage to defend the 1.20 floor for some time, which means that EUR/CHF could continue to hover around this level in the near future. Only if Eurozone tensions skyrocket and jeopardise the survival of the euro – which is unlikely to happen in 2013 – will it become too risky for the SNB to hold on to the peg.

Another scenario, although less likely, is also possible. Once deposit rates at the ECB turn negative, savers could abandon the low-yielding deposits in the core Eurozone countries and open deposits with banks in the peripheral Eurozone, where interest rates are higher. Such a capital inflow could even prompt a positive spiral. If so, the banks in the debt-laden member states will have more money at their disposal, which

Chart 1: Japanese government revenues as % of debt falls, while national debt servicing costs rise



Source: Thomson Reuters Datastream/ECR they can lend out or use to purchase government bonds in order to drive down long-term interest rates.

The latter has been happening during the past few months and, if the above scenario unfolds, it could continue for longer. The upshot could be fewer Eurozone tensions. If conditions continue to improve, non-EMU investors could be tempted to purchase euro assets, which would cause the euro to appreciate and drive down demand for safe haven currencies such as the CHF. In that case, an increasing number of investors would withdraw their capital from Switzerland in order to profit from a EUR/CHF rally.

EUR/JPY

Soon after Shinzō Abe entered the Prime Minister's office, the JPY weakened considerably against the USD and EUR. Recent figures showing that – for the first time in a long time – Japanese investors have become net buyers of foreign assets has added extra fuel to the rise in EUR/JPY and USD/JPY. If this development persists, a spiral could start whereby the outflow of capital weakens the JPY even further, as existing JPY investors face mounting currency losses. This will spur them on to sell their JPY assets.

Also relevant is the rise of Japanese bond yields. This also suggests that investors are selling Japanese assets (in this case bonds) and moving the proceeds out of Japan. Rapidly rising interest rates could sound the death knell for the Japanese public finances, as the country's national debt and budget deficits are very large. Owing to higher interest charges, the public finances will spiral out of control, more investors will sell government bonds and bond yields will skyrocket, etc. Before long, the central bank will come under enormous pressure to purchase more government debt (with newly created money) in order to prevent additional interest rate rises, which will weaken the JPY even further.

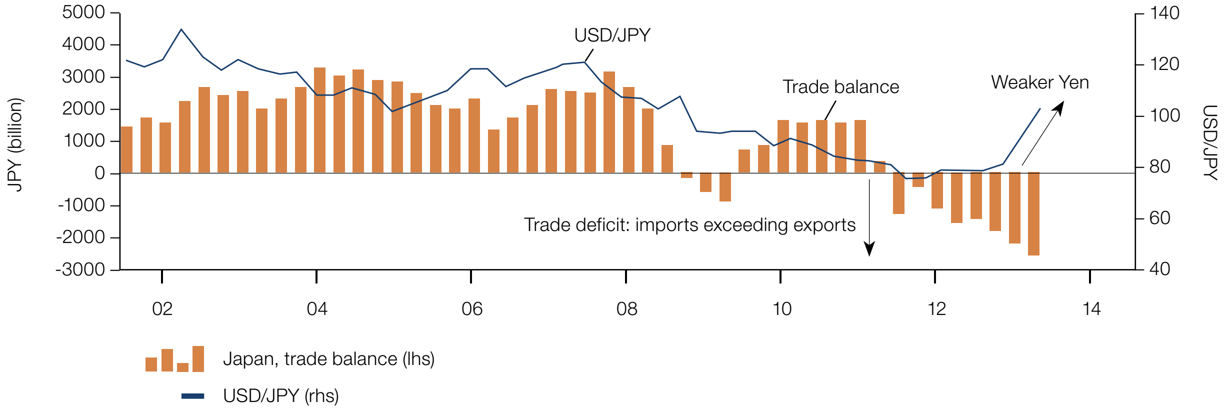
The risk is low that this will happen in the coming weeks to months. Theoretically, the bond yield rallies and the depreciation of the JPY could set off such a spiral, but there is also the following:

- The authorities have made it clear that a USD/JPY rally beyond 110 would do the Japanese economy more harm than good. Japanese exporters would benefit from a cheaper currency but the downside – higher import prices – would eat into consumer purchasing power. Therefore the authorities aim for an exchange rate near 100.
- Outside Japan, there is growing opposition to the rapid depreciation of the JPY. During the recent G7 meeting, Japan once again received approval to continue with its loose monetary policy. However, by now more central banks around the world are starting to ease their policies to prevent their currencies from appreciating too much.

Owing to the above, the Bank of Japan (BoJ) is not expected to pursue a far more accommodative policy than it has announced in the past period. These measures have already been discounted in the exchange rate of the JPY. The same is not true of monetary easing outside Japan.

To give one example, the ECB has cut its rate at the start of May and ECB President Mario Draghi has hinted at more monetary easing. Central banks in, among others, Australia, South Korea and Poland have lowered their key interest rates. Increasingly, this will put upward pressure on the JPY. In combination with an expectation of rising Eurozone tensions in the coming months, EUR/JPY is expected to drop towards 115 over the coming months. ■

Chart 2: Yen weakness aids exporters but also means Japan pays more for (increasing size of) imports



Source: Thomson Reuters Datastream/ECR

Cash: will it ever die?

Despite the score of business reasons why cash should be quietly killed off, its death-grip hold on the consumer means that most industry experts believe it will be around for a long, long time. But there are also new developments in the industry that corporates should keep tabs on.

Reports of the death of cash are greatly exaggerated. In 2010, $14.4 trillion of consumer payments were made with cash worldwide, compared to consumer payment card transactions valued (excluding commercial payments) at $9.582 trillion, according to 'The Global Cash Digest', published by global trade body the ATM Industry Association. A total of 62 billion ATM cash withdrawals worldwide in 2009, says the report, is forecast to rise to 94 billion cash withdrawals in 2015.

While cash is still around, the global volume of non-cash payments continues to show healthy growth, with the largest gain in volumes occurring in developing markets, according to the 'World Payments Report 2012' (WPR12). Non-cash transaction volumes grew by 7.1% to reach 283 billion in 2010.

Volumes jumped 16.9% in developing markets, boosted by an increase of more than 30% in both Russia and China. That growth far outpaced the modest increase in volumes in developed markets, which were still suffering the effects of the financial and sovereign debt crisis. Even in developed markets, though, the growth in non-cash payments volumes – at 4.9% – outpaced the rate of growth in gross domestic product (GDP), and developed markets still accounted for about 80% of all non-cash payments transactions globally. Debit and credit cards, says the WPR12, are the biggest driver of non-cash payments volumes globally. They accounted for 55.8% of all non-cash payments in 2010, up from 53.4% in 2009 and 35.3% in 2001. Debit cards alone accounted for more than one in three of all payments, partly as the use of cards for smaller-ticket transactions becomes more widespread.

But for many, cash remains king – and even more so since the onset of the global financial crisis. Rodney Gardner, Head of Global Receivables, Global Transaction Services at Bank of America Merrill Lynch (BofA Merrill), points out that in the US 43% of the population do not hold any credit cards and 20% have no type of payment card. Moreover, 17 million US citizens do not have a bank account. "For my corporate clients, the cost for accepting and handling cash must be accounted for. But there is opportunity for clients to take advantage of new technologies that can significantly reduce the cost of handling cash."

There is much discussion about cash dying out, but there are only two or three countries worldwide where less than 50% of payment transactions are made in cash, says Gareth Lodge, Senior Analyst in the Banking Group at financial industry analysts Celent. "By the number of transactions, cash is the dominant payment type in every country in the world. It is, in fact, typically more dominant than all other payment types put together," he says.

Most payments industry experts interviewed by Treasury Today admit that the demise of cash will be a long, slow burn. Moreover, it is difficult – or too early – to predict which non-cash payments instruments will prevail. However, cash is in the sights of financial institutions and governments as it is deemed to be expensive and vulnerable to criminal usage. Some of the typical reasons cash is being targeted are outlined in the Cashless Lagos Project in Nigeria, for example. Here, the government is supporting a cashless policy as part of a drive to develop and modernise the country's payments system.

New developments: Nigeria leads the way

Under the scheme, the Central Bank of Nigeria (CBN) has introduced a cash-handling charge on daily cash withdrawals or deposits, aimed at reducing the amount of physical cash circulating in the economy and to encourage consumers and businesses to switch to electronic payment (e-payments) transactions. The Nigerian government believes an "efficient and modern" payments system is "positively correlated with economic development and is a key enabler for economic growth".

Additionally, the cashless project is designed to reduce the cost of banking services, including the cost of credit, and to drive financial inclusion by providing more efficient transaction options and greater reach. Finally, it is hoped a reduction in cash transactions will help to improve the effectiveness of monetary policy in managing inflation and driving economic growth.

The negatives of cash, say Nigeria's authorities, manifest themselves in a variety of ways, including:

- A high cost of handling.
- High risk in terms of robberies and other cash-related crimes.
- A high subsidy – investigation has revealed that the entire banking population subsidises the costs of a tiny minority of cash users.
- The existence of money outside the formal economy, which limits the effectiveness of monetary policy.
- Inefficiency and corruption.

Authorities in other countries, including Canada, Sweden and the Netherlands, are also pursuing cash reduction initiatives. For example, Canada's MintChip, announced by the Royal Canadian Mint in 2012, is a digital currency for digital payment transactions, based on a secure smart card chip that can connect to computers and mobile devices. A survey of Canadians conducted by Leger Marketing in 2011 suggested that a majority of people in the country would be happy using digital forms of payment instead of physical currency. Of the 1512 Canadians surveyed, 56% said they would prefer to use a digital wallet and 34% said they would rather use a smart phone than cash to make a payment.

Additionally, in February Canada removed the copper one penny coin from circulation. Authorities cited the coin's eroded purchasing power, rising manufacturing costs, hoarding by households and the outlay by retailers in handling the coins as reasons for its removal. Other countries to have removed copper coins from circulation include Australia, Brazil and Sweden.

The Nigerian project is noteworthy because developing markets tend to be more cash-based for the reasons BofA Merrill's Gardner cites – low penetration of bank accounts, a lack of cards and higher poverty levels. However, in Africa more citizens have mobile phones than bank accounts and many organisations believe mobile payments (m-payments) represent a huge opportunity. This may be true but to date only M-Pesa in Kenya has been successful; a success that has proved difficult to replicate.

> "By the number of transactions, cash is the dominant payment type in every country in the world. It is, in fact, typically more dominant than all other payment types put together."
>
> Gareth Lodge, Senior Analyst, Celent

"In most emerging markets cash is still very much an integral part of buyer's behaviour and we do not see markets moving away from cash any time soon," says Karin Flinspach, EMEA Head of Payments and Receivables, Treasury and Trade Solutions, Citi. In such markets Citi works with companies that have innovative cash handling solutions that may reduce the risk and cost of handling cash.

"These innovative solutions include, for example, the use of terminals for immediate cash deposit after collection from the buyer and thereby removing the need to keep the cash in office premises, which poses risk and also delays the cash crediting process associated with traditional over-the-counter (OTC) deposits or cash pick-up deposits," she adds.

Generally in developed markets there is a strong trend towards "electronification" and digitisation, says Flinspach. "In retail, growth is mainly seen in online ecommerce, which popularises cards as a method of paying that in essence reduces days sales outstanding (DSO) to real-time confirmation."

In addition, online retailers are also searching for other instruments to integrate into their online platforms so that they can offer a wider range of payment methods to their customer base. "This is further accelerated by the fact that market infrastructure is changing for electronic transfers, so-called faster payments, and now allows for the instant movement of cash online which is very suitable for the online retail model," she says.

Celent's Lodge says in order to replace cash, the payments industry and businesses need to consider what cash does that other payments types don't do. "Payments behaviour is driven by habit and convenience, which are characteristics of cash. Anyone developing alternative payment systems has to compete with that." To date, debit cards have done a good job because many consumers regard them as an electronic form of cash. The number of people who switched from using credit cards to debit cards post-financial crisis was "staggering", says Lodge. "People know that debit cards represent what is in their account and therefore what they can spend."

The corporate cash conundrum

Bank of American Merrill Lynch's Gardner says corporates at times lack the complete picture of what impact cash payments have on their bottom lines. There are hidden costs with cash – a retailer will typically require reconciliation staff, people who could otherwise be on the floor making sales. Also, there is a high cost associated with the physical handling of cash because specialist security companies have to be paid to pick up and deliver cash.

Cash is trapped in stores until it is delivered to the bank and the corporate has no visibility over its cash position. One of BofA Merrill's focuses is on reducing cash in the business-to-business (B2B) sector. "Take, for example, a retail distributor – it will employ a driver to deliver goods to a number of small grocery stores, the proprietors of which are likely to pay by either cash or cheque. So the delivery van goes out full of goods and returns full of cash and cheques," he says. This has generated some interesting business models including companies that have instructed delivery drivers to convert cash into a money order at Western Union whenever a certain level of cash was reached, in order to reduce risk. At the end of the day the money order was then taken to a bank. "People at those companies thought about the risk connected to cash but didn't think about trying to get away from cash completely."

To reduce cash in these scenarios, Gardner says banks can set up electronic transfers between the grocery stores and the distribution company. It is important that these solutions enable the information to accompany the transaction, to make reconciliation as straight through as possible, he says.

What is tipped to replace cash?

While corporates mark time on the demise of cash and use solutions to reduce the pain and costs of cash handling, a debate continues about which non-cash instruments will succeed. At this year's International Payments Summit (IPS) in London, Niklas Bartelt, Managing Director at DZ Bank, said the question about whether m-payments would replace cash, debit and credit cards hinged on who would "pay to make that happen". He said m-payments would benefit retailers more than any other players in the payments industry (ie banks). "Retailers will be the winners with m-payments as they can be used to revolutionise and improve the point-of-sale (POS) experience and perhaps even help in the total rethink of how retail works," he said.

Any innovation in non-cash requires an infrastructure that will enable solutions to work. Marcelino Castrillo, Head of SME for Santander Corporate and Commercial, says cash will be around for a long time as it is perceived by some groups – those on lower incomes, students and the elderly – as a better way of managing their finances and controlling their spend. Any alternative to cash will have to provide the control of finances that is valued by cash users and be more convenient. Like Flinspach, he cites immediate payments, such as the UK's Faster Payments, as an important move. "Faster Payments in the UK is providing an infrastructure for alternative payments instruments. Plans to link mobile numbers to bank accounts will be a further step towards non-cash payments."

Chris Dunne, Payment Services Director at UK payments processor VocaLink, which operates Faster Payments, says the mobile proxy database will target friction in the system. At present, anyone wanting to pay someone via Faster Payments has to set them up as a new beneficiary in their bank account, which can be a convoluted process. The main UK banks have committed to the project, which will enable users to give their mobile number, rather than bank details to the person paying them. "People will feel this is a more confidential system. It also has the potential to be a mass market solution that will reduce friction. Cash has very little friction but it does depend on the payer and beneficiary being in the same room."

> "Retailers will be the winners with m-payments as they can be used to revolutionise and improve the point-of-sale (POS) experience and perhaps even help in the total rethink of how retail works."
>
> Niklas Bartelt, Managing Director, DZ Bank

Dunne says the mobile database has been built for peer-to-peer (P2P) m-payments; a much broader set of applications will also be developed for corporate applications, enabling request for push payments. "We are building an ecosystem that will allow the biller to send an invoice to a customer on their mobile phone. All of the invoice details will go with the payment, which is important for companies as they need to know which transaction a payment is related to."

Picking the winners and losers in non-cash instruments is difficult. Marcus Treacher, Global Head of eCommerce for Payments and Cash Management at HSBC, predicts that smartphone contactless payments could quickly reduce cash payments significantly in many parts of the world. "That will have a huge impact in terms of cost reduction on the cash cycle and more efficient receivables handling for bank processing centres and large retailers such as supermarkets." Today one in seven payment transactions below £20 at Marks & Spencer stores have been made via contactless cards; Pret a Manger, a very early adopter of contactless cards, has seen the use of contactless payments grow from 3% to 20% since they were introduced in 2008.

Contactless card solutions are becoming more integrated with smartphone devices, which will accelerate the mass adoption of m-payments using technologies such as NFC, he adds. "There is a great deal of innovation occurring in the mobile and cloud arenas. Although it is difficult to work out what and who will be successful, the clear trend is towards contactless payments. Mobiles will increasingly displace cash because they will be used to make e-payments, but it will take a while." ■

What's yours is mine

Fraud is a perennial problem for businesses and tackling it seems to require a level of cunning that fraudsters themselves would be proud of. But instead of keeping the lid on it, experts say the best response is to be more open and communicative. Are you ready for change?

Whatever anyone does to try to prevent it, fraudulent activity will never go away. Corporate treasuries have the same fraud risks as anyone else, but given the access treasury has to strategic information, pools of funding and payments mechanisms, they are also subject to some bespoke risks and potential for major loss. The risks need to be mitigated.

Alongside the processes and procedures laid down by a company as the framework in which its employees are expected to operate, there is the element of the people themselves who have different and unpredictable needs and behaviours. There is also a technology element that can put controls around the people and ideally some workflow around the processes, but this can also complicate matters. "Where these three elements come together, if you get them right you can significantly reduce your corporate fraud risk," says Steve Wright, Product Development Manager at payments processor, VocaLink. But, he adds, although the idea is to "make it as difficult as possible", fraud is an ongoing threat: if a criminal is determined to act, then they will.

With this in mind, all these usual practical measures – including controls around passwords, clear-desk policies, training against social engineering, locking computers when away from the desk, implementing banking processes that require multiple approvals, segregation of initiation and approval of payments – are just "basic things that apply to any business", according to Bill Trueman, Managing Director of corporate fraud and risk management consultancy, UK Fraud. What is really needed is a change of culture. The common corporate practice of keeping the lid on fraud only serves to perpetuate it and, says Trueman, building silos of risk and compliance expertise into each corporate function (including treasury) serves to limit the level of communication and thus the agility of the business when responding to the threat.

All change

The nature of corporate fraud, notes Trueman, has moved beyond the relative simplicity of the corrupt office manager and the occasional "weights and measures issue" with a supplier and into a sophisticated world where highly intelligent professionals – and professional criminals – will manipulate processes and procedures to inflict heavy damage, both financial and reputational, on their targets. The defeat of a modern sting can thus require multiple corporate functions to co-operate and communicate as never before.

The motivation behind corporate fraud varies considerably, the methods ranging from the desperate and stupid to the ingenious. Fraudsters may act alone or as part of an organised crime syndicate. They may be part of the company or have no connection. But in the corporate world, when a fraudulent act is revealed, the sums involved can be staggering.

Indeed, recent history has thrown up three monumental cases of corporate fraud. Each was inflicted upon a multi-billion dollar business and saw their CEO convicted and sentenced to a long prison term for their efforts. Former Tyco CEO, Dennis Kozlowski, was convicted in 2005 of misappropriating more than $400m to fund his extravagant lifestyle (which allegedly required $6,000 shower curtains). The CEO of telecoms firm, WorldCom, Bernie Ebbers, was convicted in 2005 of fraud and conspiracy in the US's largest ever accounting scandal. False financial reporting caused investors to lose more than $11 billion. Around the same time, the Enron scandal hit. Its CEO, Kenneth Lay, played a major part in what was termed an "institutionalised, systematic, and creatively planned accounting fraud" that led to the collapse of this US-based energy, commodities and services company. Lay was found guilty in 2006 of multiple counts of securities fraud. He died before he could be given a custodial sentence which was expected to be 20 to 30 years.

These high profile scandals served to cast a dark shadow over the accounting practices and activities of many US corporates, and the realisation that all was not well had earlier heralded the arrival of the Sarbanes–Oxley Act of 2002, which placed culpability for accounting inaccuracies directly in the lap of CEOs who signed off financial statements. That year also saw the award for the IgNobel Prize in Economics (an American parody of the Nobel Prize) go to the CEOs of various companies known to be involved in the corporate accounting scandals. Each was lauded for "adapting the mathematical concept of imaginary numbers for use in the business world".

There may be dark humour to be extracted from this situation, but the 2013 AFP Payments Fraud and Control survey shows that 61% of organisations questioned experienced, attempted or actual payments fraud last year. Some 27% reported that the number of fraud incidents had increased, with affected organisations being hit more often, indicating that the fraudsters know they are a soft target and, more worryingly, that nothing had been done to close the breach.

The latest findings from the UK's fraud prevention service, CIFAS, saw its member organisations (spread across multiple sectors) report a 53% rise in 2012 of facility takeover fraud – unlawful access to and fraudulent operation of an account. In a survey published in December last year by EuroFinance, more than a third of global financial professionals stated that they had worked in an organisation in which serious financial malpractice had taken place. The prevalence of fraud is a concern but, according to the survey, there is a serious obstacle preventing companies from tackling it head on.

Corporations, it seems, are far less likely than banks to prosecute fraudsters. Some 57% of respondents said that whistleblowers severely risked damaging their careers by speaking out. When serious financial fraud had been detected, 42% of corporate respondents said that the perpetrators had been fired but that the issue was merely hushed up. Of the banks, 76% of respondents said the guilty party had been prosecuted. Whilst corporates are seemingly prepared to get tough on minor fraud cases, they are not prepared to risk seriously damaging company reputation (and potentially their share price) by going public, and so they often sweep it under the carpet. According to Melvin Glapion, UK Managing Director of global risk and security consultant, Kroll Advisory Solutions, this reluctance to face up to the issue sends out all the wrong signals.

Know your employees

Whilst fraud will always present a challenge, Glapion feels that unless companies establish an appropriate culture around this topic it will remain a taboo. Failure to tackle the underlying problem will not make it go away.

The major corporate fraud that takes place is usually internal, notes Trueman. The perpetrator is often at a relatively senior level and will nearly always have a personal issue (such as a gambling habit) or corporate issue (being overlooked for a promotion) driving them. "Usually the fraud involves significant amounts of money," he says. Sophisticated stings are much in evidence but most often are based on a deliberate 'conflict of interest' where the perpetrator will work with an existing supplier and arrange to overpay for products, or they will work with a relatively new supplier to the company and receive a kickback from them in exchange for continued business.

As such, corporate fraud tends to be an ongoing problem. "If regular payments go to the same supplier, the name becomes familiar within the immediate company in terms of invoicing," Glapion explains. It thus becomes commonplace and unremarkable. Once it has become a part of the system it is much more difficult for other staff, especially at a junior level, to question it.

The challenge for a corporate is in how to identify and mitigate such fraud, says Trueman. A possible deterrent that can also be an investigative tool may be found in a back office IT system that can create an audit trail for every process carried out by staff. But, he notes, the fraudster will know how to sidestep these systems (just think of Nick Leeson or Jérôme Kerviel).

IT toolkit

VocaLink's Wright argues the case for as much automation and straight through processing (STP) of accounts payable (AP) and receivable (AR) as possible. As well as eradicating points of intervention and creating a clear audit trail, he says that it removes the need for back office staff to have access to bank accounts and core systems, or for others to handle sensitive account details on bits of paper. "If someone is manually assigning receivables to a particular account and they have found a way of diverting those funds, and if they are also doing the accounting, the fraud can go undetected for years." He adds that if someone gets away with it once "invariably they will go back again and again and it only comes out when it has become a big problem".

Automation clearly has a key role to play in prevention, but when it comes to fraud detection Glapion notes that relying on "algorithms and analysis" to try to figure out where fraud is going to occur and who is going to do it is part of the toolkit "but it is not the answer in itself". For Glapion and Trueman, the key lies in being able to monitor and understand employees at a more human level. Internal fraudsters may exhibit behavioural traits such as obviously living beyond their own means or refusing to share workload or take holidays. Observing such changes is a key part of detection.

Who are you?

All businesses therefore need to be able to answer a very basic question: who are the employees in the company, particularly in the finance, sales and marketing and executive teams? Details such as address and spouses name and employer can be cross-referenced with the company's database of key suppliers to see if there is any matching information. "We do find conflicts of interest which have not been disclosed to the corporation," Glapion says.

However, in some countries, harvesting and cross-referencing this kind of data is illegal (in Germany, for example). He urges all businesses to "think outside the box" when it comes to looking at how legitimate information can be checked to ensure there is sufficient basic knowledge about all employees.

Related to this is the more pressing need for companies to carry out background screening of those in or being considered for key roles. In treasury, says Trueman, the task takes on greater importance because of the sensitivity of the information they may have access to, including strategic corporate information and any trading and merger and acquisition (M&A) activity.

"You'd be surprised at the number of companies that don't do this," comments Glapion. "Many tell us that they don't feel comfortable prying into personal lives. But quite frankly, it is just basic due diligence. They will do it for M&A transactions and on the financial side for tax and pensions reasons, so they certainly should be doing it when employing key personnel."

A credit check can be a useful indicator of an individual's propensity to be compromised. But for key employees it is necessary also to uncover any issues around litigation or criminal records and to acquire 'human intelligence' by talking to people who have worked with or have been involved in deals with this individual. It is, Glapion notes, "basic common sense" that the higher up you go in an organisation the broader the scope of enquiry should be. "Candidates looking for a very senior level position should expect that the company possibly about to hire them will want to know more about them." Some searches require permission; any candidate that refuses may be hiding something (but it may just be an objection on moral grounds).

Watching the watchers

The task of checking and monitoring staff is often seen as the responsibility of HR. But for Glapion, this is "much more of a commercial responsibility" and should be shared with General Counsel (the legal head), HR and other key department heads such as finance and sales and marketing. Department heads should be looking at individuals within their department and asking for the information at the point of hire and reviewing that information every one or two years. Indeed, if there has been a change in an employee's circumstances or behaviour it may be necessary to review their levels of access and authority and be "mindful of situations" that could place them in a position where they may be compromised.

Accepting that many people are uncomfortable talking about these investigative activities, Glapion insists that they are absolutely necessary. No individual should be above this process, from the CEO and Board down, and this is why the responsibility sits well within the legal division and not HR.

A cultural shift

To counter inevitable accusations of Big Brother-type surveillance, it's necessary to normalise the checking process, making it part of company policy and bringing it into the open so that everyone knows it is part of the process. Whilst the information gleaned must be treated with absolute confidentiality, the discovery process itself should never be covert, as this engenders mistrust and suspicion.

When a company is subjected to a major fraud it will almost certainly and understandably close ranks and seek to suppress it. There may be certain aspects that have to be reported in the accounts, says Wright, but he adds that "no one wants to make public where their issues are". This secretive approach can permeate the business and create an environment in which discussion is awkward, if not impossible. If individuals do not feel comfortable communicating their concerns upwards it can enable someone to operate outside of policy and procedure unhindered.

Companies need to state the absolute expectation that all communication is made through the official channels and not conducted in secret. It also needs to be asserted that individuals will not be subjected to any repercussions if they report something that they believe to be out of the ordinary, even if it means reporting something about their direct manager or the CEO.

If this out-in-the-open approach is enshrined in policy it will be seen as a genuine requirement that will be taken seriously. "Companies should also be able to demonstrate it in action, even with something that didn't result in finding fraud," Glapion advises. "If an employee in a subsidiary discovers something unusual that relates to a senior executive and it transpires that it was nothing, there is no reason not to praise that employee for raising the matter to show other employees that this is what is expected of them, as a means of combatting fraud."

Another matter that should be addressed is the standing that fraud prevention often has in the hierarchy of corporate needs. In the current environment where personal budgets are squeezed and redundancies are hanging over ever more people, the temptation to defraud an employer can escalate into a need, notes VocaLink's Wright.

The corporate investment agenda tends to be driven by revenue, profit or cost simply because these are areas that most can relate to within a business case. When tackling fraud, Wright notes that many companies will implement measures only when their business has been hit because it is a pure cost centre. "It's one of those things that people believe probably won't happen to them," he notes. But unless tackling fraud is moved up the agenda, enabling firms to put the right measures in place and to look at the intersection of people, processes and technology, how confident can a business be that it is not already a victim? ■

Milton Friedman

In the polarised cold war landscape of the 1960s and 1970s, Friedman, an uncompromising advocate of free market economics, was unquestionably a divisive figure. Yet even his fiercest detractors today concede that his influence on both the economics and politics of the 20th century was enormous – matched only by that of his great philosophical adversary John Maynard Keynes. Treasury Today assesses the legacy of the economist credited as the intellectual spearhead of the counter-Keynesian revolution.

When Milton Friedman, an American economist, began his career as professor at Chicago University during the 1950s and 1960s, Keynesian ideas were the dominant force in macroeconomic analysis. In the years following, the World War II Western governments, with the depression of 1930s still fresh in their minds, began to move away from the laissez-faire approach to economic management that had until then been the dominant force in most capitalist states. But by 1976, the year Freidman collected his Nobel Prize, Keynes' hegemony in economics had, for a while it seemed, been overthrown with monetarism firmly established as the new orthodoxy.

Inflation: it's the money supply

Friedman's economic theories led to many important developments in the 20th Century – however, it was his restating of the quantity of money theory that cemented his reputation as a leading economist and earned him the Nobel Prize.

In the late 1950s, a New Zealand-born economist A.W. Phillips gained recognition for his observation of a historical correlation between unemployment and inflation. Periods of high unemployment were often accompanied by periods of low inflation, and vice versa. However, governments, mistakenly, came to believe this historical correlation suggested a permanent trade-off between inflation and unemployment. If a government wanted to stimulate employment, then that increase could, in a sense be bought, at the expense of higher inflation.

Friedman pointed out that the relationship between the two may hold – up to a point – but there could be no permanent trade-off. Inflation might lead to higher levels of employment because it becomes increasingly profitable to hire workers if prices rise faster than wages. However, if high levels of inflation continue for a sustained period then workers, understanding that their purchasing power is being diminished, will begin to bargain for higher wages in advance. Eventually, wages will to rise again in line with inflation and higher unemployment will inevitably result, whatever adjustments governments make.

"During the 1950s and 1960s, it looked as if Keynesian interpretation was right," Friedman would later recall. "After all we had relatively prosperous countries, relatively stable prices as well as relatively low interest rates – it was a golden era."

But this 'golden era' proved to be very short-lived. In 1973, an oil embargo declared by the Arab members states of OPEC knocked the wind out of the global economy and, as inflation and unemployment soared, helped to trigger a crisis of faith in the Keynesian paradigm. According to Friedman, "during the 1970s, you had a combination that under Keynesian analysis could not exist. You had high inflation and high unemployment at the same time – something named 'stagflation'. It was that experience, more than anything, that led to a change in public and intellectual attitudes towards money."

Under the strain of the 1973 Oil Crisis, the historical correlation between the rate of inflation and unemployment broke down – as Freidman had foreseen five years earlier. Predicting the occurrence of stagflation cemented Friedman's status as one of the leading economic thinkers of the day with both his peers and the wider public. His insight also prompted a paradigm shift in the political economy of the day; helping to smash the Keynesian consensus by providing intellectual backbone to the neoliberal reforms enacted when Ronald Reagan and Margaret Thatcher came to power in the late 1970s and early 1980s.

Monetarism, the economic school of thought promoted by Friedman as an alternative, contended that since inflation was a problem of "too much money chasing too few goods", limiting the growth of the money supply would be the most effective solution to the problem of stagflation. To keep inflation in check, he recommended that central banks should be tasked with increasing the money supply at a steady, low rate of 2%-3% from which they would not be permitted to deviate, regardless of how the economy is performing. His instinctive distrust of central bankers even led him to propose a more radical, although perhaps less realistic, remedy – getting rid of them altogether. "I've always been in favour of abolishing the Federal Reserve and substituting it for a machine programme that will keep the quantity of money going up at a steady rate," he once said.

A free market ideologue

Friedman did not spend his entire career as a public intellectual working to produce largely apolitical analyses of economic phenomena such as inflation. There was also another side – Friedman, the free market ideologue.

Using a range of media platforms, such as his weekly column in Newsweek and his TV series 'Free to Choose', he persistently endeavoured to spread the gospel of free markets.

On this principle, he saw no room for compromise. Whatever the issue was – healthcare, education, even the global trade in recreational drugs – he favoured free market solutions and steadfastly opposed any call for government intervention.

His tireless efforts appeared to be rewarded. In the 1980s, Western economies began to shift back to the same laissez-faire approach to economic management that had prevailed prior to the Keynesian revolution. Protectionist trade policies began to be reversed, regulation was loosened and the public sector beat a hasty retreat from many areas of national economies. Today, most economic historians acknowledge that Friedman's free market activism was a factor in the speed of this ideological reversal, even if the economic mess of the late 1960s and 1970s had made the return to liberal economics almost inevitable.

Monetarism – a flawed idea?

Through his work on prices, Friedman had correctly identified the in-built weaknesses of the Keynesian approach to economics that had brought about stagflation in a number of capitalist nations in the 1970s. However, some economists today continue to dispute whether the solution he prescribed, monetarism, achieved its objectives when put into practice. In the early 1980s, both the US and UK experimented with monetarist policies, attempting to control inflation by limiting the growth of the money supply. The results were mixed.

In the US, unemployment soared and the experiment was quickly abandoned. Meanwhile, under the rule of Friedman's loyal disciple Margaret Thatcher, the UK persisted with monetarist policy. Inflation was successfully brought under control, reduced to 4.3% by 1983, down from an astronomical rate of 27% in the mid-1970s.

Since then, central banks in Western economies have adopted a much more flexible approach than the one Friedman advocated. The US Federal Reserve, for instance, responded to recession in 2001 by slashing interest rates and allowing the money supply to inflate. Then, once the return to growth was assured, interest rates were raised and growth of the money supply dropped to zero. And all this, it should be noted, took place even under the supervision of the self-proclaimed monetarist Alan Greenspan.

Paul Krugman, the Economist and New York Times columnist, is one of the most high profile critics of monetarist theory. Writing in 2007 an essay for the New York Review of Books, he contended that modern central banks were remarkably successful in their application of the "discretionary fine-tuning that Friedman decried". Inflation, he wrote, by and large remained at acceptable levels throughout the 1990s and early 2000s, and recessions, when they occurred, tended to be briefer and shallower compared to downturns in the previous decades – this, of course, was written prior to the cataclysmic events that unfolded in the autumn of 2008.

But if the experiences of Western economies in the past two decades raise questions on the practical applicability of monetarism, the story of China's stratospheric ascent during the post-Mao years offers some evidence to the contrary. In 1988, authorities in Beijing, troubled by double-digit inflation, turned to Friedman for guidance. As expected, Friedman advised the Chinese leadership to rein in growth of the money supply – the alternatives, price controls or rationing would only serve to exacerbate the problem, he argued. China took Friedman's advice and inflation returned to acceptable levels where it has since remained.

The 'miracle of Chile'

Friedman's role in the supposed 'miracle of Chile' is undoubtedly the most contentious facet of his legacy. In the early 1970s, Chile suffered a severe economic crisis followed by a social and political crisis. The outcome, the overthrow of the democratically-elected government of socialist President Salvador Allende in a coup d'état by General Augusto Pinochet, proved to be the watershed moment – not only in the history of Chile, but also in the Cold War.

After seizing power, Pinochet and his military junta, acted on the advice of Friedman and the 'Chicago Boys' and quickly set about undoing the economic and public policies of his predecessor. State enterprises were auctioned off, financial and trade regulations were abolished and the countries nascent welfare state dismantled.

The fact that Chile now stands as one the strongest economies in the Americas is, Friedman's acolytes argue, a testament to the value of economic liberalism. Others, including Krugman and Indian economist Amartya Sen, insist that sustained economic growth was only truly realised until the late 1980s, by which time Pinochet's hard-line free market policies had been considerably softened.

But whatever view one takes on the economics, Friedman's association with a regime which violently disposed of an elected government and crushed dissent from left-wing activists and union members with torture and murder is undeniably a blemish on his reputation. Friedman was once reported to have said that, "history suggests that capitalism is a necessary pre-condition for political freedom." But the history of Chile in the latter part of the 20th Century seems to suggest something entirely different.

The return of Keynes?

Today, history seems to have come full circle. Following a financial crisis that has been widely described as the worst since the 1930s, it seems only natural that governments across the world once again turned to the ideas of Keynes.

In the immediate aftermath of the 2008 crisis, governments in the US and Europe proceeded to enact large fiscal stimulus packages; borrowing and spending to offset falling demand in the private sector. It was precisely the solution Keynes would have prescribed, and precisely the sort of move Friedman would have opposed.

But those who argued that the financial crisis spelled the end of Friedman's contemporary relevance were perhaps guilty of speaking too soon. For one thing, the austerity measures enacted in the UK and Europe over the past few years appear to be straight out of the Friedman textbook. He would have certainly approved of the logic, frequently espoused by the governments of the UK and Germany, which says that nations cannot address a budget deficit by spending money. However, he would have set delimited time periods to quantitative easing (QE), as he did during Japan's deflationary crisis in the 1990s when he advocated "until the high powered money starts getting the economy in an expansion". ■

Black belt treasury

Peter Schädelbauer
Head of Group Treasury, Lindner Group and
Managing Director, Lindner Finanz

Peter Schädelbauer's moves over the years from banking to corporate finance and treasury have armed him with a thorough understanding of how businesses operate. He also has a keen sense of order and balance, which has a lot to do with his expertise in the martial art of karate.

The Lindner Group KG, based in Arnstorf in Bavaria, Germany, is one of Europe's leading companies for the building envelope, interior fit-out, insulation and construction-related services. Founded in 1965, the 100% family-owned business manages production plants and subsidiary companies in more than 20 countries across Europe and beyond. Lindner Group KG's annual report 2011 revealed an operating income increase year-on-year of 22%, from €698.4m to €851.7m, with a balance-sheet total of €671.8m. Equity stood at €397m giving an equity ratio of 59.1%.

Despite the best efforts of certain governments to continue with infrastructure projects as a means of kick-starting their economies, the construction industry around the world generally remains troubled. But not every company engaged in this vital sector is struggling. Germany-based Lindner Group KG, a provider of what it describes as 'building envelope, interior fit-out, insulation and construction-related services', has not been immune to global financial upheaval, but according to its most recent financials, it has "excellent liquidity" at its disposal and an investment-grade credit rating with its banks. Recent negative developments in the Eurozone – the heartland of Lindner's business – have put more pressure on the company's general outlook, but it is responding in a way that few could see as anything other than impressive.

In short, it is a well-run business. Pre-crisis, as a cash-rich company, accurate cash forecasting was little more than a 'nice-to-have'. The full effect of the 2008 crisis was somewhat delayed for Lindner as it had a number of major projects still with up to 18 months to run, but it realised well in advance of their completion that it had to take steps to protect itself, not least from the increased possibility of customer default. Liquidity planning and rolling forecasts were rapidly elevated to 'essential' status – a strategy put in place by the firm's Head of Group Treasury and Guarantees and General Manager of Lindner Finanz, Peter Schädelbauer.

"We had to bring a lot of information together and create a new business plan to prepare the company for impact," he recalls. The extent of his work over the years earned him a 'Highly Commended' in the Best Process Re-engineering Solution category of the 2012 Treasury Today Adam Smith Awards and crucially places Lindner in a stronger position to face the future.

The move to Lindner

With more than 23 years' professional experience in the finance field, Schädelbauer, who had spent a decade rising up through the ranks of the German banking sector before moving into commercial treasury, moved to Lindner in February 2006. Here he took up a managing role within its banking department. This was not treasury per se but it handled most financial matters such as payments and bookkeeping. However, change was in the air and his cumulative experience enabled him to oversee the development of Lindner Group's central treasury department, in-house bank and ultimately the creation in 2009 of Lindner Finanz which now acts as the main treasury and finance function within the group.

Having already seen positive results from the closer integration of functions and the optimisation of a number of processes and systems (including the creation of new reporting structures), the board (comprising the Lindner family) fully understood and supported the notion that to move forward, the company needed to invest in a major new software implementation. It sanctioned a discovery phase that kicked off in 2007, Schädelbauer citing this as "the beginning of the plan to optimise our processes to become a modern treasury".

By 2008, driven by increasing complexity (new subsidiaries were being created and acquisitions integrated), the company commenced implementation of its first treasury management system (TMS). With Schädelbauer now fully ensconced in the treasury hot seat, a three-month market investigation provided a shortlist of three systems and ultimately a deal with Germany-based BELLIN.

The overall finance function now has nine staff (a mix of full and part-time) covering areas such as performance guarantees, billing, credit management and insurance as well as traditional treasury functions such as cash management. There was some scepticism from individual departments when their amalgamation into a group treasury was first mooted, but with the changes made in the past few years, inter-departmental working has enabled Lindner to vastly improve its finance function, each function now bringing information and understanding that the others do not have, benefitting all.

One of the outcomes of this co-operative development has been the creation of a major new financial report. It delivers vital information about the cash position, capital developments, outstanding amounts and so on, all in one monthly retrospective report, with specific weekly reports produced for matters such as liquidity and cash.

With around 15 banks and 300 bank accounts worldwide it was, states Schädelbauer, vital for Lindner to deliver the TMS and new reporting regime so that it could have an accurate and timely overview of group liquidity. Treasury now receives SWIFT MT940 electronic account statements, these being uploaded into the TMS, which records every transaction.

As part of its strategy for improved oversight, Lindner has also implemented an inter-company netting system. This covers all internal payments and is executed by the TMS before being uploaded to the ERP system (a bespoke development used group-wide from German vendor, Oxaion) for booking and so on. With these changes most transaction data from its banks can now be integrated within the cash forecast plan. The process itself is highly rules-driven and is currently capable of processing around 95% of all transactions, giving a daily cash overview of the all main entities within the group.

Technology is seen by Schädelbauer not just as a nice-to-have but as an "absolutely essential" part of Lindner's treasury operation. Whilst treasury skill and judgement remains an essential part of the role, automation and process optimisation has enabled the expanded function to reduce many processes to minutes rather than hours. "When I started at Lindner there were five people in the banking department. It would be absolutely impossible with the staff we have today to run all the services we have now in treasury without technology; we should have a lot more people."

The choice of 15 banks (where some firms of this size might work with just a couple) is part of the policy never to limit partnerships. A small number of core banks are used alongside a spread of other institutions. "It means more work for us but it benefits us too because we can easily compare banks, their terms and conditions."

Lindner's bank relationships are far from casual though and it has put in place limits and systems to monitor their performance. Data for analysis is drawn directly into the TMS from the treasury's ancillary systems. As an example, where previously it had relied upon single bank connections for FX trading, Lindner now uses 360T's multi-bank portal. The reporting tool enables easier performance comparison giving treasury a single view of which banks are offering the best deals over a specified period. The results are used to drive discussions with those banks, securing the best deals. Based on actual savings, 360T, he says, "paid for itself in six weeks".

Taking control

At a departmental level, Lindner's credit management and insurance department is a prime example of how the firm has taken control and shaped its destiny. It no longer pays for credit insurance, instead running its own checks and setting its own limits. The decision to dispense with annual insurance costs is an interesting one: as the recession bit harder and many customers faced difficulties, the credit insurance that was available was often too expensive or highly restrictive in terms of which customers were accepted. By taking it upon itself to check customers' credit worthiness and their ongoing status as paying customers (or otherwise), Lindner has been able to safely increase the number of customers it deals with. It is able to gather external information (from ratings agencies, for example) and data from its own records, to build a risk profile for each. From this it can create its own scoring, rating and credit limit which can be revisited as required or as credit events occur. "Because we monitor customers ourselves, we have more interest in the process and take more care," notes Schädelbauer.

Indeed, as much of the order-to-pay (O2P) cycle is now in-house, any signs of customer default or a change in payment behaviour can be handled immediately. Additionally, if a customer requires a greater credit limit or different terms the credit department can make its own provisions, for example by ensuring the right performance bond is in place.

SEPA is the process du jour for many corporates, and having started a project to create the required environment in mid-2012, Lindner's work on this is about 80% complete. "In December we tested Lindner Finanz completely for single and bulk payments," says Schädelbauer. "Our ERP system is ready so we now need to prepare the system for creating STEP2 (the pan-European automated clearing house payments). We are on schedule to completely finish by September 2013."

Schädelbauer is somewhat less sanguine about the actual benefits of SEPA though, arguing that it is not in reality a single payments area as every country still has its own format for XML files and separate ways of handling this. The dream of having access to every bank in Europe with just one file, he states, is not real. "There are still a lot of separate regulations. Overall SEPA has some benefits, but I don't think it makes things much easier. It's still too complicated."

On the subject of complexity, he cites the European Market Infrastructure Regulation (EMIR) as another source of frustration. EMIR is the EU's regulation covering all entities that enter into any form of derivative contract and concerns improvements in transparency and risk-reduction. "We execute a lot of deals internally and we also have to report those contracts. This creates a lot of work for us. The idea is to protect the market from speculators; making new regulations for companies is not the right way forward."

Cash rich

Lindner Group does not have an external rating but its bank rating is currently investment-grade. Although it relies on its current cash flow and assets to support its general activities, from time to time significant long-term investments are made which do require a bank loan, such as its acquisition in May 2011 of UK-based Prater Ltd. (a building envelope specialist). "We also have credit lines on a daily basis with the banks so that if we have a project where we need say €1m or €2m for a couple of days, we have that facility."

Of course, cash rich still requires prudence and any excess cash is invested in two ways. Lindner Finanz handles all short-term investments, up to one year, using instruments such as floating-rate debt and money markets. Longer-term investments are executed by a specially appointed external investment panel consisting of four managers, each from a different institution. It has a discretionary approach based on a medium risk profile. Its quest for a steady return (typically between 3% and 6%) operates within pre-set limits. A competitive environment, in which the performance of each manager is reviewed at three and six month intervals, keeps investments on track. Every few years the panel of four managers is assessed, Lindner setting up a "beauty contest" to decide which are retained.

With optimised processes, controls and technology in place, the major concern for Schädelbauer lies beyond the company walls. "At the moment the euro-crisis is something that I think about in terms of how it will impact on the business, but this is probably something that every treasurer is thinking about." Action has been taken by Lindner to deflect the worst effects. Some operations, such as those in Slovakia and Spain, have been scaled back accordingly, yet the company has retained at least a skeleton staff and business function so that the units can be scaled back up again once the construction industry returns to form.

Lindner is fortunate in that its products and services can be deployed almost anywhere in the world. It has thus been able to move into new markets to try to offset the decline of others. Australia, Turkey, the GCC countries, Brazil and the US are all presenting new opportunities. "As a family-owned business, we can make quick and effective decisions, but as other companies move into the same regions the competition inevitably becomes tougher. We always have to try to predict how the business will develop when thinking about new possibilities."

Looking to the future

Future-proofing a business is difficult, but Schädelbauer is certain that standing still is not an option. "Treasury is an evolving process and one idea I have is to develop Lindner Finanz into a clearing centre for the group, turning it into a real banking function, like a central bank for the group," he reveals. He adds that although this ambitious project "remains a dream", he is making provision for such an event.

Indeed, Schädelbauer takes his duties seriously and is keen to impart his knowledge for the benefit of others. He is a member of the German treasury association, Verband Deutscher Treasurer (VDT), has written many articles and is a seasoned speaker at various professional conferences such as Finance Symposium.

Since 2006 he has found time to volunteer for Caritas, an international relief, development and social service organisation. Schädelbauer manages the financial function of his local unit in the Bavarian town of Vilshofen. One of its roles is to help those with financial worries, maybe as a result of a bereavement or accident. "For me it is important to understand what can happen to individuals or families when financial circumstances change for the worse."

Accepting that events can take over and that they therefore have to be approached with an ordered mind is a philosophical approach that is in part borne out of Schädelbauer's devotion to the martial art of karate. At first glance this seems not to have anything to do with the role of the treasurer. But he takes the view that both require many years' training to master the basics before developing a personal approach. "In the first stage you watch and learn and in the second you create your own way." But the connection is more than just one of basic training. Karate, he explains, teaches patience, belief and core strength, attributes that any treasurer working in the current environment would do well to nurture. ■

Taxing times in Asia

Profit shifting and transfer pricing have been hot tax topics in Asia for many years. However, recent developments in tax policy in Australia, India and China in particular, have highlighted the challenges facing corporate treasurers in the region.

According to the 2013 World Bank 'Doing Business' report, central Asia recorded the biggest improvement in terms of time required to comply with profit, labour and consumption taxes of any region worldwide over the last eight years.

However, the Asia Business Outlook Survey conducted by the Economist Corporate Network in December 2012 underlines the disparity within tax policy across the region. The survey found that tax rates were a 'major issue' for just 10% of Asian multinationals with a regional headquarters in Singapore or Hong Kong, whereas one-third of those headquartered in Tokyo, 25% in Shanghai and 18% in Kuala Lumpur described tax rates as a negative factor.

These findings are largely reflected in the World Bank report, which ranks Hong Kong and Singapore as the fourth and fifth easiest places in the world to pay tax based on the number of payments, time and total tax rates. Japan, on the other hand, was the only Asian country to introduce new taxes in 2011/12 (although it also cut its corporate income tax rate).

Where is paying taxes easiest and where most difficult?

Easiest	Rank	Most difficult	Rank
United Arab Emirates	1	Cameroon	176
Qatar	2	Mauritania	177
Saudi Arabia	3	Senegal	178
Hong Kong SAR, China	4	The Gambia	179
Singapore	5	Bolivia	180
Ireland	6	Central African Republic	181
Bahrain	7	Republic of Congo	182
Canada	8	Guinea	183
Kiribati	9	Chad	184
Oman	10	Venezuela, RB	185

Source: Doing Business database

Differing tax rates are not the only challenge facing corporate treasurers in Asia. Efficient tax planning depends on clarity, but this is often undermined by the practice of granting tax concessions to multinational companies (MNCs) on an ad hoc basis without clear guidance that could be used by other companies to seek similar concessions.

The fact that some countries fail to distinguish between revenue and capital when it comes to taxation is a further obstacle to a consistent regional treasury approach.

The dominant regional economies have been among the most proactive when it comes to reviewing and refining tax policy. For example, China's State Administration of Taxation (SAT) recently clarified that as part of its value-added tax (VAT) pilot study, VAT should be excluded from taxable income such as dividends, bonuses and royalty fees derived by non-resident enterprises.

The announcement concerning the corporate income tax treatment for such enterprises specifically addresses income originating from China and earned by non-resident enterprises with no in-country presence, or enterprises with an establishment in the country but obtaining income that has no actual connection with that entity.

Australian developments

One of the key developments in Australia in recent years has been the introduction of Taxation of Financial Arrangements (TOFA) in 2009, which seeks to align tax and accounting outcomes for financial instruments. Paul Travers, President of the Finance and Treasury Association (Australia) and Executive Director of Oakvale Treasury, describes TOFA as a useful initiative since it mitigates the work to be done on valuations and settlements.

"Additionally, it has allowed hedge accounting principles to also be applied to tax by, for example, being able to apply effectiveness testing (for hedge accounting) to both areas. This helps align tax and accounting outcomes, although it is not a decrease to the burden as this type of testing was not previously required for tax."

He believes this topic will become more of a focus for Australian treasurers looking to establish effective cash facilities in Asia. "The Asia capital markets are being increasingly discussed as a potential source of capital, with some corporations tapping the bond markets and having Asian banks join their banking syndicates."

In early April, the Australian government published proposals that Assistant Treasurer David Bradbury said should help discourage aggressive tax minimisation practices by large corporate entities. The most significant proposed change (which would take effect from the 2013-14 tax year) is the publication of limited tax return information relating to businesses with a total income of AUD100m or more, including reported total income, taxable income and income tax payable. In recent months, the Australian government has also updated the transfer pricing rules contained in domestic law to bring them closer to the Organisation for Economic Co-operation and Development's (OECD) standards.

Asian complexity

Governments across Asia have been particularly active on transfer pricing in an attempt to make sure companies leave a 'fair share' of their profit behind, explains Alf Capito, Tax Policy Leader Asia Pacific, Ernst & Young (E&Y).

"The Philippines recently promulgated transfer pricing guidelines and even set a profit benchmark, and Indonesia has taken similar steps to make it harder for MNCs to charge management fees and royalties. The burden on reporting transfer pricing has become greater because more documentation is required and tax authorities also want to see the substance of what the company is doing. Corporate treasurers need to keep an eye on this issue because their tax base could be exposed to penalties and adjustments if they are not careful."

> "Treasurers across the region would benefit from co-ordinated lobbying of governments on tax policy issues."
>
> Delores Goh, Head of Tax in Asia Pacific, Jones Lang LaSalle

General anti-avoidance rules (GAAR) are also a hot topic, adds Capito. "China has had GAAR for a while but is now framing legislation for how such rules will be enforced. About two-thirds of countries in the region either have GAAR or are planning to introduce them."

David Smith, Senior Advisor, PricewaterhouseCoopers (PwC), refers to efforts to counter 'treaty shopping' leading to increasing challenges and disputes in relation to structures long used by Asian groups to hold investments in other countries. "At the same time, the OECD's work in areas such as the meaning of 'permanent establishment' and 'beneficial ownership' for tax treaty purposes is also calling into doubt the viability of such structures. When all of these matters are taken together, there is little doubt that the management of taxes in Asia has become more complex over the last 12 months."

Dezan Shira & Associates provides tax advice to foreign direct investors across Asia. Chris Devonshire-Ellis, Principal and Founding Partner of its Singapore office, says the unharmonised nature of the region means reform of tax regulations has been patchy and that the pace of change has slowed over the past five years due to uncertainties caused by the global financial crisis.

"Financial uncertainty is not a friend of liberal tax reform," he says, referring to Vietnam as one of the most assertive Asian nations in this respect over the last 12 months. "Vietnam has been taking the lead in aggressively targeting China in terms of reducing tax levels for attracting light manufacturing from south China in particular. Tax breaks and rates in Vietnam are two points lower than in China now as a result."

On the other hand, India has been particularly haphazard when considering corporate tax reforms, he suggests. "New tax laws and regulations generally don't increase the financial and compliance burden on companies – the overall desire has been to find ways to lessen the tax burden and stimulate foreign investment. But while the intent may be there, much has yet to be done to see that actually realised in policy, with India being a prime example."

However, changes are afoot in the world's second most populous nation. In late February, India's Finance Minister presented a budget that included several notable proposals, including introducing the country's GAAR from April 2015 and increasing tax rates applicable to business income of foreign companies above certain thresholds and to royalties and fees for technical services paid to non-residents.

These proposals are expected to be enacted by June 2013 and would see the effective tax rate on income of a foreign company from India (where total income exceeds INR100m) increase from 42.02% to 43.26%, while the tax rate on royalties and fees for technical services paid to non-residents would rise from 10% to 25%. A proposal that a tax residency certificate alone would not suffice for a non-resident entity to claim a tax treaty benefit was subsequently dropped.

Devonshire-Ellis describes the eventual enactment of India's tax reforms as a game changer that will affect all Asian foreign direct investment (FDI), impact on China and alter the global supply chain. "These changes will have the effect of significantly reducing both corporate and individual income tax levels and combined with its young and relatively inexpensive workforce, will shift export manufacturing from China to the sub-continent. India will finally lift off as an investment destination to rival what we have seen from China over the past 20 years."

Potential for greater harmonisation?

Delores Goh is Head of Tax in Asia Pacific for global real estate services firm Jones Lang LaSalle. She agrees with the view expressed in the latest World Bank 'Doing Business' report that the regulatory environment for corporate enterprises in many Asian economies has generally become more sympathetic over the last decade.

"We have seen tax authorities trying to make filing and compliance easier for businesses by introducing e-filing, simplifying tax forms and using self-service e-tax certificates. However, the transfer pricing regime in most countries has intensified and audit, filing and documentation requirements have increased tremendously, putting a greater burden on the cost of doing business."

Goh expects closer co-ordination and co-operation in the area of tax administration among Asian economies over the next few years. "We know of many tax authorities sharing information today and most tax treaties include clauses for the exchange of information across tax regimes." Goh believes treasurers across the region would benefit from co-ordinated lobbying of governments on tax policy issues.

But she also admits that it would be difficult to find a company or treasurer who would be prepared to lead such an initiative and that in any case, persuading governments to set aside rivalries would be massively difficult. "Given that Asian economies are so different, it would be very challenging – not impossible, but a very long shot."

Lattice and speciality emulsion polymer supplier Synthomer's Group Finance Director David Blackwood relates a similar experience. Most of the company's Asian business is done in Malaysia, where he says the company has found authorities across all aspects of regulation to be very business friendly and flexible and generally keen to support the business.

"The only substantial tax change in Malaysia recently has been around new transfer pricing regulations, which is right since most jurisdictions have transfer pricing rules. We are yet to see the application of these rules, but I would expect them to be applied in a balanced way based on previous experiences."

However, Blackwood shares Goh's doubts about whether tax laws and regulations across Asian countries could ever be harmonised, although he acknowledges that such a move would make life a lot easier.

Corporate compliance will remain an issue in Asia for some time as tax collection mechanisms lag behind policy, believes Devonshire-Ellis. "The simplification of tax regimes is more to stimulate growth than address collection issues. There will be closer co-ordination and co-operation in the area of tax administration among Asian economies over the next few years, but the objective will be to lessen overall tax burdens and specifically intra-Asian customs tariffs."

The rise of Association of South-East Asian Nations (ASEAN) will create a massive free trade area across Asia, and the co-ordination of bilateral and multilateral double taxation agreements (DTAs) will pave the way for sustainable regional growth for the next 20-30 years, he adds.

"ASEAN's agreements are already doing away with much of the customs duties, but I think the Asian harmonisation of corporate or individual income taxes will remain off the agenda for years. Asia is so diverse that I don't think, apart from easing trade, we will see any collusion on sovereign tax or other matters."

Tim Owen, an Independent Corporate Treasury Consultant and former Director of Treasury at Cadbury Schweppes, also doubts that Asian economies will produce any sort of harmonised approach to corporate tax.

"Certainly in India, whilst there have been moves to be more tax-friendly towards MNCs (for example the liberalisation of 100% foreign ownership around the turn of the millennium) there is still some way to go, as exemplified by the problems that MNCs such as Vodafone have had recently. This seems to me to involve the levying of income taxes on capital transactions, which is a very different approach from the rest of the world. The struggle of foreign retailers to get access to the Indian market is another example."

Singapore-based Managing Director of Acarate and former Vice President of Treasury at Chinese telecommunications equipment maker Huawei, David Blair, says India's recent claims that several MNCs (including Vodafone) failed to properly value transactions with their Indian subsidiaries is evidence of a more aggressive and sophisticated approach to corporate taxation.

He believes Asian treasurers are "very passive" on issues that affect their functions and would benefit from co-ordinated lobbying of regional governments.

Adapting to change

In order to take advantage of reforms in China and India, treasurers need to move quickly to evaluate treasury management changes and provide optimal structures and processes. That is the view of Gourang Shah, Head of Treasury Advisory, Asia Pacific Treasury and Trade Solutions at Citi, who recommends optimising funding options for investments in India and integrating renminbi (RMB) into group-wide cash and liquidity management structures.

The latest benchmarking survey from Citi Treasury Diagnostics found that a high percentage of Asian MNCs are failing to leverage technology, accounting for just 10% of all companies using SWIFT worldwide. The large number of Japanese corporates still using in-house spreadsheets or databases rather than treasury management systems (TMS) is a legacy of the fact that they didn't historically manage global treasury operations from the headquarters, explains Shah.

"As MNCs from other parts of Asia globalise and their business scale increases, they will need to be more efficient in terms of treasury management. That will require them to centralise and TMS will be needed to support centralised treasury management. Some have already started licensing and implementing solutions." ■

Favourable locations for RTCs: Singapore and Malaysia

Setting up a regional treasury centre in a location with a favourable tax and/or regulatory environment is an option for achieving a more tax efficient treasury solution. Several Asian countries, such as Malaysia and Singapore, offer specific incentives to locate such centres in their jurisdiction.

Malaysia provides a range of incentives to companies to establish their treasury functions within the country, including:

- Income tax exemption of 70% of statutory income from qualifying treasury services rendered to related companies for five years.
- Withholding tax exemption on interest payments on borrowings from overseas used for qualifying activities.
- Stamp duty exemption on loan and service agreements for qualifying activities.
- Expatriates working in the treasury management centre taxed only on the portion of their chargeable income attributable to the number of days they are in Malaysia.

MNCs who establish a finance and treasury centre in Singapore can avail themselves of tax rates of 5% or 10% for five or ten years (with possible extension) on qualifying income, which includes fee income received from related companies, offices and associates outside Singapore for the provision of qualifying services, as well as interest, dividends and gains earned from qualifying activities.

Providing they incur significant local business spending, employ a team of professional staff and provide qualifying services to approved network companies, these companies can also qualify for an exemption on withholding tax.

Deal or no deal: anatomy of an FX portal

Effective foreign exchange (FX) trades are a key part of many a treasurer's role. Getting the best out of a deal requires an understanding of the channels used and how they work. Treasury Today dives under the bonnet to explore the pros and cons of FX portals.

There is no doubt that the natural evolution of foreign exchange (FX) dealing has seen it move well beyond its early status as a by-product of international business and into a space where more opportunistic FX traders (such as hedge funds) work with it to make considerable profit. According to bank-owned settlement infrastructure provider, CLS, FX is now the largest financial market by value.

The evolution of FX as a vital part of global commerce has brought a number of complex derivatives – and matching technologies – that, whilst enabling traders to be more in control of the risk, have also attracted the attention of regulatory measures, such as the latest Dodd-Frank and Markets in Financial Instruments Direct (MiFID) requirements regarding transparency, record keeping and reporting.

Indeed, as regulation around financial services increases, electronic solutions appear even more attractive because they offer the kind of audit trails and reporting functionality that old-fashioned voice trading does not. Few corporates look at their treasury as a profit centre, and the precise determination of when and how they trade is often something they do collaboratively with their banks: price and convenience may be hugely important in some deals but the relationship side of FX for corporates is equally so, especially in tough economic times.

There are three 'buy-side' models. Voice trading (over the telephone) is often favoured for large or complex orders. The other two rely on web-based portals and are offered as single-bank (eg bi-lateral) or multi-bank trading variants. It is not a case of either/or, but rather of using the most appropriate tool for the circumstances.

e-Portals make their mark

As the name suggests, the multi-bank portal allows users to obtain a range of prices, products and services from a range of banks whereas the single-bank option delivers the same from just one bank.

The single-bank option was first to appear. In the early days, a request for quote (RFQ) model was used. The treasurer would log in to the bank's website, state how much was needed of a required currency, and receive within 30 seconds or so an automated quote. Once that offer was accepted all the downstream processes, such as clearing and settlement, had to be executed offline. Continual investment by banks in their technology has today created greater levels of automation and facilitated ever-lower latency of price streaming, more akin to professional traders' requirements, to the point where users can instantly see the depth of liquidity in the market.

> Few corporates look at their treasury as a profit centre, and the precise determination of when and how they trade is often something they do collaboratively with their banks.

The sophistication and capability of a system's functionality today tends to be driven from the top downwards by the needs of the financial institution (FI) and pro-trader market, but the way in which users wish to work and interface with these systems tends to be driven from the bottom upwards by the needs of the retail market. In other words, users want a simple, intuitive interface but with all the clever behind-the-scenes trickery garnered from the top end of the market.

With the high levels of FX trade flow a system is required to handle, many pre and post-trade services have also been integrated with platforms to try to create as much of a straight through processing (STP) environment as possible. For corporates, trades are usually integrated up front into an order management or trade planning system and then uploaded into the FX platform before execution, with automated booking of these trades back into the treasury management system (TMS) or spreadsheet.

For a treasurer, the choice between single or multi-bank platform seems obvious at face value. Why wouldn't they sign up for a multi-bank FX portal and get the lowest price at the click of button? Certainly the multi-bank portal's arrival was seen by some observers as the death knell for single-bank platforms. But it has not been the case. Why?

It may be that the treasurer does not execute a sufficient number of trades to warrant subscribing to a multi-bank portal. But there may be another factor at play too. Just as retail supermarkets don't always come out on top for customers when factors such as service, product knowledge, advice and even customer loyalty are factored in with price, so multi-bank portals may not always deliver best execution for a corporate treasurer. Another factor often considered when trading is the need to spread the share of the corporate wallet. Quid pro quo, a treasury may wish to ensure that its banks are getting a fair share of its business – even if that means a particular FX trade is executed on a non-competitive basis. The reason is simple: they may not want a certain bank – especially one with which they have a valuable line of credit – to pull the plug on the relationship because it was deemed unprofitable.

If one thing is certain, it is that the treasurer is yet to be presented with a one-size-fits-all FX solution and that until such a tool is made available, it is essential to understand the pros and cons of each in order to make the most appropriate choice in each situation.

All change as multi-bank portals arrive

In the late 1990s, encouraged by the rapid uptake of the internet for business purposes (driven in part by rising consumer confidence in web-based transactional tools), players in the banking and technology communities saw a niche in the FX market. Corporate treasurers were typically engaging in multiple bilateral relationships with liquidity providers. The new connectivity technologies would enable treasurers to request and receive FX prices from multiple banks, and place orders, all in ultra-fast time, through one central platform. A number of multi-bank platforms hit the market around mid-2001.

For the corporate, these portals promised more than just a convenient price discovery tool. They could also deliver workflow, enabling treasurers to see all their accounts, trades and the scope of their portfolios in one place. With further integration into SWIFT (via the automated MT101 request for transfer message) and the Continuous Linked Settlement (CLS) system, such a combination would eventually deliver post-trade services, right through to clearing and settlement. Connectivity between the front end of a TMS and corporate back office functions became a reality in October 2012 for 360T's multi-bank FX trading platform, when it announced that Kyriba was to integrate it into its own software-as-a-service (SaaS) delivered TMS.

But the early rush to join the multi-bank platform race ended almost as soon as it began for some, with SunGard's system, part of its STN Treasury unit, and Citigroup, Deutsche Bank and J.P. Morgan Chase's Atriax failing to make the grade within a year or two of hitting the market. The (short) list of those that survived includes FXAlliance (aka FXall, a business originally owned by a consortium of 16 banks, but since July 2012 a part of Thomson Reuters), the aforementioned independent German-based global provider, 360T and the State Street-owned Currenex.

However, the breadth of products, currencies and liquidity providers available on each of these – and later arrivals such as Bloomberg's FXGO – has flourished. Platforms now typically cover electronic trading across the range of instruments including spot, forward outrights, swaps, non-direct forwards (NDFs), options and deposits. All seek to add value in as much as users can access functions such as market surveillance, statistical and comparative analysis and portfolio and risk management. The number of banks available to trade with will vary by platform, but most major institutions will make themselves available in this way to their corporate clients.

At the technological heart of all multi-bank FX portals is the electronic communication network (ECN). For web-based FX trading, this has been around since 1999, being first offered by New York-based Matchbook FX. Multi-bank platform providers today, such as Currenex, Bloomberg, 360T, FXall and Knight Capital's Hotspot FX, use it to stream quotes from the world's major banks. Because ECN is a live exchange-type order book driven by spreads on all quotes, buy-side users (often FIs, but sometimes the pro-traders of MNCs) can actually move prices. Using an ECN-enabled platform means traders generally enjoy improved price transparency and faster processing than single-bank portals, whilst the highly automated process enables banks to lower their costs and widen margins.

Multi-bank versus single-bank

Why multi-bank? The multi-bank vendor argument against voice-trading is that treasurers seeking price differential this way will call their usual panel of banks for quotes, but by the time they have done the rounds the market may have moved away from them. The multi-bank portal automates the RFQ process, making it faster and more efficient. But large and complex deals may still require human interaction, this being borne out by the observation that very large trades remain resolutely voice-based.

The riposte to the single-bank model from a multi-bank perspective is that a major corporate is likely over time to accumulate a multitude of portals to manage. Arguably too, pricing is less favourable when there is no competition. But FX tends only to be part of a relationship and a wise bank will deliver greater benefits to the corporate that gives it a greater share of its wallet.

In terms of FX this may include extras such as client-specific pre and post-trade functionality. When a corporate transacts through its bank's own platform, it may also have access to the bank's proprietary trading algorithms and be able to automate its own trading preferences for best execution. This is a valuable selling point that has not gone unnoticed by multi-bank provider, FXall. Since mid-2012 it has been able to deliver some of these algorithms through its own platform, starting with Credit Suisse, Deutsche Bank, Goldman Sachs and J.P. Morgan. This suggests that more of a partnership exists between the three parties than had previously existed, perhaps because banks have realised that they can reach a wider corporate base if they make themselves more readily available to their clients, and platform providers know they do not have the benefits of extended corporate relationships.

In practice, a multi-bank portal will offer a range of execution methods. The traditional RFQ model, as discussed above, remains the dominant model. Other trading models, such as portfolio-trading (which facilitates trades across multiple allocations, currencies and forward dates) and active or direct access trading (which provides price streaming) require a higher degree of trader-sophistication, often reserved for in-house corporate traders, FIs or professional traders.

Most banks that have developed a one-to-one FX portal will retain it because there will always be clients that at one time or another have reason not to use a multi-bank option. There may be clients for whom the cost savings are irrelevant or are outweighed by other considerations. Indeed, if a corporate has a regular line of trade with a bank it may be that the bank's FX portal effectively becomes a gateway to other benefits. Anecdotal evidence even suggests that some banks have been actively upping liquidity for favoured clients using their proprietary channel. Banks that have been investing in the well-being of their proprietary FX portal are effectively doing so as a means of investing in their client relationships, providing access to the whole pre-trade, trade, and post-trade value-chain (which may include underlying services such as trade finance or letters of credit (LCs) as opposed to just thinking about the narrow trading processes.

> The multi-bank portal automates the RFQ process, making it faster and more efficient. But large and complex deals may still require human interaction, this being borne out by the observation that very large trades remain resolutely voice-based.

For all these reasons, the advent of the multi-bank portal has not overseen the demise of the single-bank option (nor voice trading). The advantages of multi-bank portals are obvious and many corporates have adopted them with relish (one enthusiastic group treasurer told Treasury Today that on savings alone his system paid for itself in just six weeks). But banks are in a unique position of being able to steer clients towards the most appropriate solution at that time, whether that means voice trading, their proprietary FX portal or a multi-bank platform.

There are clearly roles for all and the likelihood is that most corporates will continue to pick and choose the platform and the trades that suit them best, which means providers need to keep all channels open and work with the flow, not against it. ■

Don't forget to ask…

When choosing a platform provider, treasurers will need to match the kind of instruments they wish to trade to those that the platform is able to deliver. But if the need is to trade in any significant volume, there is also a need to understand exactly the level of automation being offered, particularly around trade uploading (some systems may require manual shifting of files).

Most systems now offer a high degree of STP and treasurers will gain efficiencies trading electronically, but the degree to which execution and reporting of both competitive and non-competitive trading is enabled is important for treasurers even if 'non-competitive' trading is an alien concept for FI users.

Net benefits

Netting is often cited as a cash management technique that can allow treasurers to create efficiencies and make cost savings. But the term 'netting' can be applied to a variety of different tactics.

The process of netting can be used in various areas of cash management. In its most basic term it is usually a way of offsetting cash amounts in a way that results in benefits for the corporate, such as reduced transaction costs. However, the scale of the benefit can differ significantly depending upon the type of netting that the corporate is involved with. Many forms of netting cover areas of the banking relationships that the corporate holds, while perhaps the most beneficial form of netting focuses on inter-company transactions.

Payables and receivables

Netting accounts payable (AP) and receivable (AR) could be considered the most basic form of netting. A corporate has obligations to a bank, where it may have a derivative instrument, loan or deposit, and is expecting an immediate payment back from an investment with that bank. At the same time, the corporate may have a foreign exchange (FX) contract with the same bank through purchasing some foreign currency, and needs to pay the bank for that foreign currency. Here the corporate can potentially net these two sums off. This means that rather than waiting to receive its investment back and then paying the FX cost back to the bank, an agreement with the bank can allow the corporate to merely settle the net amount.

This is usually done by arrangement with the bank, to make sure that it is expecting either a net settlement or payment, based on the size of the flows either way. Typically there will be a master agreement in place between the two parties that establishes the right to net.

While this process is technically quite simple, there are many challenges. If the corporate has a $2 billion loan coming back, for example, and also has a sizeable settlement to pay to the bank (such as a large FX deal), the bank may be somewhat wary to net those two off. It is important to ensure that the settlement is done in a timely fashion so that neither party is exposed to daylight exposure, which is an intraday exposure when an account is in an overdraft position at any time during the business day.

Balance netting

Balance netting with relationship banks is sometimes referred to as pooling. For example, the corporate may have a balance in euros in France, an overdraft in Italy and a credit balance in the UK. By arrangement with the relationship bank, it is possible to pool the balance of all of these accounts and then net them off. The corporate ends up with a netted cash position, or a netted pool of accounts, in a particular geographic area. Through the arrangement, the corporate would pay or accrue interest on these accounts, on a netted basis, based on the balance.

Most companies in Europe engage in some element of balance netting. One popular practice is to pool euro accounts, where permissible. These can be offset to ensure that the corporate does not have to physically sweep cash into certain concentration accounts. Using the earlier scenario of accounts in France, Italy and the UK, rather than actually physically shifting all cash to one central account to be balanced out, banks can offer corporates the right to net out and have a pool structure. This can save a lot of money on payments that shift cash around different geographies.

FX netting

Corporates often have the right to offset FX settlement amounts. In one simple example, if the corporate has bought Canadian dollars from Bank A and has sold Canadian dollars to Bank B, these can often be netted off. The corporate may have an agreement where it can net off cross-bank settlement flows, leaving the treasurer to pay only the net to the bank they owe. If Bank B is paying the corporate €100m for Canadian dollars and at the same time the corporate owes €120m to Bank A, then Bank A would receive €100m from Bank B, leaving the corporate to pay €20m to Bank A.

This tactic avoids multiple flows of large currency amounts. The corporate can net them all off and allow the banks to settle between themselves based on the obligations they have to those banks.

FX netting is becoming more common, particularly around continuous linked settlement (CLS). The whole point of CLS is to avoid daylight exposure, by netting exposures out.

Multilateral netting

Multilateral netting is perhaps the most interesting form of netting available to corporates. It is a form of netting that is usually done on an inter-company basis where subsidiaries have inter-company payables and receivables. For example, Subsidiary A may buy some elements of the production from Subsidiary B. Subsidiary B may itself be buying some elements that it needs from Subsidiary C, and so on. These inter-company payables and receivables are typically settled on a monthly basis.

Multilateral netting allows the treasurer to set up a process where all subsidiaries go into a central repository and log all of their payables and/or receivables. Every subsidiary that is expecting to receive something from another subsidiary goes into the netting session and puts in the amount they are expecting to receive, the currency and which subsidiary it is from. The same is true for subsidiaries that go in to the netting session to declare what they are expecting to pay.

If an organisation has many inter-company settlements, a netting solution will allow it to enter all of these into a central location and then net them out. In a simple example, Subsidiary A needs to buy $10m to pay to Subsidiary B. Subsidiary B needs to buy Canadian dollars and use its US dollars to pay Subsidiary C. In a netting centre, the company can net the two off and the US dollar amount can disappear. It may be left with a euro/Canadian dollar exposure, for example. The end result is that the corporate does not have hundreds of payments in foreign currencies happening between subsidiaries. Instead, there is a limited number of transactions that central treasury has to undertake in foreign currency.

> Multilateral netting allows the treasurer to set up a process where all subsidiaries go into a central repository and log all of their payables and/or receivables.

In this case, if Subsidiary A were to pay Subsidiary B without a netting solution, it would have to go to the bank to request the $10m, while its base currency may be euros. In effect, they are doing an FX transaction. Unlike central treasury, subsidiaries are rarely experts in FX and will typically get both a poor rate from the bank and a poor spread on that rate. If a corporate buys and sells foreign currency it will pay a buy/sell spread. For example, if Company A is buying sterling from the US, they may find it at around 1.50. If conversely Company A is selling, it may be around 1.52 for a small FX deal. That spread of $0.02 for every transaction carried out can soon mount up across an organisation.

If the corporate has 600 invoices going between subsidiaries and they are all settled by an FX deal that the subsidiary did with the bank, there will be a lot of spread on currency rates and poor rates on the FX deal as the subsidiaries do not have the same banking relationship as central treasury does.

Netting allows the treasurer to go to the subsidiaries and net down this process, resulting in a consolidated netted position. The central treasury then goes to the bank and carries out the translation of that position into the different currencies. The end result means that, in the case of Subsidiary A based in Europe, it will be told what it needs to pay or should receive in euros. Each subsidiary only has one account, which is in their most suitable currency. A Canadian subsidiary may have payables and receivables in euros, Mexican pesos, Norwegian kroner, for example, but this does not matter. It will only receive one single amount in Canadian dollars. Multilateral netting simplifies the entire process down for every subsidiary, in that each will only pay or receive one amount in their base currency. All of the company invoices will be settled on a netted basis by the central treasury group.

Challenges

One of the main challenges in implementing a multilateral netting programme is that it is an education process for the subsidiaries which group treasury has to lead. People do not like being overburdened with having to present too much information if they do not understand the reason for this. Multilateral netting is one area in treasury where there is a very tangible return on investment (ROI) for implementation. It is simple to calculate the value saved based on the netting down of all of the spreads.

In terms of setting up a netting process, a corporate will typically start by going to its treasury management system (TMS) or enterprise resource planning (ERP) system. If it is a payables netting session, it will export all of the payables that it is expecting for the month. These are then uploaded to a netting solution at a certain date every month. There are typically four dates in a netting session:

1. Presentment date – when the payment invoices are input into the netting solution.
2. Cut-off date – at this point the reconciliation is done. Before this time, each subsidiary will double check that its appropriate payables and receivables correspond with what its partner subsidiaries have claimed. This dispute process happens between the presentment date and the cut-off date.
3. FX settlement date – when the central treasury settles the FX on behalf of all of the subsidiaries.
4. Settlement date – when the subsidiaries either receive or pay their money.

The first two dates here are the most important in the process. When implementing a multilateral netting process, the treasurer needs to educate the subsidiaries on how to get the inter-company payables and receivables reconciled into the netting centre. By pulling some reports the treasurer can demonstrate exactly what they are expecting to receive from the subsidiary and how the dispute process should function.

Being able to pull out accurate information by a certain date is the main challenge of setting up a multilateral netting process. Without a netting centre, a corporate will typically have standard terms of trade. The company's payable terms may be six to eight weeks in terms of invoices, but internally the treasurer may decide to go to a four-week settlement, always on a particular date. This gives the treasurer control over the internal settlement process. Rather than being on floating terms, everything goes into the netting session on a monthly basis. A netting centre brings more discipline to this process, and allows the treasury to get a better FX rate, less spread and better risk management around currency exposure.

Benefits

The benefits of multilateral netting mean it deserves consideration by all corporates. If an organisation does a lot of inter-company business, there is no reason why it should not be doing multilateral netting today. The process itself is all about cash flows. Each subsidiary in the netting centre knows when it is going to get paid for any inter-company invoices it has issued. Subsidiaries may have to pay their invoices earlier, but they know exactly which day they will receive cash on the invoices that they are expecting. This brings stability to the timing of cash flows within the organisation.

The netting off of transaction costs means that instead of having around 800 inter-company transactions between subsidiaries, treasury can reduce this considerably. Now each subsidiary just has one payment or receipt. If it costs $10 to make a payment, and the number of payments can be reduced from 800 down to 60, this is obviously a considerable saving for the organisation.

Another benefit of multilateral netting comes from the concentration of payments and receipts. The central treasury can control this process, meaning it can choose to have one bank to do its FX with. Treasurers can reduce the number of banks that they are exposed to from a settlement perspective. Savings are also available on the FX spread. The greater the number and size of transactions the corporate puts through, the greater the potential for cost savings.

Things are also very much simplified from the subsidiary perspective. They no longer have to decide which currencies they need to buy, instead paying and receiving in a single currency. This offers a potential head count cost reduction for the company, as there is no longer a requirement for staff to understand all payments in different currencies. The added discipline of running a netting centre means that internal payments are all received on time. It also gives the treasurer a good forecast capability over internal receivables, allowing them to know what is coming in and when.

> If an organisation does a lot of inter-company business, there is no reason why it should not be doing multilateral netting today. The process itself is all about cash flows. Each subsidiary in the netting centre knows when it is going to get paid for any inter-company invoices it has issued. Subsidiaries may have to pay their invoices earlier, but they know exactly which day they will receive cash.

An ancillary benefit of multilateral netting is found in hedging. When the treasurer is looking for dates to hedge their FX exposures to, if they have a multilateral netting solution they will know that it is typically the 20th of every month that their netting happens, for example. Therefore they know the specific date that they are exposed to. This allows treasury to hedge very efficiently and effectively as it reduces timing gaps in their hedging programme.

There are also benefits in terms of trade. As already mentioned, multilateral netting provides a forecastable and accurate set of cash flows in and out of the business. This means that terms of trade could be considerably shorter, as they are not spread out over a time period. All parties involved in a trade know that an invoice received by a certain date will be settled by the relevant date.

The benefits to the dispute process are similar to this, as the multilateral netting process sets up a system that records disputes within the organisation efficiently and effectively. The netting centre becomes the repository for dispute management. The treasurer can then use that to make sure that AP and AR balance. ■

treasurytoday

Corporate Treasury Benchmarking

Compare your business against others and be part of the programme to create industry-wide best practice. Treasury Today first introduced Corporate Treasury Benchmarking in 2009 and your response has been amazing – almost 3,000 respondents across five regions since our first Study.

Why participate?

The Studies focus on a wide range of issues from bank relations, counterparty risk, credit and cash, liquidity and working capital management to supply chain and technology. We now include a specific section on the key performance indicators (KPIs) being deployed and, where stated, the actual metrics companies are achieving. This data is providing yet further insight into the corporate treasury arena with many corporates adopting such measures.

Wolfgang Ratheiser, Global Engineering Finance Director at Johnson Controls, articulates the case perfectly. "For benchmarking, it is important that you anticipate where you will stand and what trends are in the market," he says. "You need to continually ask yourself, are we leading this trend? Are we falling behind? And what kind of corrective actions are we taking in order to stay ahead?"

"We now tend to review our days inventory outstanding (DIO), days payable outstanding (DPO) and days sales outstanding (DSO) on a monthly basis," says Priyanke Perera, Head of Group Treasury at Brandix in Sri Lanka. "But that is not all. We go beyond that, particularly when it comes to tracking how early or how late our suppliers provide inputs to manufacture a garment (on-time tracking) based on the dynamic production plan we have to support our buyers. This is a great indicator for the company's working capital management."

"Given the importance of cash pooling to the business, minimum cash holding serves as a key performance indicator," says Tan Lee Thong, General Manager, Group Finance at International SOS in Singapore.

What's being measured and what's new?

This year we have introduced a number of new measures, including an entirely new section enabling you to rank the banks.

When it comes to best practice, our benchmarking studies offer a unique opportunity to set your treasury's standards against the best in the field. We ask about the KPIs you are using to measure performance. This year, we look to explore the actual measures/ratios against such KPIs.

If you participate in the Studies, you will receive a confidential report which summarises the headline findings. In addition, if you complete the section on KPIs, we will benchmark your KPIs against the study universe.

The findings and individual benchmarking results are exclusively available to participating corporates.

"The treasury employs a variety of KPIs to ensure benchmarking efficiency. These include transaction costs, refinancing risk, covenant ratios and FX hedging amongst others," says Daniele Vecchi, Group Treasurer at Majid Al Futtaim in Dubai.

"The main focus of our benchmarking processes are related to maintaining relationships with our banks. In essence this means: how we choose the banks; how we manage our FX exposures; and how we manage our finance costs," says Kamal Goyal, CFO at Alumco in the United Arab Emirates (UAE).

Some of the reasons companies have given in the past for participating in benchmarking:

"Identifying problem areas in our organisation."

"Identifying other industries that have similar processes and what they are doing."

"Identify organisations that are leaders in areas that concern us."

"Helps to build processes and metrics for us to use."

"Helps to determine which areas to focus, once data is collected leading to productivity gains."

"Used to target future performance/organisation performance."

"Helping us identify where we can reduce cost."

"Encouraging us to implement new and improved business practices."

We hope you will take the time to become involved in the benchmarking programme by participating in the regional Study most relevant to you. ■

Manish Kapoor

Head of Airtel Centre of Excellence (ACE)
Cash and Banking Operations

Treasury Today spoke to Airtel's Manish Kapoor recently about benchmarking.

Why is benchmarking important to you, your treasury department and your company overall?

Benchmarking is a process which helps us to compare our business processes and performance metrics to best practices from other industries. The measurement dimensions of industry benchmarking are time, cost and quality.

The process of best practice benchmarking helps us to identify the best firms in our industry, or in another industry where similar processes exist, and then compare the result and processes of those to one's own results and processes. This helps us to learn how well the targets perform and, more importantly, the business processes, which also help us to be more successful within the industry.

How do you use the benchmarking results?

Benchmarking helps us to measure the performance using a specific indicator such as productivity, cost and cycle time, which also help in determining or identifying the defects resulting in a metric of performance. This is then compared to others within the industry to match the industry standards.

The benchmarking process is used in the company by management or operations to evaluate various aspects of their processes in relation to best practice companies' processes, which is usually within a peer group defined for the purposes of comparison. This then allows or assists the organisation to develop plans on how to make improvements or adapt specific best practices to increase performance.

Please give us an example?

Bharti Airtel decided to define a benchmark, by overhauling and revamping its entire payment model – no mean feat for a company that is one of the biggest in its industry. With the establishment of ACE Cash and Banking Operations (a shared services centre (SSC)), we were able to achieve:

- More than 97% accuracy in fund forecasting.
- Releasing the working capital of $30m.
- Increasing payments on time by 82%.
- Reduction in customer query by 83%.

All these metrics are to the highest standards in the industry.

Are there any other ways benchmarking can contribute to an organisation?

There is no single benchmarking process that has been universally adopted which could help us to know how it can contribute to an organisation. Nevertheless, the wide appeal and acceptance of benchmarking has led to continuous evaluation and improvement for our organisation.

Benchmarking helps and encourages an organisation to be open to new methods, processes, ideas and practices to improve effectiveness, efficiency and performance. The benchmarking study results offer valuable data that can motivate thought-provoking discussions with key stakeholders (internal or external). The results provide answers to the following key questions:

- What are the opportunities we should work or focus on?
- How well are we performing in comparison to other companies or organisations?
- What are the best practices followed by other companies?

Lastly, we asked Kapoor to list the reasons why corporates should participate in the benchmarking studies.

The process of benchmarking facilitates companies to identify themselves as a best firm in their industry, or in any other industry where similar processes exist, and then compare the result.

Secondly, it helps to learn how well the targets are performed and, more importantly, the business processes which help them to be more successful within the industry.

It also helps to measure the day-to-day performance using a specific indicator such as productivity gains, cost reduction, cycle time and standardisation across processes. All of these areas help in determining or identifying the gaps/defects impacting organisational goals.

Our Middle East Study is live and Asia Pacific and Europe will follow shortly.
To participate please go to **http://treasurytoday.com/benchmarking/participate**

INSIGHT AND ANALYSIS

Protecting your supply chain

According to a recent Demica report, major global banks are reporting on average an annual supply chain finance (SCF) growth rate of between 30% and 40%. The US and Western Europe, in particular the UK and Germany, have experienced the highest growth of SCF, whereas Eastern Europe, India and China are the top three regions with future SCF market potential.

RISK MANAGEMENT

Cyber risk

Businesses are increasingly concerned about the potential impact of cyber risk on their revenues and reputations, in the wake of high profile security breaches, hacking scandals and greater data protection regulation. Although it's easy enough to grasp what the threat looks like, finding practical solutions is far harder. What can be done to protect treasury from this pervasive threat?

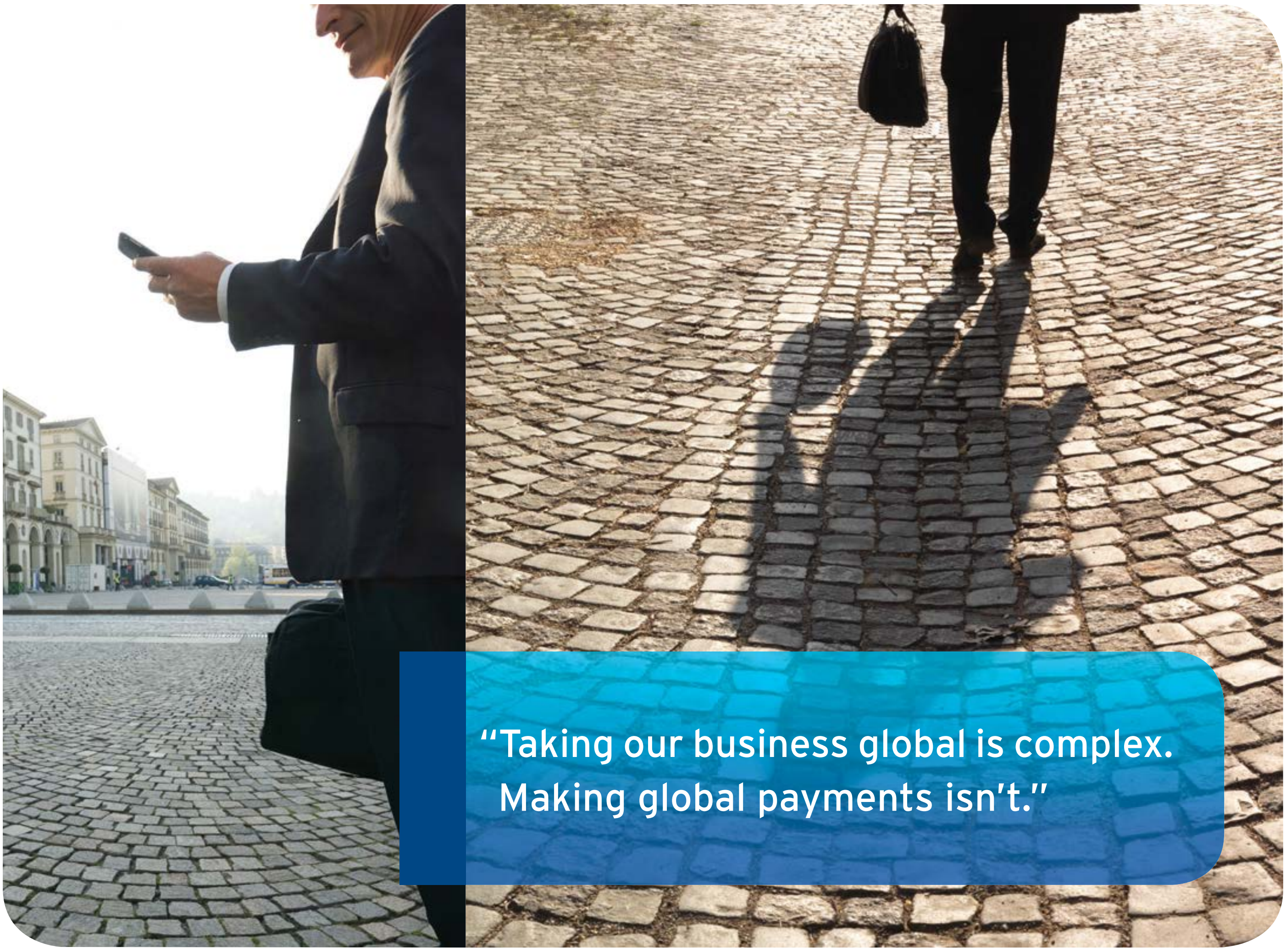
CORPORATE FINANCE

Tapping the private market

Private placement (or non-public offerings) is a long-term financing option for issuers who do not have access to, or choose not to, access the public debt markets. The market has become both deeper and larger in recent years as companies look for alternative sources to bank finance, and investors put more money to work in this space.

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

Niklas Bartelt, Managing Director, DZ Bank; **Paul Bramwell**, Senior Vice President, Treasury Solutions, SunGard; **Marcelino Castrillo**, Head of SME for Santander Corporate and Commercial; **Chris Dunne**, Payment Services Director, VocaLink; **Karin Flinspach**, EMEA Head of Payments and Receivables, Treasury and Trade Solutions, Citi; **Rodney Gardner**, Head of Global Receivables, Global Transaction Services, Bank of America Merrill Lynch; **Melvin Glapion**, UK Managing Director, Kroll Advisory Solutions; **Kamal Goyal**, CFO, Alumco; **Yera Hagopian**, Global Head of Liquidity Product, Barclays; **Lenore Kantor**, Senior Director, Head of Marketing and Communications, FXall; **Manish Kapoor**, Head of Airtel Centre of Excellence (ACE) Cash and Banking Operations, Bharti Airtel Limited; **Matt Lawrence**, Financial Market Sales, Corporates, Lloyds; **Andrea Loddo**, Financial Risk Advisory Team, Lloyds TSB; **Gareth Lodge**, Senior Analyst, Celent; **Justin Meadows**, Managing Director, MyTreasury; **Aled Patchett**, Financial Risk Advisory Team, Lloyds TSB; **Priyanke Perera**, Head of Group Treasury, Brandix; **Wolfgang Ratheiser**, Global Engineering Finance Director, Johnson Controls; **Peter Schädelbauer**, Head of Group Treasury, Lindner Group and Managing Director, Lindner Finanz; **Bob Stark**, Vice President of Strategy, Kyriba; **Tan Lee Thong**, General Manager, Group Finance, International SOS; **Marcus Treacher**, Global Head of eCommerce for Payments and Cash Management, HSBC; **Bill Trueman**, Managing Director, UK Fraud; **Daniele Vecchi**, Group Treasurer, Majid Al Futtai; **Jayakumar Venkataraman**, Partner, Financial Service Consulting Practice, Infosys; **David Whelan**, Director, Capita International Financial Services; **Joerg Wiemer**, CEO and Co-Founder, TIS; **Steve Wright**, Product Development Manager, VocaLink.



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