treasurytoday
research | insight | analysis
October 2014

Clarifying credit ratings

As the ratings agencies move beyond their crisis-induced reality check, we take a look at how their methodologies are changing and identify some of the key factors that corporate treasurers now need to be aware of when going through the ratings process.

The Corporate View

Ingmar Bergmann
Corporate Treasurer and Head of Corporate Finance
NSI N.V.

The Industry View

Bea Rodriguez
Head of International Cash Portfolio Management, Managing Director
BlackRock

Risk Management

Investing in emerging markets

Treasury Practice

Virtual accounts

Country Focus

Treasury in Nigeria

Back to Basics

Treasury outsourcing

Money can buy the land.

But ambition makes it a destination.

Corporate Banking

When you are ambitious, no goal is too big and no achievement is out of reach. At ADCB, we provide the people and businesses of the UAE with the award-winning banking products and services they need to put their ambitions into action. Learn more at **adcb.com**

treasurytoday

treasurytoday.com
Volume 16 / Issue 09
October 2014

Publisher
Angela Berry

Executive Assistant to the Publisher
Samantha Collings

Associate Publisher
Sophie Jackson

Editorial Director
Eleanor Hill

Deputy Editor
Chris Josselyn

Editorial
Tom Alford
Chris Davis

Research and Editorial
James Hayward

Research Director
John Nicholas

Relationship Manager
Megan Coates

Head of Events
Lisa Bigley

Head of Circulation
Sarah Arter

Circulation Assistant
Josh Thompson

Head of Production
Dawn Ingram

Production Assistant
Robert Murray

Website Manager
Luke Scammell

Website Assistant
Joanna Smith-Burchnell

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
Fax	+44 (0)13 0462 9010

Annual Subscription Rate £285
subscriberservices@treasurytoday.com

© Treasury Today ISSN 1466-4224

Treasury Today is published monthly
(10 issues) by Treasury Today Limited
Courtyard Offices • Harnet Street
Sandwich • CT13 9ES • UK

The entire content of this publication is protected by copyright. All rights reserved. No part of this publication may be reproduced, stored in a retrieval system or transmitted in any form or by any means mechanical, electronic, photocopying, recording or otherwise, without the prior written consent of the copyright holders. Every effort has been made to ensure the accuracy of the information contained in this publication, Treasury Today Limited cannot accept liability for inaccuracies that may occur. Where opinion is expressed it is that of the authors and does not necessarily coincide with the editorial views of the publisher or Treasury Today. All information in this magazine is verified to the best of the author's and the publisher's ability. However, Treasury Today does not accept responsibility for any loss arising from reliance on it. No statement is to be considered as a recommendation or solicitation to buy or sell securities or other instruments, or to provide investment, tax or legal advice. Readers should be aware that this publication is not intended to replace the need to obtain professional advice in relation to any topic discussed. Printed by: Buckland Media Group Ltd.

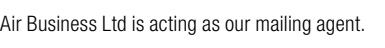
Treasury Today USPS: (USPS 023-387) is published monthly except August and December by Treasury Today Limited, Courtyard Offices, Harnet Street, Sandwich, CT13 9ES.

The 2013 US annual subscription price is $588.00. Airfreight and mailing in the USA by agent named Air Business Ltd, c/o Worldnet Shipping Inc., 156-15, 146th Avenue, 2nd Floor, Jamaica, NY 11434, USA.

Periodicals postage paid at Jamaica NY 11431.

US Postmaster: Send address changes to Treasury Today, Air Business Ltd, c/o Worldnet Shipping Inc., 156-15, 146th Avenue, 2nd Floor, Jamaica, NY 11434, USA.

Subscription records are maintained at Treasury Today Limited, Courtyard Offices, Harnet Street, Sandwich, CT13 9ES.


Air Business Ltd is acting as our mailing agent.

Cybercrime means business

Despite growing investment in measures to counter cyber-attack, an increasing number of banks and corporations are being caught short by fraudsters online. Given the pervasive reach of the internet, no country is immune from the threat of cybercrime. Nigeria, our Country Focus in this edition of Treasury Today (see page 32), is no exception. A cyber heist on the nation's banks in September saw criminals get away with more than $35m. Since 2013, Nigeria is now thought to have lost almost $120m to internet-based fraud.

Even the European Central Bank (ECB) has been hit by cybercriminals. In July, hackers stole email addresses and contact details from the bank before sending an anonymous – and audacious – email attempting to extort money from the ECB in return for the stolen information!

But it's not only banks that are at risk: in September, it emerged that North American home improvement retailer Home Depot had been the victim of a credit card breach. Reports suggest that the breach could be considerably larger than the theft of the card data of 40 million Target customers in late 2013. Home Depot said in a statement that shoppers who have visited its stores from April onwards could be impacted by the breach.

What this incident highlights is the fact that cybercrime is not just about money. It's about data – and also about reputations. Goodwill and loyalty can be destroyed in an instant by data breaches that undermine customers' trust.

The fight against cybercrime

On the plus side, banks and companies are fighting back with new technologies that should make it harder for the cybercriminals to strike. From next year, for example, UK corporate clients of Barclays Bank will be able to sign in and access online services and portals using a new form of authentication technology – one that uses unique finger vein patterns. Developed in partnership with Hitachi, the new technology will be a first for the UK banking industry.

Law enforcers are also getting tough on cybercrime. The European Police Office, Europol, has launched a cybercrime task force to address the problem in the EU and beyond. The law enforcement agency said the scheme, initially a pilot, would target threats including banking Trojans, Botnets and online fraud.

While cybersecurity and the sophistication of detection and counter measures advance, so do the cybercriminals – the challenge for banks and corporates is to stay one step ahead.

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

Segun Adaramola, Head of Treasury and Trade Solutions, Citibank Nigeria; **David Adepoju**, Head of Global Markets, Standard Chartered; **Benoit Anne**, Head of EM strategy at Societe Generale; **Timothy Ash**, Head of EM Strategy, Ex Africa at Standard Bank; **Ingmar Bergmann**, Corporate Treasurer and Head of Corporate Finance, NSI N.V.; **Jennifer Boussuge**, Head of Global Transaction Services, EMEA, Bank of America Merrill Lynch; **Jackie Bowie**, CEO, J.C. Rathbone Associates; **William Coley**, EMEA Corporate Finance Group Credit Officer, Moody's; **Claudia Colic**, Head of Transaction Banking, UBS AG; **John Coon**, Global Treasury Manager, Dow Corning Corporation; **Sonia De Paolis**, Treasury Director, TomTom; **Gautam Dhillon**, CEO, The Treasury Outsourcing Company; **Mike Dunning**, European Head of Corporates, Fitch Ratings; **Claudia Ehler**, Treasury Manager EMEA, SPX Corporation; **Simon Enticknap**, Director, Trade and Working Capital, Barclays; **Thierry Hamon**, Treasury Controller, Valeo; **Brian Hanrahan**, EVP Sales and Marketing, Sentenial; **Richard Hite**, Vice President, Supplier Finance, Barclays; **Marcus Hughes**, Director Business Development, Bottomline Technology; **Suzanne Janse van Rensburg**, Regional Head of Liquidity and Investments, GTS EMEA, Bank of America Merrill Lynch; **Niall Kelly**, Head of Group Treasury, DCC Plc; **Peter Kernan**, Managing Director, Criteria Officer, Corporate Ratings EMEA, S&P; **Laura Lanzeni Maria**, Head of Emerging Markets Sovereign Risk at Deutsche Bank Research; **Marie Laurence-Faure**, Head of Marketing Product Channels, BNP Paribas; **Pat Leavy**, Executive Director, FTI Treasury; **Kevin Lester**, Co-CEO at Validus Risk Management; **Vanessa Manning**, EMEA Head of Payments and Cash Management, RBS; **Pascal Morosini**, Executive Director, Global Head of Global Securities Financing Sales and Relationship Management, Clearstream; **Francesca Mosca**, Director, Client Coverage, ING; **Sam Ocheho**, Head, Global Markets, Stanbic IBTC; **Anita Prasad**, General Manager, Treasury Capital Management, Microsoft; **Helen Robbins**, Senior Manager, Institutional, HSBC Global Asset Management; **Bea Rodriguez**, Head of International Cash Portfolio Management, Managing Director, BlackRock; **John Salter**, Managing Director, Global Corporate and FI, Global Transaction Banking, Lloyds; **Rainer Stirn**, Head of Treasury – Cash Management, B. Braun; **Karen Van den Driessche**, EMEA Treasury Director, AVNET; **Ad Van der Poel**, Co-Head of Product Management, Global Transaction Services, EMEA, Bank of America Merrill Lynch; **Claus Wild**, Project Manager Payments and Cash Management, Adolf Würth GmbH & Co KG; **Jonathan Williams**, Director of Payments Strategy, Experian.

IN THIS ISSUE

INSIGHT & ANALYSIS 19

Making the grade: credit ratings

Understanding the minutiae of the methodologies behind corporate credit ratings is not something many corporate treasurers have time for. Treasury Today looks at how the Big Three ratings agencies are trying to increase the transparency of their ratings methodologies, the impact the financial crisis has had on the credibility of ratings and what the future holds.

RISK MANAGEMENT 16

Emerging markets risk

Emerging markets now make up over half of global GDP. Despite this many investors, struggling to achieve a decent yield in developed markets, are not fully aware of the opportunities – and risks – emerging markets present. Do the risks outweigh the rewards of investing in these markets?

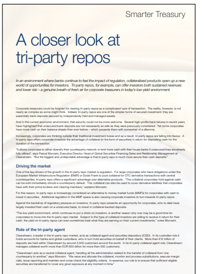
COMMERCIAL BANKING | EUROPEAN TREASURY TRENDS 26

Transforming treasury: going the extra mile

As treasurers become more involved in wider business activities, from enterprise risk management to board-level decision-making, regulation is challenging them to rethink the way they approach fundamental treasury tasks and relationships. Meanwhile, technology is enabling greater efficiencies, but also presenting a number of new threats.

in association with

SMARTER TREASURY 31


Smarter Treasury

A closer look at tri-party repos

in association with

clearstream | DEUTSCHE BÖRSE GROUP

PRODUCT PROFILE 38

treasurytoday Product Profile

Supplier finance: coming of age

in association with

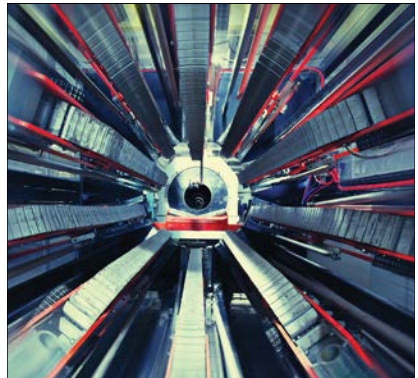
CASH MANAGEMENT UNIVERSITY 49

Rethinking connectivity

in association with

"Bank of America Merrill Lynch" is the marketing name for the global banking and global markets businesses of Bank of America Corporation. Lending, derivatives, and other commercial banking activities are performed globally by banking affiliates of Bank of America Corporation, including Bank of America, N.A., member FDIC. Securities, strategic advisory, and other investment banking activities are performed globally by investment banking affiliates of Bank of America Corporation ("Investment Banking Affiliates"), including, in the United States, Merrill Lynch, Pierce, Fenner & Smith Incorporated and Merrill Lynch Professional Clearing Corp., both of which are registered broker-dealers and members of SIPC, and, in other jurisdictions, by locally registered entities. Merrill Lynch, Pierce, Fenner & Smith Incorporated and Merrill Lynch Professional Clearing Corp. are registered as futures commission merchants with the CFTC and are members of the NFA. Investment products offered by Investment Banking Affiliates: Are Not FDIC Insured • May Lose Value • Are Not Bank Guaranteed. THE POWER OF GLOBAL CONNECTIONS is a trademark of Bank of America Corporation, registered in the U.S. Patent and Trademark Office. ©2014 Bank of America Corporation 06-14-0985.L

IN THIS ISSUE



TREASURY PRACTICE 22

Virtual accounts: keeping it real

Virtual accounts can help corporates rationalise the number of physical accounts held and simplify the management of these accounts, as well as improving reconciliation rates. Despite these enormous benefits, the solution is not yet mainstream amongst the corporate universe. We ask why.

COUNTRY FOCUS 28

Nigeria: the giant of Africa

Nigeria is an economic force to be reckoned with in Africa. Having undergone many changes and positive developments in recent years, including a rebasing which saw it become the continent's largest economy, we explore this fast developing country and highlight the salient issues for corporate treasurers operating in Nigeria.

TREASURY ESSENTIALS

Question Answered 6
Market View 9
Women in Treasury 11
Back to Basics 45

35 The Corporate View

Ingmar Bergmann

Corporate Treasurer and Head of Corporate Finance

nsi

As former chairman of the Dutch ACT and a voluntary treasurer of a Premier League volleyball team, urban agriculture scheme and a local Judo club, NSI Corporate Treasurer and Head of Corporate Finance, Ingmar Bergmann is a certainly more than just a day-to-day treasurer. Bergmann reveals how his unique skill set and delight in working with people have shaped his impressive career.

INDUSTRY VIEW 42

The Industry View

Bea Rodriguez

Head of International Cash Portfolio Management, Managing Director

BLACKROCK®

Against a backdrop of low, zero or even negative returns, heavy bank regulation and limited availability of quality investments, Bea Rodriguez, Head of International Cash Portfolio Management, Managing Director, BlackRock looks at what is currently trending for investors, plotting the rise of some very interesting alternative corporate cash management opportunities.

A new era for
cash management
Your partner, every step of the way
Times are changing in treasury, and it has never been more important to have the right partner by your side. Nordea's cash management solutions can support you. We offer everything from intuitive online tools that optimise your day-to-day payments and reporting, to global cash pooling and strategic advisory services that transform how you manage your liquidity.
To find out more, visit nordea.com/cashmanagement
Making it possible
tmi AWARDS 2013
FOR INNOVATION & EXCELLENCE
Awarded Best cash management bank 2013 in the Nordic region by TMI magazine
Nordea

Beyond SEPA

Now that the 1st August 2014 SEPA migration date has passed, does this signify the end of the migration process? What SEPA-related improvements should corporates now be working towards and what do non-EU companies need to think about?

Claus Wild, Project Manager Payments and Cash Management, Adolf Würth GmbH & Co KG:

The introduction of SEPA has brought a wide range of changes for the majority of European market participants. Even though the 1st August deadline has now passed, there is still work that can be done by corporates to maximise their SEPA projects.

During the migration period, many participants criticised the organisational complexity and lack of harmonisation between the data formats in the SEPA area. Indeed, if we look back on the migration and the implementation of EU Regulation 260/2012 in general, corporates have been – and still are – faced with many format and country-specific deviations from the SEPA standard.

As a result, we are still missing homogeneous data formats in the SEPA area, and only when these are achieved will corporates be able to fully reap the efficiency benefits of their SEPA projects. Despite this, we are still at the start of the journey regarding the opportunities which SEPA can offer corporates – after the initial consolidation phase, companies will need to examine further the benefits SEPA can offer.

Developments and changes

As a next step, or as a part of a centralisation project, companies can now look to bundle their payments in a payment factory or in a central hub. Furthermore, companies should assess their banking landscape and terminate any redundant bank accounts.

In addition, regarding the treasurer's banking administration, I expect further trends to develop. Primarily I expect corporates to increasingly require Bank Account Management (BAM) solutions and to ask for transparent bank charges (for example TWIST or camt.086 messages). Both of these should be at the top of the treasurer's wish list over the coming months as they will allow improved control and oversight over both bank relationships and costs.

Since the SEPA formats are limited to the SEPA area, CGI-MP formats will continue to gain importance in the global payments space. However, these formats are limited in the range of banks which can be included, and provide, as well as the SEPA formats, a certain degree of complexity. To close the cycle of XML formats I expect increasing bank statement processing for the XML bank statements (camt.053 or camt.054). Additional challenges will arise when attempting to integrate these within the company's ERP system.

Finally, companies which are primarily engaged in business-to-consumer (B2C) activities could focus their efforts on simplifying the collection from the often unloved BIC and IBAN. In addition to this, I expect increasing QR codes on invoices to facilitate the simplification. The relevant payment data is encrypted in the QR code, which can be scanned and paid easily with an app on a smartphone by the customers. The recipient will then receive the exact information they need to process the payment in the ERP system.

Brian Hanrahan, EVP Sales and Marketing, Sentenial:

The revised SEPA end date has now passed and so in principle every business using SEPA credit transfers or direct debits will be following the new regulations. In reality there could be some stragglers, particularly direct debit users who, say, collect annually, but these will be a very small percentage of the total.

All but a small number of companies with particular needs treated the move to SEPA as a regulatory issue, something that had to be done at a cost but something that generated little or no business benefit. A direct consequence of this was that businesses left migration to the last minute only to discover it was actually more difficult than they had anticipated leading in turn to project overruns.

Whilst businesses had ten years to plan for this, the last minute dash has resulted in many tactical solutions being deployed that are not necessarily optimum in terms of efficiency or the features they support. With material volumes of transactions now flowing through SEPA we are gradually seeing the schemes settle down to more of a business as usual, stable process. Progressively inconsistencies and uncertainties are being ironed out, it has to be remembered that the processes are nearly as new for the banks and infrastructure as they are for businesses.

Actual experience of a process is invaluable and based on this we are seeing growing interest in implementing more robust solutions and solutions which better fit a business user's environment. Apart from improving the solidity of the processes used to

generate the new SEPA data, businesses are also looking at mechanisms to deal with the exceptions produced by the scheme, the so-called R messages. Another area that has caused confusion, particularly for direct debit users, is reconciling the process in terms of balancing what money businesses expect to receive with what actually arrives in their bank account. Much confusion here results from the differing clearing cycles applied to the first and subsequent collection in the debit scheme, something which did not happen in most legacy schemes.

For the small number of businesses that operate in a multinational way within the Eurozone, other opportunities also exist to rationalise banking relationships. Very few businesses undertook this before the end date, but now some are embarking on projects to review the benefits that may arise from this process. Businesses operating within a single country could opt to use a different bank, either in their own or another country to reduce costs, but there is not much evidence of this happening.

Another area attracting attention is the use of paperless mandates in the direct debit process. The functionality is required by a significant percentage of users but has been badly handled within SEPA. Many countries had well established procedures for paperless mandates before SEPA and the move back to a paper-based environment is not seen as very progressive. There is still considerable confusion on this topic both with business users and banks alike. This is an area where solutions are now emerging and the market may dictate the outcome rather than the scheme, simply down to the time being spent to resolve.

Francis de Roeck, Head of SEPA Offering, BNP Paribas Cash Management:

The SEPA migration is now complete in euro countries. The figures speak for themselves, with SEPA Credit Transfers (SCTs) being fully migrated as of July 2014 (98.47% rate according to the European Central Bank); whereas the SEPA Direct Debit (SDD) showed a 97.01% migration rate. It is interesting to see that SDD volumes took off at a very late stage of the SEPA calendar.

As a reminder, the original end-date for the 18 countries of the Eurozone was 1st February 2014. However, an additional six months were granted by the European Institutions to allow for all economic players concerned to smoothly complete their migration.

Even though the migration period is now behind us, SEPA remains high on the agenda. For example, countries that declared niche products are now looking to replace these products either by integrating them into existing schemes or by introducing Additional Optional Services (AOS). Stakeholders are still addressing the topic of niche products, and no final decision on how they will be replaced in February 2016 has been made as yet.

Some countries (eg Italy, Spain, and Portugal) have also requested a waiver on legacy formats, meaning that corporates can still use non-XML formats; meanwhile banks will continue converting them until February 2016. However, given the current volumes still being handled in legacy formats, a heavy migration effect is still to come.

Looking more closely at the implementation of SEPA, the SEPA workflow is now up and running. Considerable volumes are being handled, with more than 36 billion credit transfers and direct debits being exchanged. To date, corporates have mainly focused on migrating, however, and the full benefits of SEPA have not yet been leveraged.

The next step

Now that SEPA is a reality, corporates can develop a more concrete, broader sense of the initiative's potential. At BNP Paribas, we believe that SEPA is a strong driver for treasury centralisation: payment and collection factories with frequent payments and collections-on-behalf-of (PoBo and CoBo) can all be enabled through SEPA. We have supported countless migrations on behalf of EU and non-EU corporates, and we know that beyond the regulatory and compliance aspects, SEPA is seen as a facilitator for standardisation and harmonisation. Moreover, the richness of SEPA XML reporting should typically ease the reconciliation process. Most of the benefits come from streamlining internal processes, rather than from the optimisation of bank relationships.

Corporates are now in a position to significantly reduce operational and processing costs and improve their treasury through greater automation and bank rationalisation. However, some challenges are still keeping them from taking full advantage of SEPA, and significantly improving their order-to-cash cycle as a result.

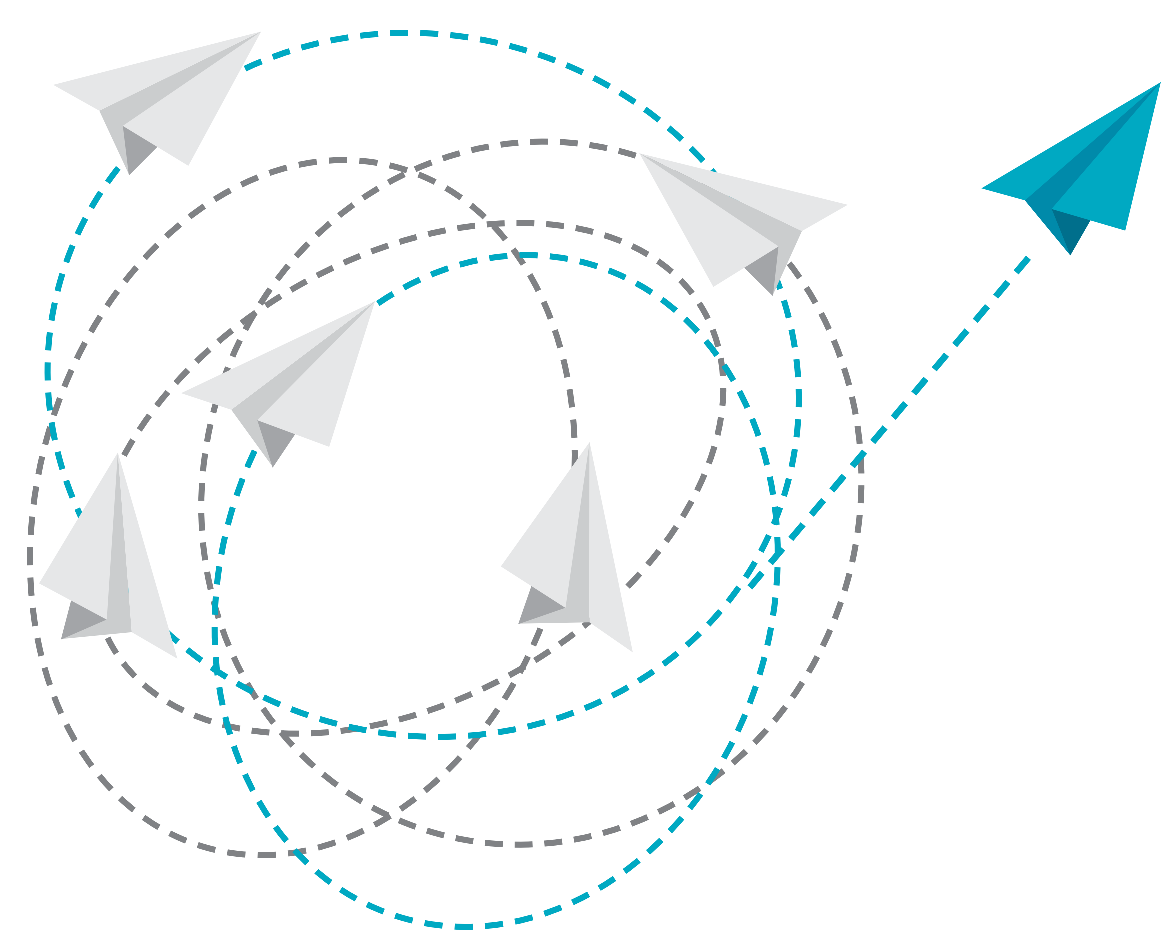
Today, it is important for non-EU companies to understand the momentum that SEPA has created in Europe if they want to take advantage of the latest market trends. For example, the standardisation brought by SEPA actually makes it possible to optimise the implementation of treasury projects.

The next question:

"For the treasury function, information is key. With the constant evolution of technology and the rise of big data, have there been any notable changes in the way that treasury departments obtain their information? Also, how can treasurers manage enhanced data and turn it into tangible business information?"

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

Clearstream
Global Liquidity Hub
We make finance flow



Are you looking for safe and efficient cash investments?

Discover our triparty repo service and benefit from collateralised deposits while maximising your cash returns.

gsf@clearstream.com

Applying the monetary brakes

As some economies, including the US and the UK, show signs of approaching full employment in the not-too-distant future, growth may need to slow in order to prevent higher inflation and unsustainable rises in interest rates. This means that policy-makers may need to apply the monetary brakes, says ECR Research.

The projections for the coming years suggest that growth will be low around the world. In industrialised countries, this points to growth near 2%. In China, growth should hover around 7.5%. From a Western perspective, such a percentage seems almost unattainable, whereas the authorities in Beijing think that if growth were to decline any further, social unrest would ensue. Moreover, this rate is substantially below what the Chinese have been used to in recent decades. Something similar applies to many other emerging economies.

Deflation threatens

At first glance, these conditions do not seem conducive to rising interest rates. Quite the opposite; sluggish growth will likely put downward pressure on wages and inflation. It could even lead to deflation. As debts are sky high, that is a risk these economies cannot afford to take as the result could be a downward deflationary spiral. The way to counter this is through ultra-loose monetary policy and persistently low interest rates. If this is a realistic scenario, the financial market trends of the past years will continue. That is to say: stock market rallies, downward pressure on long-dated government bond yields, and narrowing credit spreads.

It would also point to relatively low volatility in the currency market as most countries appear to be 'in the same boat'. However, we do not think this analysis is valid, most of all because the reason for weak growth varies among the different countries. In some, demand is stagnating and elsewhere supply threatens to falter. This has a very different impact on market rates and prices.

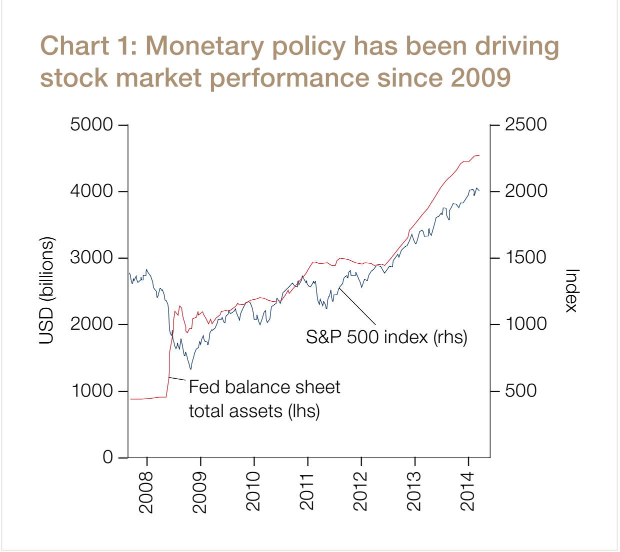
During the credit crisis, lending froze, income declined and deleveraging took place in the US as well as in many other countries. Overcapacity meant that deflation risks were high. At the same time, preventing deflation was the top priority for the US authorities. Ironically, they could only achieve this by accumulating more debt. To this end, the budget deficit widened. Simultaneously, the Fed lowered interest rates and launched a massive bond-buying programme to create more money. Eventually, asset prices rallied, especially property and share prices. This pushed up asset values in the private and business sectors. While the level of indebtedness continued to be high, it was at least offset by more valuable collateral. In turn, this facilitated new borrowing.

Tipping point

However, the higher debt (taken out following the credit crisis) was viewed as a temporary emergency measure to prevent deflation. In the slightly longer term, the idea was always to boost growth until full employment was achieved and (real) wage increases went up. The moment when real wage increases start to rise is crucial to the economy – a genuine tipping point. Generally, this happens in the case of (almost) full employment.

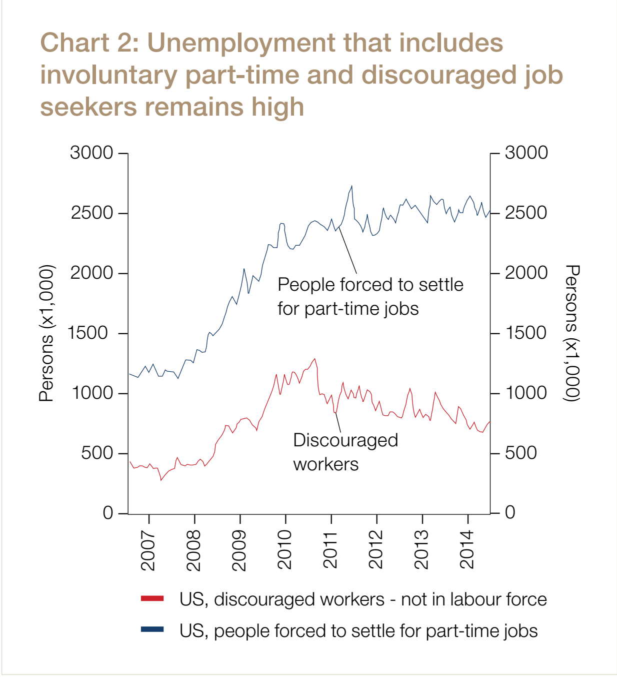
It is no secret that Fed chairwoman Yellen believes full employment is still some way off in the US. Although the jobless rate has dropped from over 10% to around 6%, she thinks there is a lot of hidden unemployment. In addition, a further fall in unemployment is unlikely to happen any time soon. At first glance, this suggests that it will be possible for the Fed to boost the economy for some time to come – and to postpone its rate hikes. However, many economists (including those who are close to Ms Yellen) are beginning to question the wisdom of such a course of action:

- Studies indicate that there is a significant mismatch between what businesses expect of their employees and what job applicants have to offer in terms of skills and/or education.
- Demographic trends suggest the decline in the participation rate (the percentage of people of working age available for the labour market) will decline further. Fed research suggests in 2016 just 45,000 additional workers will enter the labour market each month. To put this in perspective: this year, on average 200,000 new jobs have been created on a monthly basis.



Source: Thomson Reuters Datastream/ECR

Chart 2: Unemployment that includes involuntary part-time and discouraged job seekers remains high



Source: Thomson Reuters Datastream/ECR

The European approach

The surprise ECB rate cut and announcement to buy up various bank loans in early September differs from the actions of the Fed. The latter has focused on purchasing bonds, as most US credit is supplied via the capital market, whereas in Europe almost all of it comes from the banks. It seems an effective way to boost credit. After all, one of the main reasons why growth is sluggish in Europe is that the banks are reluctant to lend; specifically in the weak Eurozone countries.

Many economists fear that regardless of interventions by the ECB, economic growth will remain low in the EMU. They point out that the demand for credit is sluggish in both the business and the private sectors. Based on this, they assume that – eventually – the central bank will have no choice but to purchase government bonds on a large scale. However, some European governments are strongly opposing such large-scale quantitative easing as happened in the US:

- They want to avoid growth fuelled by credit that could lead to another crisis.
- Germany and the ECB in particular want more structural reforms to increase the added-value per worker to generate growth. They worry that once easing credit starts to boost growth, structural reforms will never be implemented, which would jeopardise the future of the whole of Europe.

For this reason, the ECB is proposing a deal. It will keep the money taps open – alongside some fiscal stimulation, as far as the central bank is concerned – on the condition that structural reform takes place. The latter will not happen overnight. So for the moment, Germany and the ECB will only boost the economy to the extent that deflation and a negative spiral can be avoided. In practice, this points to growth rates near 1.5%, barely higher than the productivity increase. In other words, the unemployment rate is unlikely to fall (substantially).

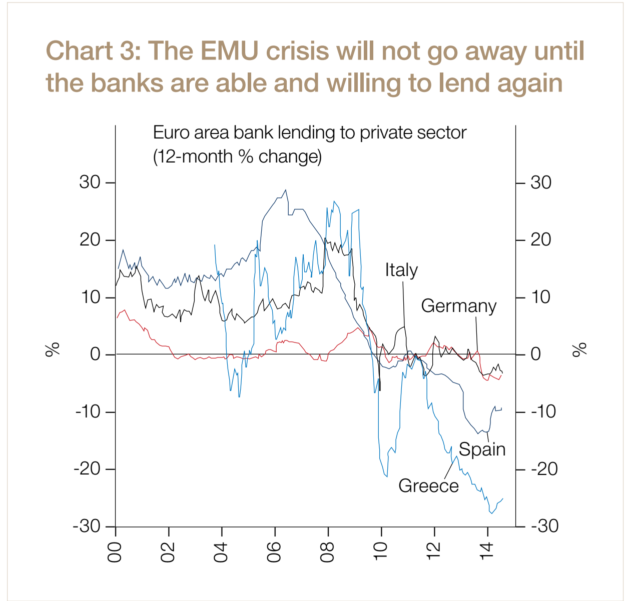
The only other 'windfall' that Europe can expect is euro weakness. The US will certainly not object to this: as full employment approaches, a stronger dollar would be helpful.

Conclusion

Global economic growth seems set to slow in the coming years, except, perhaps, in emerging economies that manage to substantially boost domestic demand. The reasons why growth is and will be sluggish vary from country to country. In the US and in the UK, we could see full employment in the not-too-distant future. Subsequently, growth will need to slow in order to prevent higher inflation and unsustainable rises in interest rates. In the EMU, outside Germany there is a lot of slack in the economy. At the same time, it is impossible to rapidly stimulate growth due to sluggish demand.

Whereas the Fed and the Bank of England are approaching the moment when they have to apply the monetary brakes, the euro area will need very loose monetary policy in the years ahead. This means we expect US interest rates to increase by much more than those in the EMU and that EUR/USD will decline to 1.20 and lower in the coming months and quarters. ■

Chart 3: The EMU crisis will not go away until the banks are able and willing to lend again



Source: Thomson Reuters Datastream/ECR

Unique approach for time pressed decision makers

ECR's unbiased and thought provoking research on the major currency and interest rate markets is subscribed by thousands of CFOs and treasurers globally. Get your complimentary trial on www.ecrresearch.com and experience your new web based research solution!

Leaving the grey suits behind

Treasury Today's recent Women in Treasury Forum in London was certainly a colourful event. Stern opinions, bold personalities (and some fantastic fashion sense) saw traditional treasury stereotypes pushed to their limit.

In the world of corporate treasury, being in a room with 185 female colleagues and just five male peers is a rather unique sensation. But challenging the norm is precisely what Treasury Today's Women in Treasury initiative is all about – and for those 190 attendees, the second annual Women in Treasury Forum that took place in London on 18th September certainly delivered.

Although conversations during the pre-lunch networking session were already sparking much debate, Angela Berry, Publisher of Treasury Today and Founder of the Women in Treasury initiative, prompted further dialogue by sharing some of the findings of this year's Women in Treasury Study, proudly supported by RBS. One of the most surprising highlights – judging from the audible gasps in the room – was the fact that 4% of respondents (all female) believed that they were being paid more in their current role than their male counterparts. Somewhat predictably though, the number of women that felt the reverse, was still very high at 48%, the Study showed.

Another contentious statistic was that, despite so many women having family responsibilities, 56% do not have flexible working arrangements. In the 25-34 age range, this figure increases to a significant 72%. So it's clear that achieving an effective work life balance still remains tough for many professionals – both female and male. And it's no coincidence that this topic was the first to be addressed by the lively panel session which took place after lunch.

A tricky balancing act

Treasury Today's Woman of the Year – Anita Prasad, General Manager, Treasury Capital Management, Microsoft – was the perfect person to pick up this subject and share her experience and knowledge with the audience. According to Anita, the secret to achieving a balance between her work life and her home life is to not forcibly separate the two. "Work is part of my life, just like my family is, my friends are and my hobbies are. Rather than trying to juggle my work and my home life, I prefer them to be intertwined – my work is key to defining who I am. That's why it is so important to find a job that you have a passion for so you can feel professionally fulfilled. If you can do that, it won't even seem like work," said Anita, prefacing that observation with the disclaimer that it might not be everyone's ideal solution.

For some, it might seem like having such a close connection between your work and family life would mean that work would always intrude, but Anita believes in leveraging technology and setting clear expectations with her partners and stakeholders to define her optimal balance. "My team knows that I am always reachable except for the two hours starting at 5.30am three times a week; it is my gym time. It is equally important to balance needs of your team and business deliverables and make exceptions if needed. This is when the ability to leverage my smartphone, tablet and data that is always available in the cloud is a great enabler," she explained.

"Similarly, my husband respects the fact that the first thing I do in the morning is to check my emails on my phone. Once I'm up-to-speed with work, it's easier for me to focus on the family – because I'm not thinking about what might be going on at work in the back of my mind," she admitted. You need to live in the moment and be fully devoted to work (or family) while you are at work (or vacationing with family); don't feel guilty about spending time on either aspect of your life.

In addition to setting clear boundaries, "I have a set of clear principles that guide me in everything I do: honesty, integrity and trust," Anita told the audience. These principles have helped her throughout her career to maintain the work/life relationship that she has so successfully mastered.

Battle of the sexes

The next panellist to speak was Jennifer Boussuge, Head of Global Transaction Services, EMEA, Bank of America Merrill Lynch, who tackled the topic of driving equality. Like Anita, Jennifer wakes up every day with her BlackBerry in her hand – but she too has a very understanding husband who, Jennifer explained, actually put his career on hold in order to allow her to progress.

"I'm extremely lucky because, throughout my career, I've been given the support that I need both at home and in the workplace. Many women don't have that luxury and they struggle to reach their full potential in the workplace as a result," noted Jennifer. "That's a real shame, because the statistics around the value that women in senior positions bring to a company are quite something. A McKinsey study, across all industry sectors, found that the companies with the highest proportion of women on their boards significantly, and consistently, outperformed those with no female representation by 41% in terms of return on equity, and by 56% in terms of operating results. The numbers speak for themselves."

So what is holding women back? "What women require to be successful isn't always the same as what men need to be successful," Jennifer observed. "We need to carefully consider the level of coaching and mentoring that we are providing for women – not only on returning from maternity leave, but throughout their careers. Women often aren't as vocal as men in the workplace, and managers need to recognise that. Just because women don't voice their desire for promotion, doesn't mean that they don't want the opportunity."

As well as improving the formal networks, it is also important for women to take it upon themselves to do more informal networking, she explained. "Men play golf or go to the pub on Thursday nights for a drink. Creating these kind of networks for women, while also ensuring they have key sponsors and mentors from within the organisation, are vital to encourage greater diversity at senior levels."

The dream team

Sonia De Paolis, Treasury Director at TomTom – and the next panellist to speak – agreed with Jennifer's observations, saying: "We work in a male-dominated environment and we need to create the space for women to proceed. As such, it is important to have self-awareness about what you want to do and where you want to go; don't just do what is expected."

On the subject of nurturing talent, Sonia had some useful, practical advice for attendees: "When you look for talent, the most important thing is to put your biases to one side." She went on to explain that there are sometimes hidden gems – people that might not necessarily tick all the boxes on paper, but in reality have a lot to offer. "As an example, there was a young lady who was in an administrative role in another department in our company, who volunteered to get involved in a cross-functional project at a time when no-one from that department was being overly co-operative. She was absolutely brilliant when we collaborated, so much so that we invited her to join our team and gave her the opportunity to study for her qualifications as well. She jumped at the chance and she was enormously motivated by the recognition of her abilities."

Not only is it important to nurture hidden talents, but the whole team should be given something to believe in – a vision and a mission, Sonia added. "Creating a work environment where people feel that they are really part of something is invaluable. People work hard for what they believe in."

Climbing the ladder

Building a dream team is also a very important step in helping you to get further ahead in your career, according to the final panellist, Claudia Colic, Head of Transaction Banking, UBS AG, Switzerland. "You need to have the confidence to hire the best team possible – don't be afraid to hire people that are

better than you at certain aspects of the job and don't be afraid to be challenged by your team," she advised.

Other key steps in moving up the career ladder, said Claudia, are: understanding who you are and recognising where your strengths, weaknesses and interests lie. "Once you know what you want and what your interests are, then you can match them with your strengths – not that they are always complementary. Then, you can begin to cultivate a recognisable identity for yourself, rather like a personal brand, so that everyone knows what you stand for." To really get ahead, this brand also needs to be authentic, Claudia noted. "Generally speaking, women aren't good at pretending to be something they're not."

Finally, Claudia advised attendees to work on communicating with confidence if they want to get ahead in their career. "Because of our collaborative nature, women often like to ask others their opinion, so that everyone has a chance to voice their thoughts. Although this is in many ways good for the team, it can make it seem like you don't have a firm opinion of your own. That's not what people look for in a leader – they want someone who knows their own mind."

Securing success

After the panel's individual presentations, there was a lively question and answer session that covered everything from part-time working to the relative productivity of women returning from maternity leave – which interestingly, the panel felt was actually greater, since new mothers are more motivated to get everything done in order to leave the office at a decent hour!

Some additional networking then took place over coffee before the event closed. This was a good opportunity to gather some feedback on the Forum from attendees and to find out what advice they would be taking away from the event. Karen Van den Driessche, EMEA Treasury Director, AVNET, said: "Anita is the perfect fit for the Woman of the Year Award, she totally deserves it. I particularly enjoyed her comments about managing your work/life balance effectively, and that if you are passionate about something then it shouldn't be seen as work."

Francesca Mosca, Director, Client Coverage at ING was impressed by the 360 degree approach to the topic of Women in Treasury. "There really was advice for everyone from the panel, whether it be how to learn from your mistakes, or how to leverage informal as well as formal networks in order to get ahead. Another key takeaway for me was the panel's advice around building a brand for yourself. It's important to match your strengths with your interests and skills, so that you can be confident in what you do.

On the topic of work/life balance, the point around distinguishing between a job and a career seemed to strike a real chord with the audience. A job is a nine to five, but a career will always be part of your life. To be successful in your career, there will naturally be risks that need to be taken and compromises that need to be made," she said.

Helen Robbins, Senior Manager, Institutional Client Propositions, HSBC Global Asset Management agreed that the stories from the panel were very inspiring. "I liked the point that even senior women still need a mentor. And that it's ok to ask someone to be your mentor – women should have the confidence to do this. It is also important to understand how others have overcome issues in the workplace and you don't often get that opportunity outside of events such as this. The Women in Treasury Forum is a vital platform for networking and knowledge-sharing," she observed.

The mentoring discussion was also very interesting for Claudia Ehler, European Treasury Manager at SPX Corporation. "I haven't had a mentor for many years and I've been inspired by the panel's comments to go and look for a mentor. I've also learned that it's ok to ask people that aren't necessarily in your immediate work circle to mentor you – it could be someone that you admire in another company."

Elsewhere, "getting together with peers and having a forum focused on women makes the discussion more open and frank as we have similar challenges to manage," commented Claudia. This sentiment was shared by many others in the audience, who greatly appreciated the focus of the event, but would also like to see more men at next year's event so that they can hear first-hand about the challenges that women face in the world of treasury. Consider the gauntlet well and truly thrown down. ■

Women in Treasury Annual Study 2014

proudly supported by

The backbone of Treasury Today's ground-breaking Women in Treasury initiative is the annual Study that we conduct among female treasury professionals across the globe. This year's Study, proudly supported by RBS, builds a clear picture of the careers of women across the industry.

The results are in...

Conducted between April and September 2014, the Study attracted over 220 responses from a broad universe of respondents. From a geographical perspective, 22% of respondents were located in the Asia-Pacific region, 14% in the Americas, and 62% in Europe, with the remainder being Rest of World. Respondents were aged between 25 and 65 years; 57% have been working in corporate treasury for over 10 years and 76% are professionally qualified.

Highlights

One of the most contentious areas of the Study was, unsurprisingly, pay equality. This year's findings reveal that 48% felt they were being paid the same as their male counterparts, 48% felt they were being paid less, and 4% felt they were being paid more. This is an improvement on the 2013 results, which indicated that 58% believed they were not being paid the same as their male colleagues.

An aspect of corporate life where there is still a great deal of room for improvement (not just for women but for men too) is around mentoring. Despite an enormous 98% believing that mentoring is beneficial in career advancement, only 37% of companies provide a mentoring programme. The number of companies that still do not allow flexible working arrangement is also high – at 44%. So it is clear that corporate attitudes to modern life and the needs of their employees still have some way to progress.

Nevertheless, the level of support that mothers returning to work from maternity leave are receiving from their employers appears to be positive, with three-quarters of respondents saying that the company they work for is proactive in this regard. Interestingly, despite just over half of respondents (53%) having dependent children, 77% said they were prepared to move to a new region or country in order to progress their career.

When we asked respondents in more detail about their career aspirations, the majority were ultimately aiming for the role of Group Treasurer, with Director Treasury & Finance in second place, and CFO third. One of the more surprising findings of this year's Study was that when asked to rank certain factors in order of importance to their career enhancement, job satisfaction was voted the number one most important factor – above a clear career path in treasury; above being treated equally; and above being accepted by senior management. This begs the question: if women were treated equally; had a clear career path; and were accepted by senior management; would that actually lead to increased job satisfaction?

Moving ahead

As we build on the Women in Treasury Study each year, we will continue to analyse the questions and challenges that the females in our profession face every day. We will also strive to share best practice and knowledge among the treasury community. To that end, we would like to thank everyone involved in this year's Study – we could not have done it without you.

We'd also like to encourage you to join our Women in Treasury LinkedIn Group where you can carry on the discussion, contribute your insights and benefit from an amazing networking opportunity. Simply contact our Circulation Manager, Sarah Arter, on sarah.arter@treasurytoday.com to join and be part of our successful programme. ■

Carole Berndt

Managing Director, Global Head Transaction Services, RBS

Speaking on behalf of RBS, an organisation committed to promoting diversity within the workplace, I believe supporting the Treasury Today Women in Treasury initiative is a natural extension of how seriously we take our responsibility to build understanding and encourage discussion around this important topic. But as a woman working in a male-dominated industry, I also know how absolutely vital it is to share the experiences, the challenges, the successes and the failures, so that we may speak as one within in our chosen profession.

In the course of my career in treasury I have met many incredible women, all of whom have been innovative, determined and ready to help others achieve success in their chosen field. The 2014 Women in Treasury Study gives voice to these inspirational people. But more importantly, it delivers a clear picture of the careers of all women across the industry, from the most senior to the most junior, allowing everyone to have their say.

The 2014 Women in Treasury Study is a valuable contribution to the discussion and promotion of the issues that really matter to women in the workplace. We all have responsibilities to our organisations, but we also have responsibilities to ourselves and to our families too. Hearing how other women in treasury tackle the core issues of work-life balance, career progression, mentoring and pay parity, all the while maintaining a sense of personal identity gives a focus to the voice of women in treasury. As sponsor and as a woman I am proud to be a part of it.

AVIVA INVESTORS LIQUIDITY FUNDS

In 2008, Aviva Investors took the view that AAA-rated money market funds should be VNAV in structure. The industry disagreed. In 2014, the SEC issued new rules requiring institutional money market funds to go VNAV. European regulators are expected to issue similar rules in the near future. In the six years since moving to VNAV, Aviva Investors has developed unique, market-leading experience in managing VNAV money market funds with no volatility in the daily NAV.

To find out more go to **avivainvestors.com/liquidity**
call **020 7809 6000** or email **colin.cookson@avivainvestors.com**

For investment professionals only. This is not to be viewed by or used with retail clients.

Unless stated otherwise, any sources and opinions expressed are those of Aviva Investors Global Services Limited (Aviva Investors). They should not be viewed as indicating any guarantee of return from an investment managed by Aviva Investors nor as advice of any nature. Past performance is not a guide to the future. The value of an investment and any income from it may go down as well as up and the investor may not get back the original amount invested. This document should not be taken as a recommendation or offer by anyone in any jurisdiction in which such an offer is not authorised or to any person to whom it is unlawful to make such an offer or solicitation. Aviva Investors Global Services Limited, registered in England No. 1151805. Registered Office: No. 1 Poultry, London EC2R 8EJ. Authorised and regulated by the Financial Conduct Authority and a member of the Investment Management Association.

Contact us at Aviva Investors Global Services Limited, No. 1 Poultry, London EC2R 8EJ. Telephone calls may be recorded for training and monitoring purposes.
A14/0586/311214

Emerging market risk

Despite the fact that emerging markets now make up more than half of global GDP, many investors are still in the dark about the risks and opportunities they present. We spoke to a range of experts to find out what emerging markets are, the special challenges they pose, and their outlook for the future.

Investing in emerging markets (EMs) can be something of an acquired taste. Even while investors struggle to achieve a decent yield in developed markets, some still balk at the high risk they perceive to be inherent in EMs. Recent performance of EM stocks has done little to inspire investor confidence.

Indeed, EMs underwent a torrid end to the third quarter of 2014. In September, the FTSE Emerging Index, comprised of large- and mid-cap securities from advanced and secondary EMs, declined for seven days in a row, dropping almost 3% for the week. This was both the longest run of falls – as well as the largest weekly decline – since November of the previous year.

Increasing Treasury yields have historically harmed developing markets, and talk of the Fed potentially raising its benchmark interest rate has had this exact effect. "EM assets have again come under pressure as fears of higher US rates and a stronger dollar have outweighed the promise of additional liquidity from the ECB," wrote Robert Burgess, Chief Economist at Deutsche Bank, in a research note published in September.

However, as has been widely reported by the financial press, some EMs' current and prospective growth dwarfs that of many developed markets. For instance, both India and China have exceeded GDP growth in the US by at least 1.5% every year since 2001. What exactly are EMs, and what are the risks investors need to understand before venturing beyond developed markets?

Defining emerging markets

One challenge with emerging markets is actually defining what they are. The term itself is not particularly helpful. Considering that EMs now make up more than half of the world's GDP according to the International Monetary Fund (IMF), the word 'emerging' appears to be something of a misnomer. Many of these markets have very much emerged already.

While it is reasonably safe to assert that some economies, such as the US, are developed, and others, such as Chile, are emerging, the exact measure of why some are EMs and others are not can be ambiguous. And many countries qualify as EMs according to some criteria but not others.

"There is no hard and fast rule for defining EMs – it's an amalgam of lots of different things," says Timothy Ash, Head of EM Strategy, Ex Africa at Standard Bank. "You can look at per capita GDP, but it is more subjective than that. There are also factors such as institutional capacity and strength, business environment, rule of law, legal system, and political stability. Some countries are clearly emerging markets, while others are borderline, and on top of this the parameters are constantly shifting."

The Czech Republic, for example, makes it onto the FTSE Emerging Index (as one of its 'advanced EMs'), but it does not qualify as one of the IMF's 'emerging economies'. Conversely, the IMF considers Estonia an EM, although the Baltic republic does not feature on the FTSE's Index.

Another EM yardstick is the G10 currencies. The 11 economies that make up the confusingly named Group of Ten (comprising Belgium, Canada, France, Italy, Japan, the Netherlands, the UK, the US, Germany and Sweden, as well as the 11th member, Switzerland, which joined later) are widely considered to be developed by most measures. Some investors and economists consider that anything beyond G10 could reasonably be an EM, although opponents claim it is an overly broad definition.

While there is some ambiguity as to what an EM is, there is more consensus around the benefits they present investors. The biggest of these is pure and simple yield.

Chasing yield

"Yield is a big selling point for EMs, as there is really no yield left anywhere else," Benoit Anne, Head of EM strategy at Societe Generale tells Treasury Today. "Quantitative easing policies undertaken by the Fed and other big central banks in developed economies have pushed rates to record lows for quite a few years now. This has driven a strong appetite for EMs among investors."

Despite the attractiveness of EM yields, the markets are not immune to turbulence. The MSCI Emerging Markets Index hit 1,083 at the beginning of 2013, before falling to as low as 883 in June of that year – a fall of almost 20% (see Chart 1). Only in Q3 2014 has it started to reach the heights of January of the previous year.

"Of course last year there was a massive correction in EMs, simply because markets sometimes need to correct themselves when they become over popular and overpopulated," adds Societe Generale's Anne. "But overall EMs still offer a favourable environment. The European Central Bank's recent big policy signal (to cut interest rates to a record low and to buy up private sector bonds, in September) is promoting this environment, and until the Fed starts hiking its rate, EMs will continue to be well positioned."

This favourable environment for investment has been facilitated by economic, infrastructural, and political advances in many of the larger EMs.

"EMs have undergone a tremendous change with respect to the economic fundamentals over the past ten to 15 years," says Maria Laura Lanzeni, Head of Emerging Markets Sovereign Risk at Deutsche Bank Research. "There is a very long-term structural trend in many of these markets towards better management of external debt, reduced exposure to dollarised debt and dollarised banking sectors, increased fiscal prudence as well as more central bank independence and anti-inflationary policies. These trends are obviously not present in all EMs, but overall the average EM is much better placed from an investment and risk perspective than in the 1990s."

Furthermore, this contrasts with conditions in certain developed markets, which in recent years have not progressed in this respect, and have indeed in some ways regressed. A number of large developed markets have gone backwards, especially in terms of their fiscal accounts and public debt, including the Eurozone, Japan and the US. Given the very serious fiscal problems the governments of these developed nations are grappling with at the moment, EMs can therefore look relatively attractive to investors.

Standard Bank's Ash concurs that recent events have made the case for EM investment somewhat more attractive in relative terms. "Some EMs are arguably less risky than some developed markets these days," he argues. "Particularly in the case of sovereign debt, the European periphery crisis has proven that many developed markets are perhaps not what you think they are, and that perhaps the ability and willingness to pay off sovereigns in some EMs are better."

He cites Poland as an example of this. Though an EM according to many measures, its balance sheet and willingness to pay off sovereign debt is superior to many Eurozone periphery countries, he says.

First world problems

Beyond the yield benefits, diversification is another factor drawing many investors to EMs. "There is a structural drive among the investor base to allocate more of their assets to EMs simply to reflect these markets' greater share of global GDP," explains Standard Bank's Ash. "Especially from a fixed income perspective, investment funds' investment mixes are still generally underweighted in their exposure to EMs."

However, as they compete with developed markets for investment, EMs have also started to experience some of the 'first-world problems' their more developed counterparts are used to. Rapid growth must also be handled sensibly and sustainably, otherwise it may be short lived.

Brazil, for example, once the darling of many EM investors and part of the BRIC group (also comprising Russia, India and China), has struggled of late. Partly on the back of foreign direct investment, its GDP rocketed from $504 billion in 2002 to a whopping $2.5 trillion in 2011 – almost a five-fold increase. In 2012 its GDP decreased to $2.25 trillion, and in September 2014 economists reduced their forecasts for the country's expansion – the 15th downgrade in Brazil's growth outlook so far in 2014. Brazil, which is the largest economy in Latin America, fell into technical recession in Q1 2014.

"As EMs come into the mainstream, they also become subject to the same trends and fluctuations in their business cycle that affect more developed economies" says Deutsche Bank's Lanzeni. "Much of the euphoria that surrounded Brazil five years ago was perhaps premature, as lots of money flowed into the country, but reforms then started to falter, with obvious repercussions for the country's growth. As economies grow, so too does the extent to which they are subject to global economic conditions at large."

Currency restrictions

One key challenge to investing in EMs is the currency restrictions in place in certain jurisdictions.

"Currency controls and direct intervention in FX markets are key factors impacting both equity and fixed income investments in EMs," says Societe Generale's Anne. "The exchange rate policy a government pursues also needs to be considered before you invest there."

The difficulty for those looking to invest in these markets is that these controls are often subject to rapid change. However, this change can also work to the advantage of investors. China is a prime example of an EM where rapid regulatory change is benefitting foreign investors.

"The possibilities from a currency standpoint in China today are significantly greater than they were two or three years ago. While a full-scale hedging programme for RMB risk is still not as easy as it is for euro-dollar risk, it is now feasible at least," says Kevin Lester, Co-CEO at Validus Risk Management. "A fast-changing regulatory background is one of the defining features of EMs. It is important that treasurers take this into account when drawing up a risk management programme for EM investment, and that they remain adaptive and open to rapid developments."

In addition to tighter currency restrictions, another argument sometimes made against EM investment is that many less-developed jurisdictions are rife with corruption. Obviously generalisations like this are of extremely limited value.

The Corruption Perceptions Index, published by NGO Transparency International, is a ranking of 177 countries and territories based on how corrupt their public sector is perceived to be. Countries are scored from 0 (highly corrupt) to 100 (very clean). In the most recent Index published in 2013, two-thirds of countries scored below 50, with none scoring the top 100 score and none the minimum 0.

Denmark and New Zealand topped the index with scores of 91, with Finland and Sweden in joint third (with a score of 89) and Norway and Singapore joint fifth (with 86). The most highly corrupt countries, according to the index, are Afghanistan, North Korea and Somalia (joint 175th place, with a score of 8).

The Index suggests that EMs do tend to be more corrupt on average than developed countries. There are, however, some notable exceptions. Italy, a developed economy by most measures, comes in joint 69th place (tied with Kuwait and Romania on 43 points). Barbados, meanwhile, is ranked joint 15th (tied with Belgium and Hong Kong on 75 points), while Chile and Saint Lucia come in at joint 22nd (tied with France with a score of 71).

Of the BRIC nations, Brazil is the highest ranked, in joint 72nd place (tied with Bosnia and Herzegovina, Sao Tome and Principe, Serbia and South Africa, with 42 points). Russia is the lowest-ranked of the 'big four', ranked joint 127th place (tied with Azerbaijan, Comoros, Gambia, Lebanon, Madagascar, Mali, Nicaragua and Pakistan with a score of 28). China comes in at joint 80th place (tied with Greece on 40 points), while India is

ranked joint 94th (tied with Algeria, Armenia, Benin, Colombia, Djibouti, the Philippines and Suriname on 36 points).

Standard Bank's Ash points out that the problem of corruption is not limited to EMs. "Corruption is everywhere, and we have seen high-profile corruption cases in developed markets. Clearly, high levels of corruption stall economic growth, slow investment, and make the business environment more challenging," he says.

Deutsche Bank's Lanzeni concurs that there are a number of examples of corrupt jurisdictions in developed markets and 'cleaner' EMs. "Long-term corruption has a negative impact on a country's growth prospects, and while this remains a problem in many emerging economies, there are examples of 'islands of cleanliness', such as Uruguay and Chile in Latin America, and Botswana in Africa – that is, economies in a region not characterised by above-average governance but which have themselves managed to stay relatively clean."

Geopolitical risk

Perhaps even more than corruption, geopolitical risk is a key consideration in investing in EMs.

"With multiple confrontations and conflicts taking place at any one time, the geopolitical context is a crucial risk point in weighing up EM investment decisions," says Lanzeni. "While you may be able to know where there are tensions and unrest and analyse the environment that could lead to conflict, you cannot really predict exactly when something will erupt. The fact that the Arab Spring came as such a surprise to most if not all analysts, is proof of this."

Despite this apparent difficulty in predicting when conflict situations might flare up, there are ways of assessing which countries are most at risk. Risk consultancy Maplecroft publishes an annual 'Political Risk Atlas', ranking countries in terms of the risk and placing them into five categories: extreme risk, high risk, medium risk, low risk, and no data. In its 2014 Atlas, Somalia was ranked the country with the highest political risk, followed by Syria, Afghanistan, Congo, Sudan, Central African Republic, Yemen, Libya, South Sudan and Iraq. All these countries were categorised as at extreme political risk.

In the study, Maplecroft said that since 2010, almost 10% of countries worldwide have seen a significant increase in the level of dynamic political risk, "with foreign investors facing increased risks of political violence, resource nationalism and expropriation."

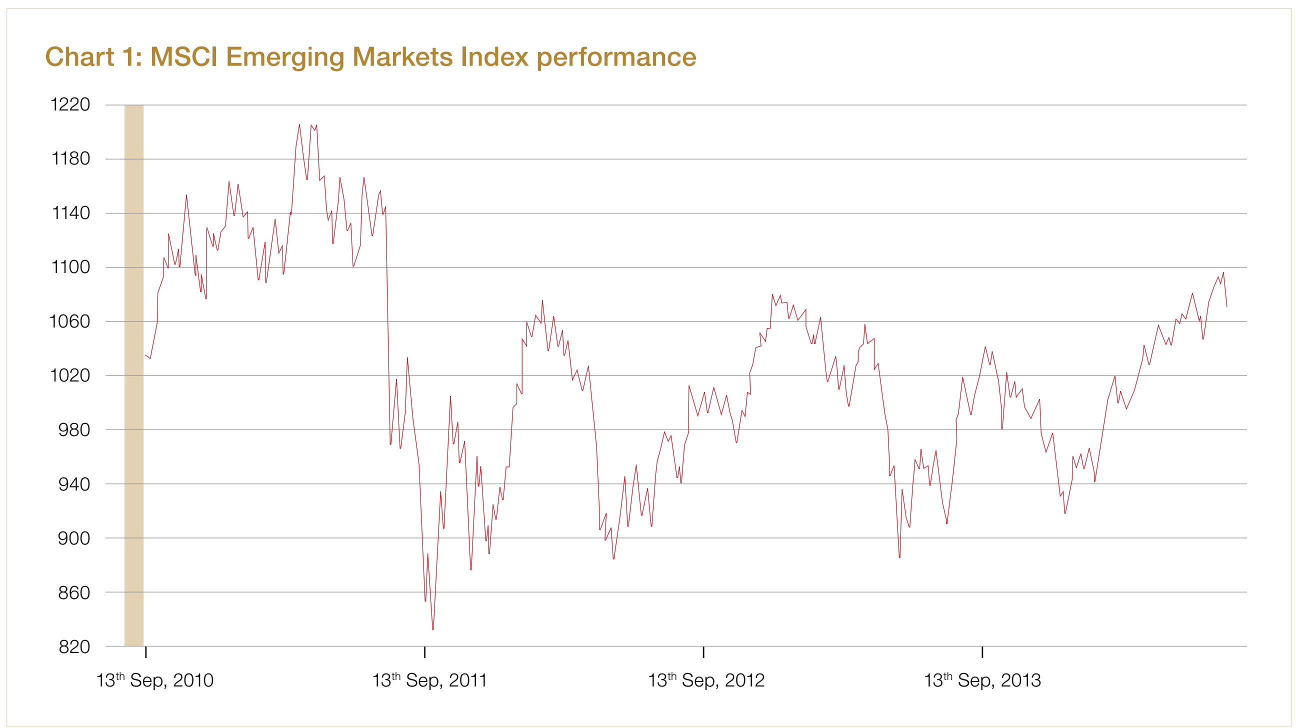
Beyond potential conflict situations, political events can influence the business environment in a country too. The Brazilian general election set for October 2014 is one key date that EM watchers will follow with interest.

Similarly, Argentina has been under the spotlight of late since the country's debt default in July. The economy is not currently an attractive market for foreign investors, with the central bank's foreign currency reserves at their lowest level for eight years, and inflation bordering on 40%.

"The situation in Argentina illustrates the political risk dimension that investors in EMs can be exposed to," says Validus' Lester. "Not only is the currency risk very significant, but the fact that an entire company can be seized from an investor without warning is even more of a danger."

In the short to medium term, it seems the recent rocky patch EMs have experienced, with investors taking capital out to move to developed markets (particularly the US), will continue amid speculation that the Fed could bump up interest rates before long. One defining risk of EMs is that they can be much more prone to swings based purely on market confidence than more developed markets.

However, despite the risks, as long as interest rates in developed economies remain low, and provided that the BRIC countries, particularly Brazil, can get back on track, investors may well see EMs as an asset class to keep an eye on. ■



Source: MSCI

Catching up with credit ratings

Let's be honest. Few treasurers have the time to become experts in the minutiae of the rating agencies' methodologies. But treasurers do require at least general understanding of the basic principles involved. Now with the 'Big Three' ratings agencies promising more transparency around how they reach their decisions, those fundamental principles are evolving. In this feature, we bring treasurers up-to-speed with the latest developments.

For corporates looking to issue debt on the capital markets, an investment-grade credit rating is not entirely essential. But with many institutional investors prohibited from investing in all but the safest credits, having those three A's next to your company's name sure does help.

If you want to make absolutely sure that your company receives the rating it deserves, it helps to have an understanding of how the likes of Moody's, S&P, and Fitch work when scoring the creditworthiness of corporate issuers. Most treasury teams will be familiar with the corporate credit ratings grids (see Chart 1) used by the 'Big Three' ratings agencies, yet their knowledge of the methodologies behind a rating, and the factors that can trigger a change can often be patchy.

Do you, for example, fully understand how M&A activity is treated by the ratings agencies? If a corporate announces an opportunistic acquisition, against a previously declared strategy of organic growth, how will that impact the credit rating? With Fitch's methodology, this kind of event would be excluded from the prior rating, and would "typically generate a rating review based on materiality and impact, depending on the funding mix and cost," according to the agency.

One of the problems with such ambiguities is that they do not tend to breed trust or confidence, two things the agencies have been desperately trying rebuild in recent years.

As we all know, the Big Three agencies came in for robust criticism in the wake of the financial crisis for their ratings of collateralised debt obligations (CDO) – part of a family of instruments Warren Buffett once described as "financial weapons of mass destruction" that were, according to one academic, responsible for $542 billion in write-downs at financial institutions between 2007 and early 2009.

And while many companies continue to attach significant weight to the agencies' judgement post-crisis, others are reluctant to trust them fully. "The ratings agencies are starting to build up credibility again and they have made great strides, but some corporates still look at them with hesitancy," says John Coon, Global Treasury Manager at Dow Corning Corporation. "With counterparty risk analysis, for example, most corporates used to give the agencies free rein to get on with their job, and would rely almost entirely on their outlooks and ratings for that. But now, at least for our own counterparty risk analysis, our reliance on the ratings agencies has gone down. They still play an important role, but we combine their information with a greater proportion of research we have conducted ourselves."

He is not alone in highlighting this pre-crisis over-reliance of corporates on credit ratings. In June 2014 the International Organisation of Securities Commissions IOSCO said "the role of credit rating agencies has come under regulatory scrutiny,

Chart 1: Comparison of Moody's, S&P and Fitch credit ratings

<table>
<tr><th colspan="2">Moody's</th><th colspan="2">S&P</th><th colspan="2">Fitch</th><th rowspan="2">Rating description</th></tr>
<tr><th>Long-term</th><th>Short-term</th><th>Long-term</th><th>Short-term</th><th>Long-term</th><th>Short-term</th></tr>
<tr><td>Aaa</td><td rowspan="6">P-1</td><td>AAA</td><td rowspan="6">A-1</td><td>AAA</td><td rowspan="6">F1</td><td>Prime</td></tr>
<tr><td>Aa1</td><td>AA+</td><td>AA+</td><td rowspan="3">High grade</td></tr>
<tr><td>Aa2</td><td>AA</td><td>AA</td></tr>
<tr><td>Aa3</td><td>AA-</td><td>AA-</td></tr>
<tr><td>A1</td><td>A+</td><td>A+</td><td rowspan="3">Upper medium grade</td></tr>
<tr><td>A2</td><td>A</td><td>A</td></tr>
<tr><td>A3</td><td rowspan="2">P-2</td><td>A-</td><td rowspan="2">A-2</td><td>A-</td><td rowspan="2">F2</td></tr>
<tr><td>Baa1</td><td>BBB+</td><td>BBB+</td><td rowspan="3">Lower medium grade</td></tr>
<tr><td>Baa2</td><td rowspan="2">P-3</td><td>BBB</td><td rowspan="2">A-3</td><td>BBB</td><td rowspan="2">F3</td></tr>
<tr><td>Baa3</td><td>BBB-</td><td>BBB-</td></tr>
<tr><td>Ba1</td><td>Not prime</td><td>BB+</td><td>B</td><td>BB+</td><td>B</td><td>Non-investment grade speculative</td></tr>
</table>

Source: Moody's, S&P and Fitch

mainly as a result of the over-reliance of market participants, including investment managers and institutional investors, on CRA ratings in their assessments of both financial instruments and issuers in the run-up to the 2007-2008 financial crisis." Were the agencies entirely to blame for the corporates that found themselves in hot water during the crisis?

Here it is important to distinguish between corporate credit ratings activity – which has largely performed well for the ratings agencies before, during, and after the crisis – and the mortgage-linked ratings which drew such high-profile censure after the fall of Lehman Brothers.

Indeed, the ratings agencies are quick to point out that there is a distinct segregation between their mortgage-related securities businesses and that of corporate credit ratings. "A fact that is sometimes lost is that the crisis was largely limited to one asset class – US subprime mortgages, which is a very small piece of our business," says Mike Dunning, European Head of Corporates at Fitch Ratings. "Corporate ratings have held up very well since the financial crisis, as evidenced by the default and transition data and reports that we regularly publish."

And while non-financial corporate credit ratings businesses were not implicated in the turmoil in 2007-2009, the agencies have nevertheless taken steps to refine and enhance transparency on this side of their activity post-crisis.

"Since the financial crisis we have taken a number of steps to improve the overall performance of the business. Our criteria function operates independently of our ratings practice, and analysts now rotate so they don't spend an indefinite amount of time on a single account," says Peter Kernan, Managing Director, Criteria Officer, Corporate Ratings EMEA at S&P. "We are now regulated, too."

Regulation is one area in the credit ratings industry that has altered post-crisis, with legislators in Europe and the US putting measures in place aimed at governing the integrity and transparency of the rating process and sustaining confidence in the quality of ratings being produced.

The Securities and Exchange Commission (SEC) in the US put a first round of regulation for ratings agencies into effect in 2007; this was supplemented by the 2010 Dodd-Frank Act, and in August 2014 the SEC adopted further requirements for credit ratings agencies. In Europe, agencies are regulated by European Securities and Markets Authority (ESMA) legislation that came into force in 2010.

Adding value

Beyond the reputational aspect of the ratings agencies, another question a treasurer might ask when it comes to the ratings agencies is, given a large part of their research is based on published historical financial information, where and how exactly do they add value in the ratings process?

"As a cash manager, I don't really care what happened yesterday when I'm looking at credit ratings, I want to know what's likely to happen tomorrow or next month," says Dow Corning's Coon. "Analysing a company's financials definitely holds a lot of weight in predicting future performance, but you need to add further analysis and judgement to get something that's forward-looking."

"Historical information is always helpful, but it is only ever a starting point in our analysis," says William Coley, EMEA Corporate Finance Group Credit Officer at Moody's. "If all ratings were made just on the basis of historical information, you could rate everything by computer. Our analysts provide the additional and important dimension of forward-looking analysis so our ratings have a degree of stability and predictive quality." He adds that Moody's recently introduced a forward-looking grid score to its corporate Credit Opinions that demonstrates how it expects different elements of a company's credit profile to evolve over the next 12 to 18 months in an effort to provide further transparency over their rating rationale.

Issuer understanding

For corporates issuing debt, the treasury department is likely to have considerable interaction with the ratings agencies' analysts. Here the Big Three have several pieces of advice for the treasurer:

- **Watch the sensitivities.** "The key area for treasurers to keep an eye on is the rating sensitivities. The treasurers who manage the credit relationship well are the ones who stay close to that process, who actively engage with the ratings agencies' analysts to keep us informed, to understand themselves what, if anything, it is that's causing us to be concerned," advises Fitch's Dunning.
- **Engage in constant dialogue.** "We are constantly engaged in dialogue with the companies and entities that use our corporate ratings," says S&P's Kernan. "Our strategic goal is to ensure our criteria is very well understood by all parties who use it, and our new criteria make it much easier for corporate treasurers to foresee potential future ratings changes."
- **Be proactive.** "In recent years we have seen that, rather than approaching us on a just-in-time basis, many treasurers from issuing companies now come to us early on in the process to use a range of our products, such as unpublished monitored loan ratings, to their advantage, and to establish a sound relationship with the analyst," notes Coley of Moody's. "Best practice is that ratings committee outcomes should never come as a complete surprise to the issuer."

Mechanisation

As mentioned earlier, the ratings agencies are taking steps to improve the transparency around their methodologies. But might these efforts not dilute the judgement element that goes into a rating, thereby diminishing their value to users? Some in the treasury community evidently see it that way.

For example, in 2013 S&P issued a request for comment to gauge the market's reaction to proposed changes to its revised corporate ratings criteria. The revisions impacted non-financial companies, and included changes to S&P's corporate methodology, ratios and adjustments, country risk, industry risk, group ratings methodology and ratings above the sovereign.

At the time, the ratings agency said the move was intended to improve the transparency and comparability of its ratings. Although the clarifications in the revised criteria were welcomed by some treasurers, others expressed their concern at what they perceived to be the over-formalisation of the new criteria; something they argued has reduced considerably the role of judgement in the corporate ratings process.

L'Association Française des Trésoriers d'Entreprise (AFTE), for instance, while describing the revisions as a "proactive approach to criteria evolution," also went on to claim that the new methodology could lead to too mechanical an approach to credit ratings. "Rating must not become scoring," said the AFTE in an open letter to S&P.

According to S&P's Kernan, this is not the case at all. "We went to great lengths when designing our corporate criteria to make them transparent but also to continue to embed them within our analytical process judgement calls," he says. "There are many areas where our analysts and credit committees are having to make judgement calls."

For example, if a corporate has undergone what S&P describes as a 'major transformational event' such as an M&A or significant recapitalisation, S&P's analysts now have the ability to change the time series used in a rating, giving a reduced weight – or in some cases no weight – to historical information.

"Strategically we will continue to embed this judgement element within the ratings process. We believe we add value in this respect as we have deep, global insight into corporates and their industries, and the ability to make judgement calls in our financial forecasting is clearly very important," he adds.

Fitch's Dunning agrees that this judgement factor is key to the ratings agencies' service. "You have to balance the issue of being visible and adding value to the process, but retaining this element of judgement within credit analysis is absolutely critical," he explains. "This is something we defend very strongly; this judgement call needs to stay with us as it's part of the value that we add as an independent third party with an objective opinion."

New player

And for those who are unsatisfied with the Big Three's corporate ratings, a new player has emerged to offer an alternative, at least in Europe.

Scope Ratings was established in 2011, with its corporate rating business starting up in 2012. It has since begun rating banks and structured finance products, too. Scope intends to offer a local knowledge advantage to Europeans over its US-based competitors of Fitch, Moody's and S&P.

"We rate smaller and midcap companies – but we will also rate larger corporates in the near future," Britta Holt, Executive Director of Scope's Corporate Ratings franchise, tells Treasury Today. "Scope used to be a family-owned business, which has provided us with a natural understanding of smaller and mid-sized companies. Our ratings business is a good option for investors looking for an alternative to the Big Three, who are all headquartered in the US."

So far Berlin-based Scope has rated corporates in Germany, Austria, Spain, France and the UK. "We only rate European corporates. Our criteria are broadly in line with those of the larger players. We provide forward-orientated analysis, focusing on cash flow generation capability," adds Holt. "We don't focus on the sheer size of a company alone in our analysis, but also on its positioning in the market – we concentrate on this aspect much more than the larger ratings agencies."

However, despite the emergence of Scope, as well as regional players like China's Dagong Global, the hegemony of the Big Three appears hard to displace: in 2012 they accounted for around 95% of credit ratings worldwide.

Ratings in the future

It is interesting to note that despite the adjustments being made around methodologies in recent years, the fundamentals of corporate credit ratings remain, for the most part, familiar.

"Over the past five to seven years we have seen mass volatility in the financial markets, but our corporate ratings methodologies have not fundamentally changed, and they should not fundamentally change in future," says Fitch's Dunning. "Companies will be impacted by weaker markets, lower growth, or deflation, but the way we assess them should remain broadly the same."

Moody's Coley agrees that the basics of corporate ratings should not change radically. "Our corporate methodologies are not subject to step change, but rather an evolution as they are typically updated on a three- to four-year basis. The methodologies we have in place for traditional industries such as mining, shipping, manufacturing and retail have been developed over decades so our sector-specific views are not likely to change overnight," he says.

"However, we do adapt to emerging trends – we now have a pay-TV methodology, for instance – and I'm sure we will create new methodologies when and if required to capture new industries that may emerge." So, while fundamental revision of the ratings process is unlikely, ongoing subtle, incremental changes are a possibility.

That could mean, for example, interactive ratings tools that allow companies to experiment with variables and get an on-the-spot estimate of how these could impact their credit rating. "We are working on a navigation tool that can sit on a banker's or treasurer's desktop and allow them to adjust certain financial and operational parameters in an interactive manner to see how these affect the way we rate them," adds Fitch's Dunning. "Technological advancements like this should help further inform discussion between analysts and users, making the ratings process as visible as possible. This is to everybody's advantage."

Treasurers who use corporate credit ratings would also like to see technological advancements in the way ratings information is delivered. "While some of the ratings agencies' client-facing products are very slick, from a cash management perspective we want to reduce the number of URLs and portals we have to use to access the information necessary to do our job," says Dow Corning's Coon. "The next step would be to systematically feed the ratings information I need into the TMS I already have in place. That is a question for the future." ■

Virtual accounts: keeping it real

They say that if an idea seems too good to be true then it probably is. But the concept of virtual accounts appears to be offering a number of major benefits to corporates that few would decline if they knew about them. What are they and how do they work?

Imagine a bank offering that can help rationalise the number of physical accounts held by a company and also allow that company to simplify the management of its accounts. Imagine also if that same solution enabled a business to gain superior visibility over its cash and liquidity and head off accounts receivable (AR) and reconciliation issues at a stroke. And all this without adding layers of complexity or expensive technology.

By most treasurers' standards, it would seem like a rather good idea. And yet, even though such an offering already exists, the virtual account is far from being mainstream.

What is a virtual account?

Along with their associated account 'numbers' (or, perhaps more correctly, 'identifiers'), virtual accounts are provided to a corporate by its banking partner. Essentially each account is a 'subsidiary' or sub-account of the client's own physical account with the bank; they cannot exist outside of that immediate relationship, hence they are virtual. The identifier serves to segregate any funds from any other funds in the same main account and yet is inextricably linked to that account.

The key to a virtual account is thus the virtual account number/identifier. This may be provided to the client by the bank (in which case it will typically be structured like an IBAN) or to the bank by the client. If the client provides the identifier, it will commonly adopt customer identifiers – customer account numbers, for example – drawn from its own system of record such as an ERP or TMS. Either way, it eases subsequent integration of account data into those systems, potentially facilitating the full automation of payments and collections processes, which for in-house banks, payments on behalf of (POBO) and collections on behalf of (COBO) operations, is just perfect. It may also be possible for the client to generate virtual accounts using its bank's online 'self-service' tool.

Regardless of how the accounts and their identifiers are created, each one will be uniquely assigned by the corporate to each of its own customers that it wishes to bring into the structure (in a large business this may be both external and internal). In theory there is no limit to the number of virtual accounts that a corporate may append to one of its physical accounts and it is entirely feasible to establish a multi-level hierarchy of virtual accounts to mirror the structure of its business relationships.

Why go virtual?

Typically, virtual bank accounts will be used to manage the allocation and reconciliation of high-volume, low-value transactions. According to Finnish banking technology vendor, Tieto, they may also be used in a supply chain context "to satisfy reconciliation requirements for supplier remittances and receipts". The vendor says that virtual bank accounts can also be used "where customer pre-funding for an activity is required, such as investments".

In the European market there is a serious driver for the adoption of such a solution right now. As part of the technology preparations for SEPA, many companies have been busy centralising their payments and collections processes. The pressure to re-engineer these processes has inevitably given rise to concerns around receivables, credit and risk processes. This 'need' is propelled further by the desire also to draw on internal liquidity rather than rely on bank funding. Anything that can enhance the mechanisms of payments and collections factories must surely be a welcome source of relief.

In the banking space, RBS has been offering virtual accounts to its corporate clients in Asia since 2011. Development and roll-out has taken place in the region because it is home to a number of jurisdictions where, says Vanessa Manning, EMEA Head of Payments and Cash Management, RBS, "local clearing truncates so much information that customers were unable to easily adopt straight-through reconciliation processes". RBS is not alone in thinking this is a good idea – institutions such as HSBC, Deutsche Bank, UniCredit (see case study below), Allied Irish Bank, Barclays and Bank of America Merrill Lynch (BofAML), as well as providers such as Korea Exchange Bank and Indonesia's Bank Mandiri, all offer virtual accounts in Asia, for example.

Wherever a business may operate, most are focused on accelerating their cash conversion cycle – applying cash faster and improving their reconciliation and DSO (days' sales outstanding), notes Manning. Increased DSO obviously has a negative impact on working capital requirements, just as failure to reconcile remittances efficiently can lead to chasing payment from a customer who has already paid – streamlining the credit control process is vital in establishing an accurate picture of individual client and overall income, not just in being able to extend credit to good payers but in quickly tackling delinquent accounts.

Many businesses are also focused on the consolidation and rationalisation of their bank accounts: virtual accounts can be used to eliminate the need for many physical accounts. This can reduce counterparty risk (especially where smaller local banks are used) and remove associated account management costs. "A virtual account has a far lower impact in terms of the cost, central bank reporting and audit requirements than a physical bank account has," comments Manning. But it is not just the immediate cost that is saved. Fewer accounts can mean increased standardisation and automation of processes which in turn facilitates automatic processing and matching which is faster, more accurate and cheaper than doing it manually.

> Typically, virtual bank accounts will be used to manage the allocation and reconciliation of high volume, low value transactions.

BofAML is currently piloting its virtual account offering with a number of large corporate clients and, says Ad Van der Poel, Co-Head of Product Management, Global Transaction Services, EMEA, for BofAML, businesses are expressing interest in the concept, mostly around receivables reconciliation.

Not just an AR tool

Banks offering virtual accounts are unlikely to let the concept rest without further development. In the context of receivables reconciliation, virtual accounts may be, as Van der Poel says, "just a very granular level of reporting", but he argues that the centralisation of treasury or set up of shared services centres to handle both COBO and POBO really does have mileage.

By opening virtual accounts for each entity within a group and appending sub-level virtual accounts to these, clients of those entities can effectively remit to a central account (whether national, regional or global) using their own unique virtual account identifier. "In this case it is not so much used to identify the payer but more as a tool for visibility and control over what each entity is doing," explains Van der Poel. As a variation on (or even replacement of) the pooling concept, it can facilitate genuine benefits around liquidity management.

In practice

With high-volume, low-value payments being the bread and butter of virtual account deployment, Van der Poel offers an example of how they might be used in this context.

A business may own real estate in three countries, with multiple properties in each country and multiple tenants in each of those properties. That business may have a single bank account in its name, or one for each country. If the tenants of each property pay their rent into the bank account, in some cases it may be difficult for the business to identify where certain payments come from and what they represent. In this example, it could be that the tenant did not complete the payment details correctly or it may be that the banks involved in the process (including the clearing bank which may limit the number of characters permissible in the reference field of a payment instruction) either did not have access to or pass on all the invoice data. Payee error tends to occur more in the consumer space than in the professional accounts payable function but errors do occur nonetheless.

To resolve the problem for the property owner in the example, one physical deposit demand account (DDA) could be established in the owner's name and one virtual account could be created for each country. Below each country level, one virtual account could be set up for each property in each country. Taking this down another level, it would be possible to then create a virtual account for the tenant in each property. This hierarchy of accounts may sound complex but in reality there is only one physical account supporting that structure. In the example, each tenant pays into the account assigned to them, which is connected to the property's account, upwards to the country account and on to the physical account. Payment at the tenant end shows immediately in the physical account.

As another example of how a business might benefit from the adoption of virtual accounts, consider the franchise business model, says Van der Poel. The franchisor is in a central position, supporting its network of franchisees with goods and services for which the latter must at some point be invoiced. If the franchisee is typically paid in cash (as for example a fast food restaurant would be), it will normally have a bilateral agreement with a cash collection service, there being many such agreements across the full franchise territory.

However, the franchisor could make a bilateral agreement with a cash collection agency to collect and deposit into virtual accounts cash from all of its franchisees across a certain territory – each franchisee having its own unique identifier and account linked to the central DDA held by the franchisor. Via the virtual accounts, it could net-off its invoices for goods and services payable by the franchisee, paying out the balance. "If the franchisor takes the idea no further than this, it will still offer savings around the cash collection process, provide it with increased visibility over all funds coming in at a centralised level, and make savings across the whole invoice-to-pay process."

Rules and regulations

"Any centralised receivables programme which would see a company regionally collecting into one account on behalf of other jurisdictions would continue to have the normal tax and legal consequences for 'on behalf of' traffic," says Manning (referring to both COBO and POBO models). Adoption of the model "does not mitigate nor cause any new actions". However, she adds, "the need remains for banks to work with customers to make them aware of transactions that can be done onshore, offshore or on-behalf of, and the considerations around that."

Indeed, says Van der Poel, "it is important to consider that virtual accounts are not yet subject to direct regulation". Although nothing has yet been formalised, industry hearsay suggests that virtual accounts have attracted the regulators' attention around their use as a POBO mechanism (but not COBO). "Because a virtual account doesn't really exist in its own right, this forces an interesting discussion," he comments. "We need to keep an eye on how regulation evolves and on what the opportunities or limitations may be."

Each bank will thus need to undertake "full and proper legal, regulatory and tax analysis" in each country in this respect.

Too good to be true?

As a relatively easy add-on to a normal corporate bank account, the virtual account concept can deliver a raft of efficiencies around account ownership and management. For the treasurer it means being able to centralise cash whilst retaining some segregation and delineation without the increased complexity and cost of running physical accounts.

For the finance function in general it can accelerate collections and release liquidity from a corporate's internal working capital flow by reducing the dependency on information from the payer, their bank or clearing institution. It can also give broader and deeper real-time visibility over physical account data and enhance the credit control process. Still too good to be true? ■

B. Braun's healthy option

Case study

Rainer Stirn

Head of Treasury - Cash Management

Through its SAP-based in-house bank and payments factory, global healthcare market giant, Germany-based B. Braun is able to receive payments files and make payments on behalf of (POBO) transactions for around 100 group entities throughout the Eurozone using SEPA and working with different banking partners. The plan is to include Singapore and the US in the near future and eventually roll this out to most of the group's 200+ entities located in more than 60 countries.

As part of B. Braun's HR function, some locally managed payroll payments are, for a variety of reasons, made in-country, not through its SAP-based payments factory. In such cases it has adopted the virtual account solution provided by UniCredit. "Creating a virtual account is very easy; the bank gives us access to an online portal, we say what we want and that's it; we can start work," explains Rainer Stirn, Head of Treasury – Cash Management for B. Braun.

Currently UniCredit is providing each in-country HR unit with its own IBAN-based virtual account number, aligned with a single 'real' account held by group headquarters. This enables each entity to send its payment files (which could contain several hundred individual payments) via headquarters to the bank which will make the payments (via SEPA), finally debiting the 'real' account.

"The advantage for us is that headquarters receives an electronic bank statement referencing each virtual account transaction. Our SAP system is able to post these items automatically to the correct in-house cash account," notes Stirn. For him, the solution has quickly and easily provided a "perfect loop" for these payments. Although it handles most major currencies, he notes that SEPA has worked extremely well with the virtual concept "with few adjustments required", SAP and the whole infrastructure having already been set up to process these payments.

The next phase of the roll-out of the virtual account solution will enable B. Braun to process incoming payments from customers via its centralised collections on behalf of (COBO) operation. This will use much the same system as for payments but in reverse. Each entity in the group has its own IBAN-based virtual account number linked to its own in-house bank account. This means that when an invoice is paid using the virtual account number, the system will automatically credit the in-house bank account of the relevant entity. The in-house bank is able to send to the group entity that is being paid an electronic in-house bank statement containing all the details to enable it to clear the open item on its own books. "The final goal is to concentrate the outgoing and incoming payments so that group companies only have an account with our in-house bank" says Stirn.

With multiple bank accounts for group companies and a multi-currency cash-pooling structure, B. Braun is working to reduce that complexity and reduce the number of local bank accounts it needs, notably those opened just to handle foreign currency receipts by group entities. Whilst he admits that it might not work everywhere, now that virtual accounts can centralise cash automatically, Stirn views cash pooling as "a product from former times". He believes that centralisation using virtual accounts offers considerable savings in terms of time spent managing bank accounts and that most real accounts and cash-pooling transfers suddenly become unnecessary. It is a cost and efficiency saving that B. Braun fully intends to exploit.

International salt transportation: table salt was both a highly valuable trading commodity and a means of payment back in ancient times.

A comprehensive service offering: *UBS Transaction Banking.*

The service for all companies with financial needs in Switzerland and abroad.

As a strong international financial partner, we offer you reliable infrastructure and leading services tailored to your individual needs.

Some products and services may not be available in all jurisdictions. This information does not apply to, and should not be relied upon by retail clients. United Kingdom: The price and value of investments and income derived from them can go down as well as up. You may not get back the amount you originally invested. Issued by UBS AG.

www.ubs.com/transaction-banking

Names and/or references to third parties in this print advertisement are used with permission. © UBS 2014. All rights reserved.

Transforming treasury: going the extra mile

John Salter
Managing Director, Global Corporate and FI, Global Transaction Banking

John Salter is the Lloyds Bank Global Transaction Banking (GTB) Managing Director for Global Corporate and Financial Institution client sectors. Salter is responsible for all aspects of the GTB relationship across these key segments. Prior to this role Salter held a variety of senior positions at Lloyds Bank and other institutions, managing large international sales teams, relationship management, product management and network management. As a member of the GTB Executive Committee, he is part of the leadership team committed to establishing Lloyds Bank as the leading UK provider of transactional banking services.

As treasurers become more involved in wider business activities, from enterprise risk management to board-level decision-making, regulation is challenging them to rethink the way they approach fundamental treasury tasks and relationships. Meanwhile, technology is enabling greater efficiencies, but also presenting a number of new threats. John Salter, Managing Director, Global Corporate and FI, Global Transaction Banking, Lloyds Bank, discusses five key themes for treasurers to keep firmly on their radar in the months ahead.

Given that HR budgets remain constrained, treasurers must think on their feet to maximise the resources at hand – be that through implementing more cost-effective technology, new cash management structures, or simply by leveraging industry expertise.

Here we examine the key trends that are influencing the way treasurers extract hidden value from the business and deliver added-value to stakeholders.

Working capital philosophy

Despite improving economic conditions, bank regulation – not least Basel III – continues to put increased pressure on the cost and availability of bank finance. As such, 'working capital management' is becoming synonymous with 'cost effective financing'.

In fact, cutting-edge treasury functions are no longer taking working capital for granted or labelling it as a 'bank product'; instead they are looking to establish working capital optimisation strategies that underpin the business and support long-term growth. There are several common tools and methodologies that leading corporations are leveraging to achieve this goal, including centralisation. Centralisation can not only help to streamline operations, but by bringing working capital responsibilities under one roof, it can also help to improve internal alignment around working capital goals.

Companies are also now looking for smarter solutions to help them build sustainable working capital strategies that create value from existing assets. Solutions such as supplier finance, which offer key suppliers an earlier cash flow injection on better-than-normal credit terms while allowing the corporate buyer to reduce the risk of supplier failure, secure longer settlement periods, and gain an element of exclusivity over the key supplier, are growing in popularity. And with recent estimates from consultancy firm REL suggesting that approximately €762 billion remains tied up in excess working capital across Europe, the opportunity is surely too good to miss.

Regulatory challenges and opportunities

This year has seen a raft of regulatory challenges – and changes. Among the most significant for corporate treasurers was the introduction of derivative trade reporting obligations under EMIR on 12th February. For corporates that fall under EMIR's scope, all derivative trades (except FX spot) must now be reported to a regulated trade repository (TR), including trades carried out internally. Many transaction banks are helping corporates with delegated reporting services, while vendors are bringing out new reporting tools for corporates that have chosen to connect directly to a TR. Seeking external help can therefore be a significant time-saver when it comes to reporting compliance.

The largest corporates will now need to prepare for EMIR's mandatory clearing obligations, which are likely to take effect in late 2016 or early 2017. However, some trades entered in to before this date may have to be cleared from the date of implementation – known as 'frontloading'. Corporates should also be aware of derivative market reform regulations in other jurisdictions, such as the Dodd-Frank Act in the US.

Regulation of the financial sector, such as Basel III, is also indirectly affecting companies through the changing availability and pricing of lending, credit, and trade finance, for example. This means that treasurers need to think carefully about the bank lines they currently have available to them, and how these might change. Open dialogue between treasurers and their banking partners can only assist in properly assessing the impact here – and many high profile treasurers are already doing this. For them, taking into account 'wallet share' and ensuring that the corporate/bank relationship adds value for both parties are vital ingredients in ensuring a positive outcome.

Adding to the regulatory complexity are initiatives such as the EU's Bank Recovery and Resolution Directive (BRRD) which aims to deal with the threat of banks which are 'too big to fail'. In the UK, structural reform under the guise of the UK Banking Bill or the Vickers Report, is proposing significant changes to the current banking model through the use of ring-fencing, designed to separate a bank's retail operations from its institutional operations, in order to safeguard retail and SME clients. One of the main challenges for corporates here is that the derivatives offered by the ring-fenced bank (RFB) will be limited.

As these regulatory changes come into effect, corporates are encouraged to have open dialogue with their relationship bank(s) to discuss both the challenges and opportunities that they present.

Cash management efficiency

When it comes to cash management, the ultimate goal remains 100% visibility and control, while simultaneously managing risk and maintaining liquidity. Innovative industry solutions such as SAP's financial services network (FSN) are allowing corporates to communicate with many banks though a single window, for example.

SWIFT is also changing the rules of the game. Having been successfully used by many large-name corporates to achieve improved cash visibility, it is now making its services more accessible to mid-tier corporates through its Alliance Lite 2 offering.

Elsewhere, despite the hurdles the Single Euro Payments Area (SEPA) has presented, a number of companies are starting to leverage the structural changes enabled by SEPA (eg rationalisation of bank accounts) as a catalyst to improve cash management efficiency and visibility. That said, there is still much value to be derived from SEPA and the 1st August 2014 deadline did not mark the end of the migration process. Not only will corporates in non-euro countries have to comply with the SEPA Regulation by 31st October 2016, but many Eurozone companies can still take their SEPA projects further.

SEPA is also driving the use of a number of e-solutions within treasury, which again all add to the clarity of the overall cash picture. Virtual accounts, for example, can significantly improve processing efficiency and allow the real-time capture of transactions.

Tackling cybercrime

Recent research by internet security company McAfee estimates that cybercrime now costs the global economy £266 billion annually. As the guardians of corporate cash, that figure illustrates very clearly why treasurers must join the fight against cybercrime.

But cyber criminals are not necessarily motivated by profits alone. We are witnessing a growing trend towards cyber terrorism – where institutions and companies are being targeted by 'hacktivists' because of their business activities or ethics, not just their coffers or data vaults. What is more, given the constant evolution of technology, cybercrime is becoming increasingly sophisticated and there is no silver bullet.

Nevertheless, the treasurer has a duty of care to protect the company's assets in the face of this evolving threat. To fulfil this duty, treasurers must think beyond their traditional perceptions of cybercrime. While payment fraud remains a significant concern, as does keeping track of the treasury department's access to and storage of data, ensuring that IT can deploy appropriate solutions is also vital. This means dedicating budget to technology – not only to fund new software and systems, but also to allow for the company's critical infrastructure to be tested through simulation, rather like the Waking Shark II exercise which saw the Bank of England co-ordinate a major simulated cyber-attack on the UK's financial sector in November 2013.

> Being a successful treasurer is about more than just hitting targets and making the numbers stack up; it's about adding real value to the company and acting as a strategic business partner. The treasury function can support the growth and operational goals of the company by leveraging the strong banking relationships that it has nurtured.

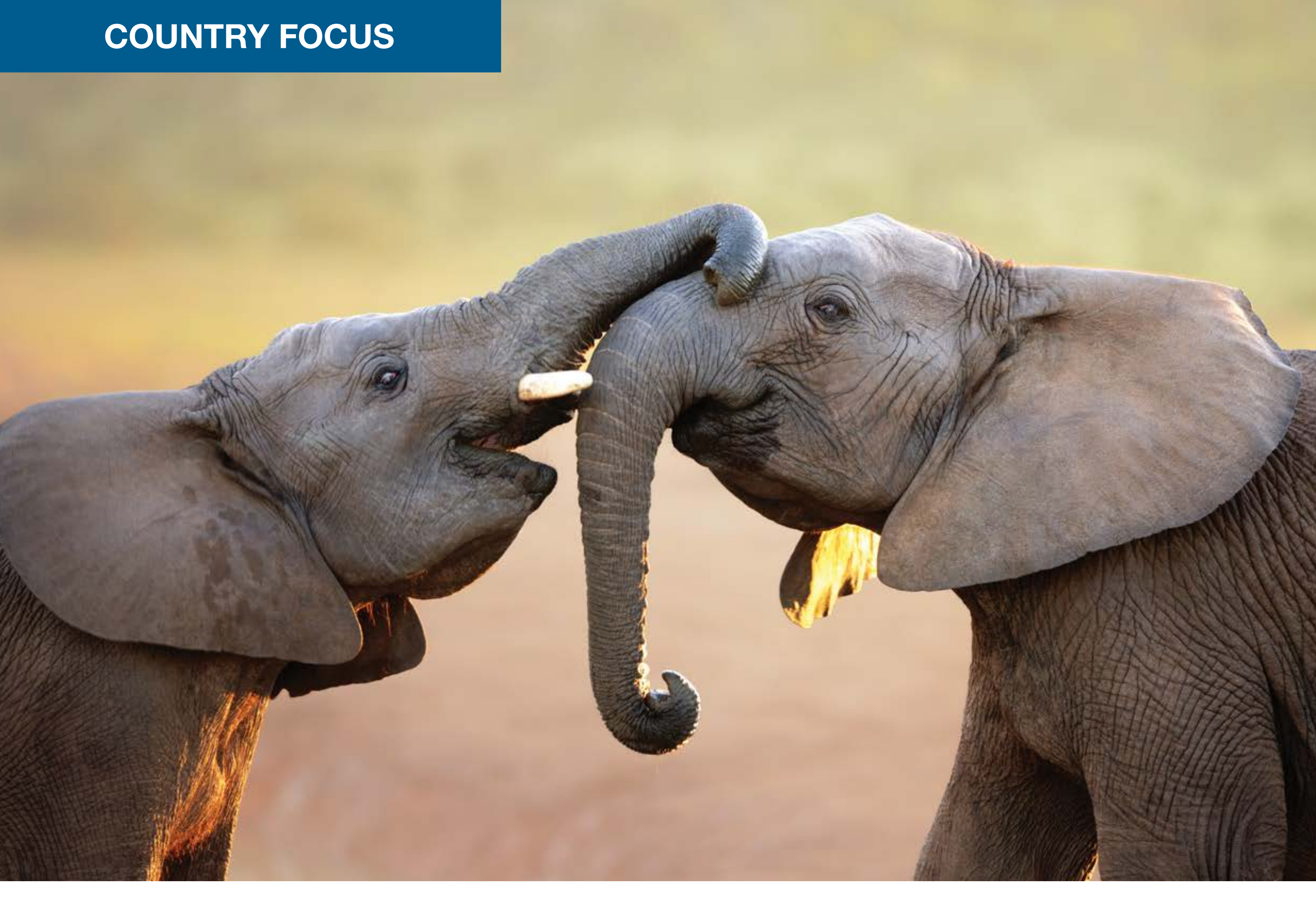
Like the banks, corporates may also wish to consider seeking expert advice from consultants and technology leaders around cybercrime – as well as setting up business units tasked specifically with managing the company's cyber defences. And although a great deal can be done to prevent cybercrime, having a plan in place to deal with a breach if one occurs will be extremely beneficial.

Treasury as a value creator

Being a successful treasurer is about more than just hitting targets and making the numbers stack up; it's about adding real value to the company and acting as a strategic business partner. The treasury function can support the growth and operational goals of the company by leveraging the strong banking relationships that it has nurtured. This entails not only securing affordable access to funding, but also choosing a forward-looking bank that will deliver an efficient cash management infrastructure.

Assisting the company in retaining its competitive edge by assessing the latest treasury technology, or bank innovations, is another facet of the treasurer's developing role in value creation. Similarly, using technology to analyse key metrics that paint a clear picture of the company's health and ability to withstand adverse scenarios, can help treasurers to add value the board by turning what was previously seen as 'data' into genuine information.

Finally, communication skills are becoming a highly valuable attribute in the treasury function. In addition to board-level communication, there should be a constant flow of information, and a sharing of best practices between the treasury function and other internal departments such as legal and accounting, tax, procurement, sales, and credit control to help enable the company to achieve its full growth potential.



Nigeria: the giant of Africa

In terms of its geographical size, population and economy, Nigeria is a force to be reckoned with in Africa. Now the continent's biggest economy, Nigeria has undergone many changes in recent years. Yet there are some fundamental challenges which still remain and need to be overcome before it can fully realise its economic potential. Treasury Today looks at recent economic and infrastructural developments in the country and what they mean for businesses operating in the country.

In April this year Nigeria, already Africa's most populous country, overtook South Africa to become the continent's largest economy. A long overdue rebasing of the Nigerian economy saw industries such as airlines, telecoms and e-commerce included in the country's GDP figures for the first time. The statistical re-shuffle added 85% to the country's GDP overnight, which now totals $510 billion, making Nigeria the 26th largest economy in the world.

Nigeria has come a long way since gaining independence from the United Kingdom in 1960. The initial signs were positive following independence and the country being awarded an 'emerging economy' label. However, political turmoil, which included several military coups and a civil war, and unfavourable economic events, have conspired against the country. Although some impressive growth was recorded during the oil boom of the 1970s, the adverse political climate meant the benefits were not passed down to SMEs, or to the general population, and the growth levels couldn't be sustained. All this led to, at the turn of the century, Nigeria being one of the poorest economies in the world.

Since then, political reform and democratisation, has brought an end to over 30 years of military rule, putting Nigeria back on track to achieve its full economic potential. The country is now regarded to be a lower middle income emerging market. Oil still remains at the heart of the economy, and is the nation's primary export to countries such as the US, India and the Netherlands. Nigeria's main imports are primarily machinery, chemicals, transport equipment and manufactured goods from China, the US and India.

In recent years, the government of Nigeria has looked to move away from its dependence on oil. And the recent rebasing of the economy demonstrates the increasingly diverse nature of

the Nigerian economy as the services sector now accounts for 52% of GDP, and manufacturing rose from 1.9% to 6.8%. At the same time, the oil and gas sector declined relative to GDP, falling from 32.4% to 14.4% after rebasing. Nevertheless, the oil and gas sector still remains the main revenue driver from the Nigerian government.

Due to these developments, and its large, youthful population, the long-term outlook for the Nigerian economy is positive. The nation was famously named as one of the high economic potential MINT (Mexico, Indonesia, Nigeria, and Turkey) countries, a term coined by Fidelity Investments.

To help the country fulfil that potential, the government introduced 'Vision 20:2020' in 2009 – an 11 year economic plan which looks to stimulate economic growth and place the country on a path of sustained socio-economic development. Five years on, although the message from the government is that the plan remains on track, Standard and Poor's has revised its outlook for the country, downgrading from CreditWatch negative to negative, citing political in-fighting and political and institutional risks. The downgrade is a sobering reminder that, despite the positives of recent years, the country still has a number of pressing issues to resolve before it can fully step-up.

Key challenges

One of the key challenges facing Nigeria is poverty. The World Bank earlier this year stated that 33.1% live in poverty, 55.9 million of the 162 million population. However, the Nigerian National Bureau of Statistics estimates that 120 million of the 162 million people in Nigeria, 67% of the population, live in poverty. Whichever the amount, income inequality, political instability and corruption are largely regarded as the key reasons for the poverty levels and the government's anti-poverty programmes are struggling to overcome the challenge.

Elsewhere, despite the political reforms, the political situation in the country still remains fragile, with in-fighting dividing the country's ruling party, the People's Democratic Party. In addition, sectarian violence is commonplace throughout the country and has caught the worldwide media's attention in recent months through the actions of Boko Haram, a militant Islamist movement based in the North East of the country. This type of violence can bring challenges to businesses as some areas of the country are too dangerous to move goods through.

Little surprise, then, that Nigeria is widely regarded as a challenging place to do business. The World Bank ranks the country 147th out of 189 in its Doing Business 2014 survey, citing not only socio-political conditions but also infrastructural challenges. Basic services such as electricity are in short supply – the World Bank ranks the country 185th out of 189 in terms of ease of getting electricity. And when electricity is not an issue, transportation is: take the underdeveloped roads and transportation networks which often create delays in moving goods around the country, for example. This can cause supply chain, forecasting and inventory problems for corporates operating in the country which can significantly increase the cost of doing business, not to mention the effect on a corporate's cash conversion cycle. It is also extremely difficult to register property in Nigeria and a weak rule of law and judiciary in the country mean that companies may be exposed to corruption and political interference.

Yet, despite all the challenges, many companies are thriving and Nigeria remains one of the top three destinations in Africa for foreign direct investment with inflows of $5.6 billion in 2013 according to the United Nations Conference on Trade and Development.

A revamped financial sector

As foreign investment and corporate involvement in Nigeria have increased, the country's financial sector has undergone significant changes following years of underperformance. To modernise and strengthen the sector, the Nigerian government has sought to consolidate the banks, raise the levels of capitalisation required, adopt a risk and rules-based regulatory framework, while also strengthening existing laws. The reforms have had a dramatic effect on the sector which now exists with just over 20 banks compared to over 100 a few years ago. "If we look at the legacy Nigerian banking landscape and compare that to what we have today, it has improved vastly over recent years," says Sam Ocheho, Head, Global Markets, Stanbic IBTC.

The sector is regulated by the Central Bank of Nigeria (CBN) and comprises mainly local banks and a handful of global banks. As is the case in many emerging markets, local banks dominate in the payments and collections space due to their expansive branch network which penetrates the furthest reaches of the country. The global banks on the other hand are primarily focused on the larger scale domestic corporates and international corporates offering more complex outward facing products and connecting these companies to the global financial system. "We find that multinational companies in Nigeria want to use one global bank in the country alongside relationships with one or two local banks," says Segun Adaramola, Head of Treasury and Trade Solutions at Citibank Nigeria. "In doing so, they are able to leverage the international banks for their sophisticated outward looking business while also using a combination of local and international banks for their domestic collections and payments." Corporate funding is widely available to all sectors of the economy and this is offered using an informal tier system. The large international companies will readily have access to the cheapest funding – in some cases it has been reported that these companies obtain cheaper funding than the government. The range of products which banks are offering to corporates is also increasing, especially as the nature of Nigerian businesses becomes more global and more complex products are called for.

Foreign exchange rules

The banks also play a key role in assisting corporates to move capital in and out of the country. In order to keep the managed exchange rate stable, the CBN has regulated the foreign exchange market extensively and there are a number of rules corporates must follow to import and remit funds. "If a company is looking to bring funds into the country, it must seek a certificate of capital importation," says David Adepoju, Head of Global Markets at Standard Chartered. "Only with this document will it be able to then convert the principle investment and capital gains from Naira to USD and repatriate."

To make the process of both importing and exporting funds easier for corporates the CBN has empowered banks to grant a certificate of capital importation based on a set of guidelines, if these guidelines are not met then the corporate will need to seek central bank approval.

Additional documentation is also required to remove profits from the country. "A corporate is required to demonstrate the transaction history of the investment in order to repatriate the full amount," says Adepoju. "The best way to do this is by

leveraging a bank or custodian, because although the process isn't necessary complex, a bank is well placed to help guide corporates through this area."

A further headache for corporates looking to repatriate profits from Nigeria is that the country can sometimes lack dollar liquidity, despite petrodollars and remittances from abroad bringing $63.17 billion dollars into the country in 2013. The level of liquidity depends on what the CBN is doing at the time. But at times that it is limited, it can make taking money out fairly difficult for corporates.

Recognising the increasing importance of China to the Nigerian economy, trade between the two countries hit almost $13 billion in 2013, and the CNB announced plans to convert an additional 5% of its dollar reserves into yuan. In an interview with Bloomberg, CBN Deputy Governor Kingsley Moghalu, stated that "It was clear to us that the future of international economics and trade will shift in large part to business with and by China. Ultimately, the renminbi is likely to become a global convertible currency."

A growing hedging market

Hedging products are widely available for corporates in Nigeria, yet despite increasing global trade, they are still rarely used. "Very few companies have a hedging strategy in place," says Ocheho. "For me this is either due to lack of capacity, prohibitive costs; lack of education or parent companies policies against hedging by multi-national companies across some jurisdictions. Companies are therefore leaving themselves open to exchange rate volatility as they develop into the global market – and also interest rate volatility."

The primary hedging products which are available to corporates are vanilla forwards and swaps. But in a bid to increase the popularity of the derivatives market in Nigeria, the CBN has been hard at work. "The market in conjunction with CBN has developed a new OTC exchange (FMDQ OTC), a self-regulatory body for OTC transactions in Nigeria," says Ocheho. "The company is expected to increase the level of transparency in our financial market and also build a credible platform where more complex derivatives trades can be done." Standard Chartered's Adepoju paints a similar picture: "As the amount of capital and finance which the country's banks and corporates have expands, and the duration of banking books and corporate loans becomes longer, there will be much more activity around hedging and the market will start developing more quickly. This is something which we have already started to see in the oil and gas sector, for example."

The end of cash

A report released by MasterCard earlier this year showed that Nigeria spends $5.1 billion a year printing and handling cash, approximately 1% of its annual GDP. In order to reduce costs and mitigate the risks of such a heavily cash-based economy, the CNB introduced a cash lite policy in 2012 which looks to reduce the circulation of cash and move to electronic transactions. As part of the 20:2020 project, this began in Lagos and has since spread further across the country.

The main elements of this policy include a cash handling charge on daily cash withdrawals that exceed 500,000 naira for individuals and three million naira for corporates. "Two or three years ago, cash in Nigeria accounted for about 60% to 70% of transaction volume. As of today this figure has reduced to around 40% or less" says Citi's Segun Adaramola. This shows the impact of the cash lite initiative and the growing importance of electronic payments in the country." To facilitate the project, there has been an overhaul of the country's payments and settlements systems. "The payments and settlements system in the country is now excellent," says Standard Chartered's Adepoju, "and this is positive for all corporates in the country." The improvements have meant that corporates are able to make payments using the improved Real Time Gross Settlement (RTGS) Service within an hour and sometimes in less than ten seconds, depending on the value. "There has been a lot of work to ensure that this works smoothly," adds Adepoju. "Also the CBN has put in place a process whereby cheque clearing has been reduced to one day, again helping corporate operations in the country."

Having only been implemented across the majority of the country earlier this year, the jury is still out on how the project will work in the less developed cities and regions. Nevertheless, Adepoju doesn't believe that there will be any significant challenges for corporates and that it is overall a positive development. "Most corporates would prefer to use electronic transfers because cash is expensive to handle. Using electronic platforms also allows corporates to have better real-time view of cash flows."

The technological infrastructure, however, may hinder the development of the cashless policy. Despite significant improvements, broadband penetration across the country is low with an adoption rate of around 15% – the global average is 35%. This may prevent consumers and SMEs from readily adopting electronic payments, meaning that corporates will still need to handle a large proportion of cash.

Cash management

When it comes to investing excess cash, short-term investment instruments in the market are also vanilla – with bank deposits, bankers' acceptance and treasury bills being the most commonly used. Money market funds (MMFs) are available in Nigeria from the leading domestic banks and government treasury bills are often used by sophisticated corporates in the country.

It is expected that as further economic development attracts more international corporates to the country, the sophistication of cash management products will increase. "As the demand creates more financing to be required by corporates then more complexity will enter the treasury landscape in order to manage the additional risk. We expect to see many exciting developments in the coming years" says Adepoju.

A developing market

In short, Nigeria is a country with giant potential and while on the whole the future looks bright, there are many challenges to overcome in the short term. It is predicted that the upcoming elections in 2015 will run smoothly – and after that, further improvements in political and social stability can be expected. Moreover, as Nigeria continues to improve its infrastructure and business landscape, the cost of operating in the country should decrease. This should drive more foreign investment into the country, which will generate greater opportunities for the young population. Organic growth such as this will help Nigeria to maintain its leading status in Africa, while also moving towards its global aspirations. ■

A closer look at tri-party repos

In an environment where banks continue to feel the impact of regulation, collateralised products open up a new world of opportunities for investors. Tri-party repos, for example, can offer investors both sustained revenues and lower risk – a genuine breath of fresh air for corporate treasurers in today's low-yield environment.

Corporate treasurers could be forgiven for viewing tri-party repos as a complicated type of transaction. The reality, however, is not nearly as complex as some might think. Indeed, tri-party repos are one of the simpler forms of secured investment: they are essentially bank deposits secured by independently held and managed assets.

And in the current economic environment, that security could not be more welcome. Several high-profile bank failures in recent years have highlighted that unsecured bank deposits are not necessarily as safe as they were previously considered. Yet some corporates have more cash on their balance sheets than ever before – which presents them with somewhat of a dilemma.

Increasingly, corporates are thinking outside their traditional investment boxes and as a result, tri-party repos are falling into favour. A tri-party repo offers corporate investors the advantage of collateral (in the form of securities) in return for depositing cash for the duration of the transaction.

"It allows corporates to either diversify their counterparty network or lend more cash with their house banks if unsecured lines are already fully utilised", says Pascal Morosini, Executive Director, Head of Global Securities Financing Sales and Relationship Management at Clearstream. "But the biggest and undisputable advantage is that tri-party repo is much more secure than cash deposits."

Driving the market

One of the key drivers of the growth in the tri-party repo market is regulation. For large corporates who have obligations under the European Market Infrastructure Regulation (EMIR) or Dodd-Frank to post collateral for OTC derivative transactions with central counterparties, tri-party repo offers a significant advantage over alternative products. "The collateral corporates hold against cash can be sold immediately should a counterparty default. This collateral can also be used to cover derivative liabilities that corporates have with their prime brokers and clearing members," explains Morosini.

For this reason, tri-party repo is increasingly considered an alternative to money market funds (MMFs) for corporates with cash to invest in securities. Additional regulation in the MMF space is also causing corporate investors to turn towards tri-party repos.

Against the backdrop of regulatory pressure on investors, tri-party repo presents an opportunity for corporates, who to date have largely invested their cash on a unsecured basis, to invest in collateral-backed deposits.

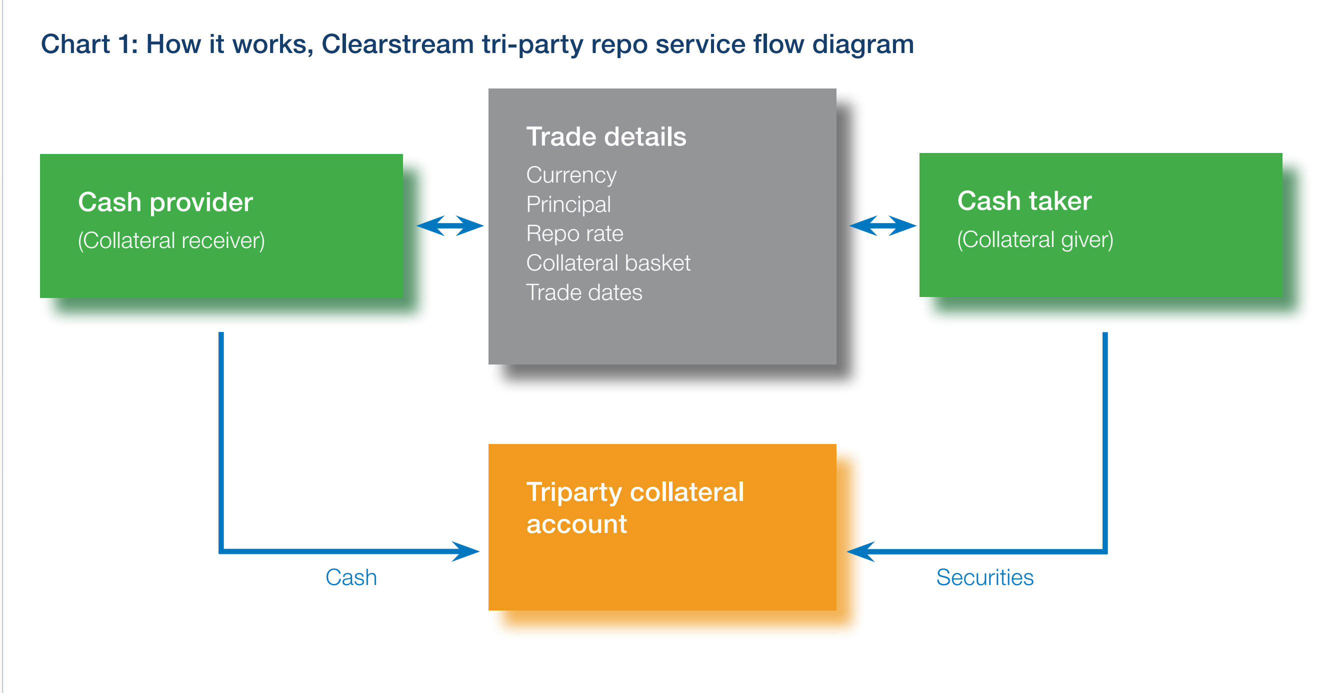
"The low-yield environment, which continues to put a strain on investors, is another reason why now may be a good time for corporates to move into the tri-party repo market. Subject to the type of collateral investors are willing to receive in return for their cash, the yield on tri-party repos can even sometimes beat what they are earning on their current investments," notes Morosini.

Role of the tri-party agent

Clearstream, a leader in the tri-party repo market, acts as collateral agent and securities depository (ICSD). In its custodian role it holds accounts for banks and global custodians, who in turn hold securities on behalf of their clients. More than €12 trillion of deposits are held within Clearstream by around 2,500 customers around the world. In its tri-party collateral agent role, Clearstream manages collateral worth more than €650 billion for more than 550 customers.

"Clearstream acts as a neutral collateral agent, handling all the administration related to the transfer of collateral from one counterparty to another," says Morosini. "We value and allocate the collateral, monitor and process substitutions, execute margin calls, issue reporting and maintain and cross-check the eligibility criteria. In essence, our role is to ensure that sufficient eligible securities are transferred to cover any given exposure at any moment in time."

Chart 1: How it works, Clearstream tri-party repo service flow diagram



The company's role as tri-party agent is an important risk mitigation factor, as Clearstream is not directly part of the transaction. This neutrality guarantees – for both parties in a transaction – that should one default, the collateral will remain segregated and be immediately available for resale.

In addition, Clearstream's tri-party repo service offers a number of unique features. The principal trading relationship remains between the counterparties, and only one signature of the Collateral Management Service Agreement (CMSA) with Clearstream Banking as the agent is required. Collateral profiles (either customised or designed according to industry standards) are predefined within the CMSA appendix, making it very easy and straightforward to sign up for the service.

Furthermore, the tri-party repo service presents distinct advantages to both the givers and receivers of collateral. Collateral givers can finance a broader basket of assets, tap into new sources of financing, use automatic asset allocation and unlimited substitutions, and be assured of optimal collateral allocation across products and locations. Receivers of collateral benefit from security of holding, an optimised balance sheet, low maintenance costs and full reuse of the collateral received.

Elsewhere, the outsourcing of back office operations to Clearstream provides corporates with access to a wide range of counterparties across the world. Clearstream clients have full control over their asset portfolio and benefit from efficient use of their cash and securities as well as from risk management solutions tailored to their individual needs. The solution is a flexible money market instrument at the heart of Clearstream's Global Liquidity Hub which can form an integral part of a corporate's wider liquidity strategy.

Clearstream offers a full suite of products under the Global Liquidity Hub, ranging from securities lending and borrowing to the posting of initial margin to central counterparties for cleared OTC derivative trades. The growing desire of corporates for greater security of the money they deposit with banking partners is reflected in the growth of the Clearstream platform, which now has more than 30 corporate users, with a combined $25 billion in cash.

In practice

For a cash provider using Clearstream, once a tri-party repo deal is concluded, the user instructs its back office to pay the cash to its Clearstream account via its cash correspondent bank. Once this has cleared, Clearstream arranges the simultaneous exchange of the cash on the account for the securities from the counterparty. A core feature of the Clearstream platform is its delivery versus payment (DVP) functionality, which ensures that cash is not paid to the counterparty until the securities have been received, meaning the investor is never exposed.

Users must also inform Clearstream of the transaction with the counterparty; this can be carried out via various channels, including the 360T platform, the Bloomberg Professional service, or Clearstream's own CmaX online communications portal. "Once you have deposited the cash in your Clearstream account and informed us of the transaction, you do not need to handle the collateral side of the transaction," says Morosini. "Clearstream handles all the administration of the transaction, and the investor can remain passive until the transaction is automatically unwound."

What's in it for corporate treasurers?

Tri-party repo was initially created as a means for broker-dealers to maximise the use of small asset positions left in their accounts. Today it has expanded to cater to the needs of the larger corporate world. Though initially conceived as an inter-bank product, Clearstream's platform is bringing tri-party repo to a much broader market. "Clearstream is opening the door for corporates to the tri-party repo market," says Morosini. "We are facilitating and streamlining access to our state-of-the-art Global Liquidity Hub with our simplified legal agreements. Our goal is to industrialise and commoditise this product and offer it to a much wider audience so they too can reap the benefits."

Indeed, greater numbers of corporate treasurers are starting to see the benefits of sustained revenues with lower risk that tri-party repo can offer.

In short the benefits could be summarised as follows:

- Access to a broader range of counterparties, thus diversifying risk and creating yield enhancement opportunities.
- Security: cash loans are secured by collateral in the form of securities.
- Simplicity: trades are negotiated like cash deposits.
- Outsource back office workload: all the administration regarding the management of securities is done by Clearstream
- Simplified legal documentation for instant access to a large number of counterparties.

Evolution and innovation

But what makes Clearstream's offering stand out? For starters, Clearstream's tri-party repo product has matured with the market, meaning that since its launch in Europe in 1992, the service has become more flexible through the implementation of a streamlined signatory process. Users of the service have also benefited from the ability to re-use securities within the system, a feature that was put in place in 2006.

The company's collateral management exchange engine (CmaX) has also been developed as a result of its longstanding industry experience and close market consultation.

Building on its core tri-party repo offering, Clearstream launched its GC Pooling product in 2005 in collaboration with Eurex Clearing AG, the central clearer of the Deutsche Börse Group. "This is essentially a tri-party repo transacted through a central counterparty with full counterparty anonymity. This product, which has on average €180 billion of outstanding, dramatically lowers risk to counterparties for corporates. It is currently unrivalled in the market and is now available for corporates," Morosini explains.

In addition to these innovative products, Clearstream's principal lending product ASLplus was launched in 2006. Through this service, Clearstream borrows securities (mainly high-quality assets such as government bonds) from its custody clients and re-lends them in its own name under a principal structure (as opposed to an agency structure). ASLplus, which is the market leader in terms of German government bond distribution, has around €50 billion outstanding.

A principal agreement is required to trade repos. This could be a Global Master Repurchase Agreement (GMRA), a document traditionally used for bilateral interbank repo trading which is negotiated with each counterparty individually. Some corporate treasurers have been deterred from trading repo as the negotiation process can be cumbersome and numerous provisions apply solely to bilateral repo, and are hence not relevant for those wishing to use tri-party repo.

Clearstream has sought to simplify the process by designing a standardised tri-party-only principal agreement, the Clearstream Repurchase Conditions (CRCs). Like the CMSA, this agreement is multilateral and only needs to be signed once with the agent. Counterparties do the same and the relationship is formed by acceptance of the collateral receiver's eligibility criteria. The combination of the CMSA and CRCs effectively gives corporate treasurers membership to a club within which they can trade with other members without having to sign further agreements. The standardised nature of this setup saves both time and legal costs. This innovation alone can speed up the process for accessing tri-party repo counterparties by up to 12 months for corporates – particularly small and medium-sized companies.

Beyond innovation, Clearstream also prides itself on the level of service it offers its customers and the advanced technological portal through which this is provided.

And as more corporates start to appreciate the potential benefits of tri-party repo, these unique features, believes Morosini, will see Clearstream's market share continue to grow. After all, Clearstream's tri-party repo service offers the advantages of being secure and sophisticated, while at the same time being simple and transparent for corporates to set up.

Pascal Morosini is Executive Director, Global Head of GSF Sales and Relationship Management, at Clearstream.

Pascal joined what was then Cedel Group in 1994 to work in collateral valuation operations. In 1997, he moved to triparty repo operations, and two years later he joined Clearstream Banking's Customer Relations Department as a Global Securities Financing sales specialist. He is now responsible for sales and relationship management for all GSF products worldwide.

Pascal holds a Diploma in Banking Management from the "Centre Universitaire de Luxembourg" and has also participated in the Clearstream Banking Global Markets training programme.

Clearstream

Clearstream is part of the Deutsche Börse Group and provides post-trade services to financial and corporate customers in more than 100 countries with access to 54 markets.

Our tri-party repo services through our Global Liquidity Hub provide corporate treasurers with a safe, flexible, collateralised money market product with innovative options including a unique 'one time' master repurchase agreement (CRCs) and end-to-end integration with vendors such as 360T.

With access to trade reporting services via REGIS-TR and OTC derivative clearing via Eurex, the Deutsche Börse Group offers a 'one-stop-shop' for all your treasury activities.

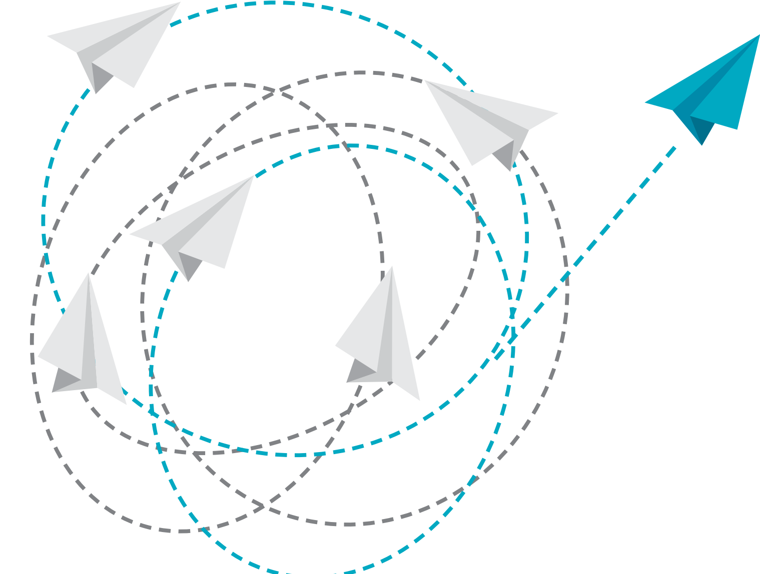
www.clearstream.com

Clearstream
Global Liquidity Hub
We make finance flow

Are you looking for safe and efficient cash investments?

Discover our triparty repo service and benefit from collateralised deposits while maximising your cash returns.

gsf@clearstream.com



clearstream | DEUTSCHE BÖRSE GROUP

Keep talking

Ingmar Bergmann
Corporate Treasurer and Head of Corporate Finance, NSI N.V.

nsi

Ingmar Bergmann is driven by a need to raise the profile and understanding of treasury. With his former chairmanship of the Dutch ACT and voluntary treasury work at a Premier League volleyball team, an innovative urban agriculture scheme and a popular local Judo club, he is certainly putting the profession on the map. How does his broad view of the role – and an obvious delight in working with people – influence his work at one of the Netherlands' most active commercial real-estate firms?

NSI N.V. is a publicly listed real estate company headquartered in Hoofddorp in the Netherlands (next to Schiphol Airport). Its mission is to invest in offices and retail space in the Netherlands in "attractive, high-quality locations" and in offices and logistics real estate in Belgium. The company, which is listed on the Amsterdam Stock Exchange, is an active landlord and manager of its own real estate portfolio with invested assets of around €1.7 billion.

What do a Judo club, an urban agriculture programme, a Dutch Premiership volleyball team and a commercial property rentals group all have in common? On the surface, not a lot it would seem. But for one individual, Ingmar Bergmann, the Corporate Treasurer and Head of Corporate Finance at Dutch real estate firm, NSI, the answer is easy; they all need treasury and organisational skills and for that task he is happy to oblige.

"I'm interested in working with different types of people in different environments and putting my work experience to good use in the community," he explains. The seemingly random collection of bodies that he currently divides his time between on a voluntary basis are in fact a reflection of his own and his family's interests. But in each case he just happened to be the right man, with the right skills, in the right place, at

the right time. The roles found him, rather than the other way round, but he is nonetheless committed to helping each organisation take their financial status to the next level, "to make sure they can carry on their activities in the long term".

Bergmann has good reason to help out where he can, being driven by the strong belief that he has personally benefitted from community resources that enabled him, through the education system for example, to achieve his own professional goals. "I feel that society is more than just family, friends and professional life; everybody has their own capacity, whether materially or non-materially, to help in some way; I do it this way." In sharing the interests and being connected with these various organisations, he adds that it is also "a lot of fun to do".

The experience that other treasurers could gain from volunteering their skills will of course depend on the environment in which they choose to work. Bergmann believes it would at the very least open an individual's eyes to a different side of society, but it could also broaden their professional experience by working with many different people. New skills can be developed too, he notes. In a commercial environment, especially as a senior executive, it may be relatively easy to make a decision. In the voluntary sector, he notes that stronger arguments are often needed to bring together many more people from different backgrounds, each perhaps harbouring different agendas, to define a point on the horizon and then to work together with all these people to make sure everyone is willingly going in the same direction. "It can be seen as a challenge but I see it as an opportunity; it gives me a lot of satisfaction."

From intern to chairman

Having studied business administration at the Rotterdam School of Management, Erasmus University, Bergmann's career kicked off with an internship at an investment bank in the Netherlands, the aim being to eventually become an investment analyst. During his internship he came across an advertisement asking for a cash manager at TNO, the Dutch institution for applied scientific research. "At that time I didn't really have a clue what cash management was but the job description sounded interesting," he recalls. Throwing caution to the wind, he applied, was offered the job, and thus started his long and winding journey into treasury. "On the way, I have had many opportunities to learn more and I now have a rather broad base of experiences to call upon. That is what gives me energy; if I only had one specific responsibility for a lifetime of work it would be too boring for me."

The degree of experience that Bergmann has accumulated over the years is impressive. With two cash manager positions (TNO was followed by an EMEA posting at Eastman Chemical) leading into early corporate treasurer roles and a period as a treasury consultant, he soon became a board member and eventually chairman of the Dutch Association of Corporate Treasurers. With Group Treasurer responsibilities at Dutch utility business, Eneco Energie and then as Director of Corporate Treasury at cabling firm, Draka Holding, a more strategic focus was called upon, requiring closer partnership with other senior executives from a range of disciplines, and the Board. This is an aspect of the job that Bergmann clearly revels in and one which was about to become dramatically more important.

"Up to the point just before the financial crisis, treasury for a lot of my colleagues was seen as a niche function that worked in isolation," Bergmann comments. "They were seen as doing some kind of 'hocus pocus' with bank relationships and then spending a lot of time 'out of office'." But as the worst of it unfolded, the voice of treasury needed to be heard loud and clear, not only by CFOs but also by other departments and the boardroom. It was, he notes, quite noticeable how the more communicative treasurers had started to embed their work deeper into the fabric of corporate life. "Some are better at it than others of course but if there is, for example, an investment issue or an acquisition, the other stakeholders invited into the treasury fold will not only ensure that treasury knows what is going on but they also genuinely appreciate treasury input on how a project can be improved and de-risked."

The voice of treasury

External communication is important for treasurers too and Bergmann is a firm believer that the wider community of treasurers can help each other to do a better job. Certain aspects of the role are naturally bound by the rules of competition; he is not advocating passing on 'trade secrets'. But he argues that some facets of the job – such as the administration of a SEPA project – are not necessarily in the realm of secrecy. Here, treasurers can often help each other by openly discussing project implementations, the pitfalls, the best expert contacts and so on. "The voice of treasury is definitely being heard and now it's time to make sure within the inner circle of treasurers that we maintain the clarity of our voice so that people keep listening."

The cornerstones of promoting the values (and value) of the treasury function are the Associations of Corporate Treasurers that exist in many countries. As a former chairman of the Dutch ACT (he handed over reins in June this year after five years in this position), and a member of the pan-European EACT, Bergmann notes that it is only a relatively recent event for the voice of treasury to be heard with any real interest in the discussions around setting international regulations such as those around IFRS and EMIR. "Corporates, together with the EACT, have been able to raise their voices and show these bodies, especially the European Union, that they should listen to the 'voice of the real economy'," states Bergmann. "Treasurers are willing to help work towards well-balanced regulation."

Being able to form constructive relationships in this way is vital for the success of treasury as a function. In this respect, leadership skills – and the vision to know where to take people and processes – are an essential part of Bergmann's armoury in his day-to-day role. He accepts that there are many people in treasury who just wish to focus on a specific aspect, to become a specialist, but he loves to work with other disciplines, to communicate and to learn their views and try to combine them with his own treasury perspective. "If you want to take treasury to a higher level then you definitely have to communicate and open up to others."

Managing the crisis

The banking crisis and the subsequent rush to impose new regulations on the industry saw many international financial institutions retrench their positions. "In the Netherlands many non-domestic banks moved back to their home markets and out of the Netherlands, having reassessed their risk profiles," notes Bergmann. This was also the case in the market in which his current employer, NSI, is active: "Suddenly real estate was not a top priority for them. When I started with NSI in 2013 we had a financing structure that relied mainly on Dutch banks, but as their

number and size had decreased rapidly over the previous few years for a real estate firm it limited our funding and refinancing."

A new more stable financing structure for the longer term was sought by the firm; this was Bergmann's priority upon arrival. By working closely with other functions within NSI, particularly the Group Controller's office and the commercial real estate teams, it was possible to collate and provide the vast quantity of information that the banks' credit committees were asking for under the new regulatory regime. With a CFO that Bergmann cites as "a master of strategy and negotiation" at the helm, the combination of good teamwork inside an open and transparent business structure and the capacity to leverage long-term banking relationships, helped NSI through the worst of it. "It really worked out well for us," he recalls adding that NSI was able to put in place €400m of refinancing in 2013 and, as part of a successful recapitalisation programme, also issue €300m in equity.

Although international banks are starting to return to the Dutch market, the lesson had been learnt that relying wholly on banks for funding "is too much of a risk". As part of NSI's restructuring programme it was agreed that 2014 should be the year it started work on a more sustainable funding structure. It will still focus on long-term bank relationships for up to 50% of its funding but the remainder will come from alternative funding.

'Alternative funding' is a very broad description that, in Bergmann's definition, includes the German Schuldschein market, retail bonds (most likely in the more developed Belgian market) and private placements. He is no stranger to the latter, having arranged the largest ever non-USD private placement whilst at Eneco Energie; this is clearly now a strong contender for NSI. Bond issuance however is not directly on the agenda, Bergmann arguing that whilst it may solve refinancing risk "it then creates a maturity risk so in a few years' time you have to refinance again".

The way forward

With NSI's funding stabilising as the refinancing plan runs its course, Bergmann's intention is to start honing treasury operations. The company now runs a centralised treasury operation whereas before his arrival it had relied on the Group Controller and CFO to execute related tasks. Although he describes current treasury processes as "relatively simple" (it only has domestic payment transactions and most contracts are fixed, for example) Bergmann is very much aware of the need to accurately forecast cash positions – this process is scheduled to come under the spotlight first. "All plans, projections and business cases do give a view of what the future might bring, but at the end of the day, it is all about cash," he states. "As I always have as a footer in my email 'profit is for science, cash is for real'."

Bringing this project to fruition will once more be a co-operative affair, treasury working closely with the Controller's office, the operational real estate teams and other stakeholders. Life is made a little easier because the whole company is connected through the Yardi ERP system (a specialist real estate solution) so that whilst everyone can work on data as they wish, even in spreadsheets, changes are updated immediately and are circulated by a logical workflow system. This means everyone involved is working from the 'same version of the truth'.

As a result of the funding programme, NSI now finds itself in a position to invest in new opportunities. Teams within the business are working on a new business strategy for the coming years which will require investment; of course, treasury is now much more involved in the early stages of such plans. This appeals to Bergmann's sense of adventure: the new strategy, from his perspective, is more than just about funding; it will involve project management and the need to work alongside people with different skills and interests, "jointly building and improving the company".

But then taking on different responsibilities is all par for the treasury course for Bergmann. During his tenure as chairman of the Dutch ACT he says there was a lot of discussion amongst members about the future of treasury and whether it should remain a pure discipline or encompass others. He comments that where in the past treasury was seen as a niche activity, sitting aloft in an ivory tower, it is increasingly needed to work alongside other business functions. "So if we continue explaining what we do and continue adding value to our organisations and operations, as treasurers we will see the types of responsibilities we have increasing."

With the likes of insurance, pension fund management and even IT being subsumed by treasury, it seems like an ideal base for anyone starting out on a career in business. Bergmann advises all prospective and junior treasury staff on this route to keep their eyes wide open and to maintain a broad horizon. "Don't specialise too early on in your career; you need to understand the business but don't see that as your end goal," he says. "Try to move responsibilities within your company from time to time. Don't try to sit in the same chair for more than a couple of years; it's good to move around, even to other departments of the company, because it helps you to learn about different disciplines and to gain different working experiences. After a few years you will know what direction you want to go in." Bergmann is naturally a keen advocate of giving something back to the community by offering valuable treasury and business acumen to those organisations that need it. The personal enrichment, he feels, is more than sufficient payback.

A life in film

Of course, no article about Ingmar Bergmann would be complete without mentioning his famous namesake. The renowned (and deceased) Swedish director of film, television and theatre may have one less 'n' at the end of his surname, but the similarity has nonetheless been the cause of some merriment over the years for his treasury counterpart. "The shared name has not always been a good thing; back in high school whenever there was trouble it was me that they always remembered. But I'd say that since then it has definitely become a benefit. When I was applying for jobs after university it was always a good way to break the ice – and people remembered me. Now it's often a great starting point for conversations."

Whilst Bergmann the treasurer has never harboured any desire to enter the film business, he says he always intended to seek out an environment that presented complex issues and where he could work with different disciplines. "I want an active, high-pressure environment where I can add value – and that is what I see in treasury." Maybe someone should make a film about it. ■

Supplier finance: coming of age

Successful supplier finance programmes deliver tangible benefits to buyers and their suppliers while also helping to create more stable supply chains. In this Product Profile, Richard Hite, Vice President, Supplier Finance and Simon Enticknap, Director, Trade and Working Capital at Barclays, examine the reasons why corporates should consider supplier finance and what needs to be taken into account when deciding to progress with this strategy.

Companies continue to face significant economic and competitive pressures and, as a result, are increasingly focused on cash generation. Buying organisations are also increasingly aware of supplier risk and the reliance they have on their suppliers. What is more, procurement often represents the largest spend within a company and many companies believe there is value that may be extracted. This may come from improved efficiencies as well as from reducing the amount of capital tied up in working capital.

As such, most companies have working capital initiatives and targets. These are usually focused on improving their net working capital position, reducing their cash conversion cycle and reducing costs. There are various means of achieving these targets with the most straightforward ones being either to accelerate the collection of cash or to extend payment terms. Simply put, companies want to hold onto cash longer by paying later while getting paid earlier.

Large corporate buyers are aware of the consequences of paying their suppliers later and, with supplier risk and Corporate Social Responsibility becoming increasingly important, they are conscious of the need to support their suppliers. Suppliers are under similar financial pressures and many would benefit from the ability to accelerate the collection of cash.

Because of these competing interests, there is the possibility of a conflict between companies and their suppliers. One potential solution to this challenge is supplier finance.

A buyer-led solution

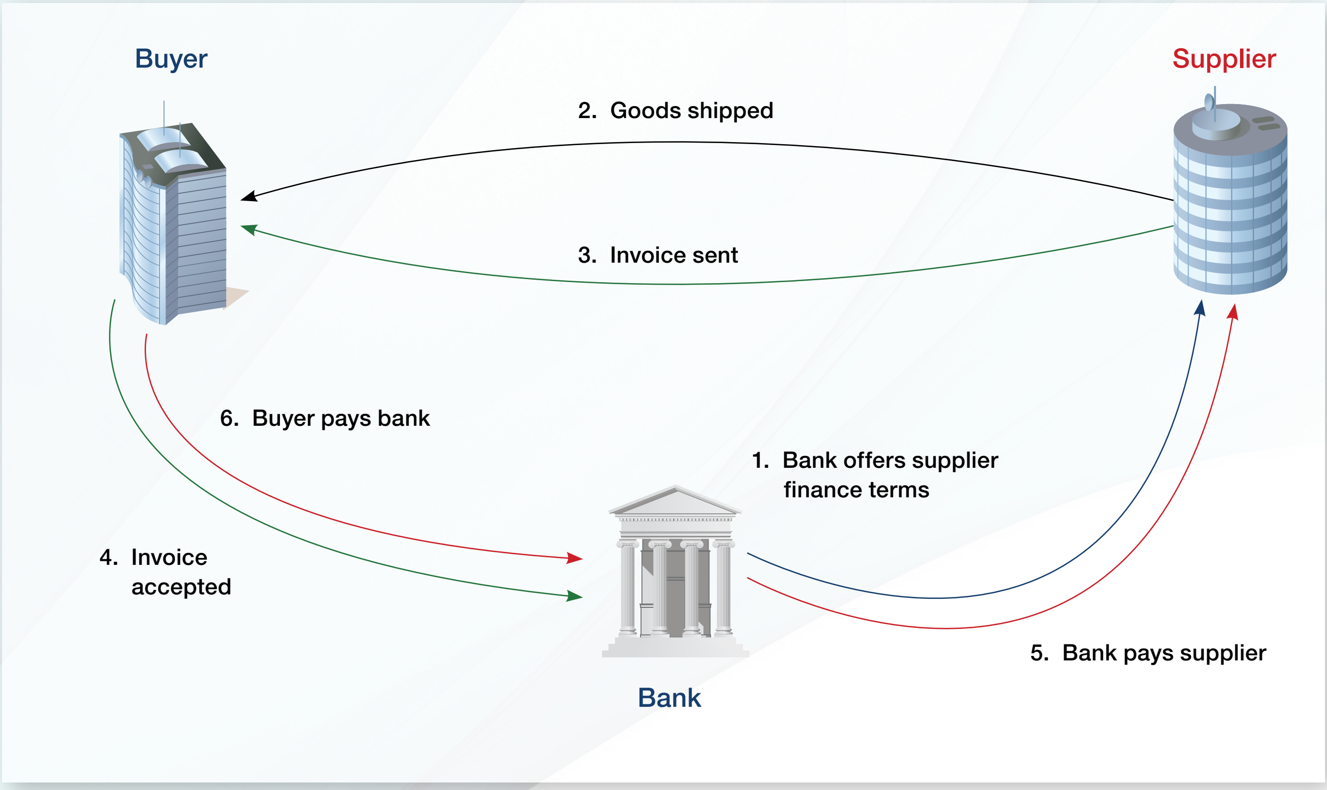
There are various products available to suppliers to accelerate the collection of cash and not wait until the invoice due date to be paid. The most common include receivables financing and invoice discounting. Supplier finance distinguishes itself from these products by being buyer-led rather than supplier-led. It also offers improved efficiencies and quicker processing.

For buyers seeking to extend payment terms, their reluctance is due to the potential impact longer payment terms will have on their suppliers. The primary impact is the additional costs that the supplier will incur as a result of having to wait longer to be paid. Most suppliers will seek to recoup these costs from the buyer by raising prices.

in association with BARCLAYS

Supplier finance removes the cash flow impact – and the cost impact – of extended payment terms. The cash flow impact is mitigated because suppliers have the ability to accelerate the collection of receivables in exchange for an early discounted cash payment – in effect, suppliers are able to get paid early. The cost impact is mitigated because the discount charge, or price, the bank charges is calculated using the buyer's cost of funds and not the supplier's. The interest rate arbitrage opportunity or differential between a buyer's cost of funds and a supplier's cost of funds is usually sufficient that it results in a lower financing cost for suppliers despite the longer payment terms.

The early discounted cash payment is the approved invoice amount less the discount charge. The bank has recourse to the buyer and not the supplier thus the reason the financing charge is calculated using the buyer's cost of funds. On the due date, the buyer pays 100% of the approved invoice amount. It is a simple calculation to compare the costs and quantify the financial benefits to the supplier.



Supplier finance is sometimes called 'reverse factoring' or 'confirming' – the latter is used in the Spanish market where the idea was originally conceived over 20 years ago. From rather humble origins, supplier finance has grown into a globally recognised solution. Today, rather than just 'noise' around the subject, experts are starting to see a genuine uptake in supplier finance activity in the corporate sector.

According to a report released in February 2014 by the Association of Chartered Certified Accountants (ACCA) and Aite Group, the current global market size for supplier finance is estimated to be between $255 billion and $280 billion. "Despite its already impressive growth, the potential for further expansion in the market as more buyers and suppliers come to realise the mutual benefits of supplier finance is significant," says Richard Hite, Vice President, Supplier Finance, Barclays.

"As the solution matures, the business case is becoming much clearer and the misconceptions around it are being dispelled," he adds. "Supplier finance is not about buyers coercing suppliers to accept longer payment terms with little or no regard for the financial strain that places them under – that is not our experience. Supplier finance is very transparent and there are not any hidden costs. It's quite a straightforward product that, when successfully implemented, produces real benefits for both parties," notes Hite.

Reaping the rewards

For most buyers, they need to extend payment terms to derive any tangible benefit. To quantify the benefit, a 30 day extension will generate £8.2m of working capital benefit per £100m of spend. But it's not just about payment term extension. Hite comments: "In addition to the working capital benefits, supplier finance provides enhanced visibility and improved control over payments and collections, and supplier enquiries are often reduced, which may lower administration costs. Many companies are beginning to see supplier finance as providing a competitive advantage".

Supplier finance also reduces the buyer's supply chain risk. According to Hite, "suppliers gain access to low cost, non-recourse cash, which is valuable to many of them".

For the supplier, the main benefits are driven from their ability to effect an early payment. This allows suppliers to improve their net working capital position, shorten their cash conversion cycle and reduce costs. The opportunity to view approved invoices, confirmed payment amounts and the due dates on-line are an added benefit.

The cost of financing is also typically lower than the cost of finance arranged directly with a bank. Supplier finance is also generally cheaper than other, more traditional, forms of supply chain finance such as factoring or invoice discounting and there is no recourse to the supplier.

Finally, using a supplier finance platform compared to invoice or receivables discounting, introduces a highly automated technology solution compared to what is often a largely paper-based process. This improves visibility, control and reporting functionality for both buyers and suppliers, while promoting process efficiency.

Buyer benefits	Supplier benefits
Mitigates the impact of the payment term extension.	Enables early settlement of receivables to reduce Days Sales Outstanding (DSO).
Mitigates supply chain risk.	Offers more predictable cash flow and supports greater control and visibility over payments.
Provides tangible support of suppliers thus fulfilling CSR objectives.	Offers non-recourse cash at a competitive finance cost.

Getting on board

For buying organisations that have decided to establish a supplier finance programme, choosing the right provider and solution is critical to success. This might sound a fairly simple process but it is actually not that straightforward. The decision is really driven by your requirements and what you need from a provider, and there are a number of factors to assess.

Hite says, "there are a number of important considerations. These include relationship, experience, approach and methodology. Depending on your geographic requirements, footprint may be a deciding factor. Credit appetite is another important consideration. Finally, don't underestimate supplier on-boarding. It is often overlooked with implementation frequently being the focus, however supplier on-boarding is probably the most important consideration". And as Simon Enticknap, Director, Trade and Working Capital at Barclays notes, "there is an increasing polarisation around the choice of provider and platform. Is it better to choose a proprietary solution or to look for more neutral technology? Corporates are understandably torn between the two."

In Hite's view, relationship plays an important role in making the right decision. "Buyers should seek a provider that understands their objectives and requirements. They should avoid a situation where a supplier finance programme is successfully implemented only to find further down the line that the funding is being withdrawn. Relationship banks that have a broad relationship with a buyer are likely to be more inclined to work with and support their client and its suppliers, particularly in a downturn."

Understanding the buyer's objectives is essential because it drives the entire process. The provider will take on board the client's objectives when it conducting its working capital analysis and in developing a supplier on-boarding strategy. An analysis of the buyer's spend with suppliers is key to a successful programme. The provider is able to quantify the benefits of supplier finance both to buyers and suppliers and calculate other financial metrics, including building a business case. This should be formally presented to the buyer along with a recommended best solution. "The buyer is making part of its credit limit available to these suppliers, so it is absolutely natural for the buyer to ensure that it is getting maximum value out of the arrangement," Enticknap points out.

Supplier finance at Barclays

"We have a team of dedicated experts who work closely with the buyer to offer a solution that is aligned, and specifically tailored, to their working capital needs. Our approach is consultative and collaborative," says Enticknap. "We also do all of the on-boarding legwork."

Once the implementation of the Barclays programme is complete and suppliers have been on-boarded, it is a highly efficient process and very light touch. This is how it works on a day-to-day level:

1. The supplier submits their invoice to the buyer for approval.
2. The buyer approves the invoice and electronically transmits the payment instruction to Barclays. The payment instruction is the buyer's commitment to make a payment of a specific amount on a date in future.
3. The supplier is notified that their invoice has been approved by email and can view the data online, including the invoice details, amount due and the confirmed payment date.
4. The supplier has the option to request an early discounted cash payment electronically via the platform.

5. Upon Barclays' acceptance of the request for discount, the net amount will be credited to the supplier's designated bank account within 48 hours.
6. On the payment due date, Barclays debits the buyer for the full invoice amount.
7. If the supplier has not submitted an early payment request, Barclays pays the supplier the full amount on the due date.

Setting up your supplier finance programme: best practice for buyers

- √ Find a provider committed to understanding your objectives and which completes an analysis of your spend. This will quantify the financial metrics, build the business case for supplier finance and identify suitable suppliers. It will also assist in developing the supplier on-boarding strategy. Most importantly, the output from this analysis will confirm if supplier finance is appropriate for your business.
- √ Consider all aspects of a provider's offering. A great deal of attention is on implementation, for example, however supplier on-boarding is essential to a successful programme and perhaps the most important aspect. The provider's approach and methodology and 'after-sales support' should be assessed.
- √ Key internal stakeholder buy-in is essential. Finance, procurement, legal and IT must all be committed to the project.
- √ Obtain auditor sign off for accounting treatment before implementation. Buyers want their trade payables to remain classified as trade payables, not reclassified as debt, as does your bank.
- √ Form a project team and appoint an internal project champion. The team should include representatives from finance, procurement, legal and IT. The project champion will drive the programme within the buyer's organisation.
- √ Internally communicate the details of the supplier finance programme ensuring every party understands their responsibilities and the benefits from their own functional perspective. Engaging internal stakeholders at every level is vital to the programme's success.

Choosing an experienced, committed and reliable provider that understands your requirements and objectives as well as having the credit appetite to support your programme, should be among the key considerations. Pricing is often a key differentiator but when evaluating a provider, it is actually one of the least important considerations.

Evolution and future

Now that companies are quite comfortable with the premise of supplier financing, we are also seeing some interesting tweaks to the vanilla model, Enticknap believes. "A handful of companies actually have in place self-invest programmes, which essentially put them in charge of buying their own risk. Others are looking further into the area of rebates and how these can be leveraged more effectively. So there is a lot of interesting and creative thinking going on in this space and the product continues to mature at an impressive pace," he notes.

Likewise, the wider supply chain and trade marketplace continues to come of age. With the bank payment obligation (BPO) slowly gaining traction and e-invoicing now being integrated into supply chain solutions, the way companies carry out their commercial transactions is certainly changing. What remains constant, however, is the need for intelligent finance solutions that enable companies to maximise value across the supply chain.

Simon Enticknap, Director, Trade and Working Capital has over 37 years of trade experience across corporate, financial institutions and structured trade finance. He joined Barclays in April 2011 and moved to the Trade and Working Capital Product team in March 2012. Enticknap currently heads up the Product Execution team which is responsible for managing the delivery and governance supporting the trade product set.

Richard Hite, Vice President, Supplier Finance joined Barclays in 2011 as a Supplier Finance product specialist. Hite has over 25 years of experience in banking, largely in relationship management, both in the US and the UK. He has also served as European Treasurer for a US Group as well as worked for independent Supplier Finance companies. He has a degree in Economics.

THE INDUSTRY VIEW

Bea Rodriguez
Head of International Cash Portfolio Management, Managing Director

BLACKROCK®

Bea Rodriguez, Managing Director, is the Head of Non-USD Cash Portfolio Management within the Trading and Liquidity Strategies Group.

Prior to joining BlackRock in 2009, Bea was with Fidelity International Investments, most recently as a sterling high-grade portfolio manager and rates specialist, and previously as a manager of institutional and retail sterling money market funds as well as short duration strategies. Bea was also a portfolio manager at Deutsche Bank AG from 2000 to 2003 where she headed up the cash reinvestment process for the securities lending desk as well as overseeing the launch and investments of Deutsche Bank's offshore UCITs money market funds. She began her career at J.P. Morgan Investment Management in 1994.

Bea earned a BSc degree in management sciences from the London School of Economics and Political Sciences in 1993.

Against a backdrop of low, zero or even negative returns, heavy bank regulation and limited availability of quality investments, Bea Rodriguez, Head of International Cash Portfolio Management, Managing Director, BlackRock looks at what is currently trending for investors, plotting the rise of some very interesting alternate corporate cash management opportunities.

What do you see as the key investment concerns for treasurers today?

There are many right now but to pick just a few 'bullet points' I'd say low yield, reduced supply – particularly in the money market space – and a reduction in the pool of high-quality investment opportunities as the banking universe is downgraded. Another critical theme for investors to factor into their thinking is changing resolution regimes across the world, particularly in Europe, which makes unsecured credit investment more risky.

As a backdrop to all of this, the changing financial regulatory architecture – via UCITS, ESMA, AIFMD, Basel III et al – is impacting the investment space, particularly secondary market liquidity. As the banks 'right size' their operations they are withdrawing from a lot of markets with the effect that there has been a substantial reduction in the balance sheet available to trade secondary market liquidity. This creates further risk in being able to sell credit. The shift in architecture is also adding a slight 'kink' to the curve because money funds want to invest in shorter term paper whilst banks want to invest longer. The sweet spot for a bank is anything beyond three to six months; they have no interest in anything under three months. The fact that the banks have been downgraded to an average 'A' rating adds to the difficulty because the appetite for 'AAA'-rated money funds means the opportunities to invest in that space are significantly reduced.

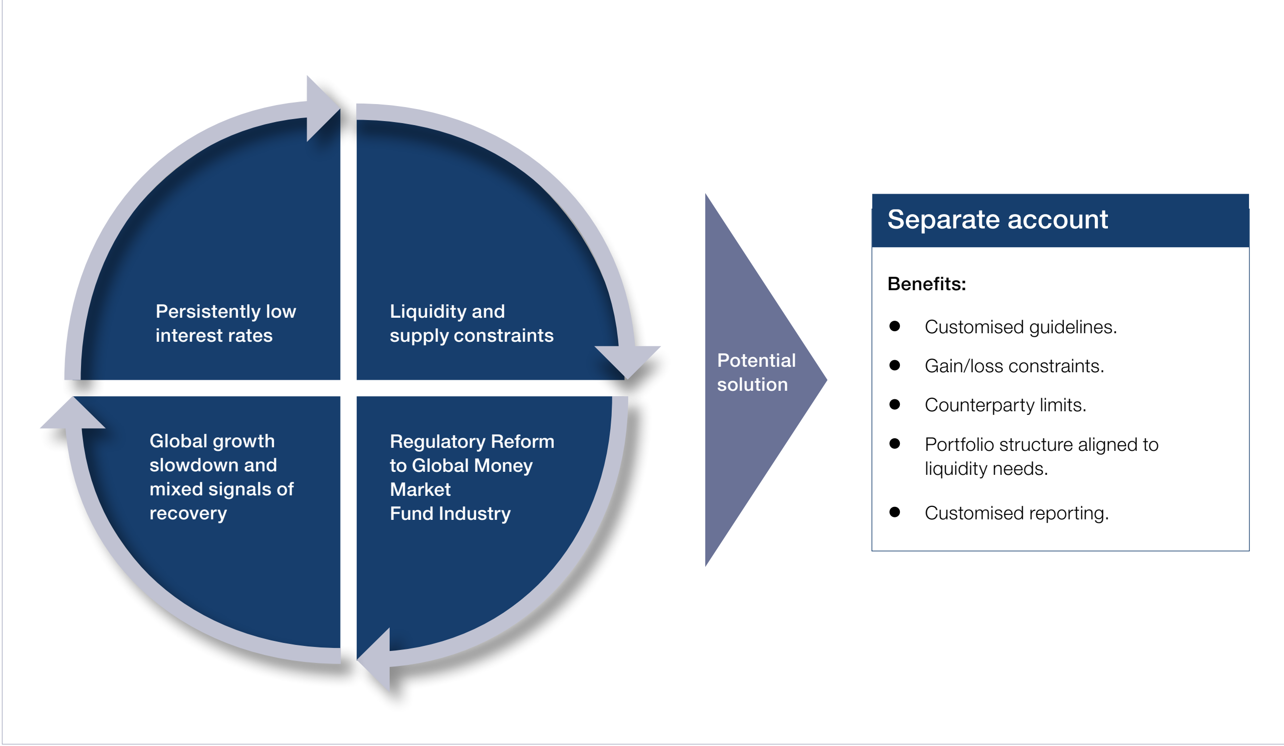
With all these market tensions, how are investors responding?

Corporate investors are aware of this backdrop and generally have been broadening their thinking. We have seen a few investors get back into repos, doing it themselves in-house as a 'risk-free' trade, taking high-quality collateral and executing a term repo trade just to get some of their cash invested. This can be difficult to do as it needs the legal infrastructure in place. I think many more are opening up their thinking around other types of investment models. We have seen a lot of interest from our corporate client base for separately managed accounts (SMAs), but we are also hearing from that segment the idea that they are prepared to drop a money-fund rating, so one of the products we have designed is our Euro Asset Liquidity Fund (EALF) which is not rated by any NRSRO.

In the past there had been a fair amount of reluctance from corporate treasurers to invest in unrated money funds. Rated funds are certainly easier to sell to the Board because there is an external due diligence that is naturally in place, but we feel that the conditions of the money markets are right for unrated funds, particularly in euros where yields are extremely low and there is so much dislocation of supply through the basis swap. In response, some – but certainly not all – corporate clients are going to their Boards seeking to change policy to open up to these 'new' investment opportunities. The final push in this direction will come when yields get that much lower.

Yield obviously remains an issue so what investment outcomes are treasurers typically seeking?

European clients tend to move out gently; the clients that really push the boundaries have typically been large US-based corporates. One of the big interests right now is in SMAs. The US clients have been conversant with SMAs for some time and now a number of them are looking to use the same in Europe too. The lead time to set up an SMA varies considerably, depending on how engaged the conversation becomes around investment guidelines, but one of the key benefits of an SMA is that it can be tailored to the investor's risk profile. Our US corporate client base that is coming into Europe for SMAs tends to be quite flexible with its guidelines; they will drop a little in quality and some will go out a bit further in duration – anything from one to five years.



Source: BlackRock

In addition to the ability to tailor a risk profile what would you say are the main attractions of an SMA for investors?

It can offer more diversification and with the extra flexibility in guidelines, investors have increased opportunity to capture return. One of the biggest wins though is the fact that investors can be in a space where money funds aren't – there is inherent value there as the market is that much more biddable. From an investor perspective, there is more scope in longer maturities because this is where banks get value on their balance sheet; investors get to play in a more value-add part of the market.

BlackRock's EALF seems to break the mould, at least for treasurers. As an unrated fund, does it raise any eyebrows?

When we first considered offering this product we wanted to bring to market something that would service clients and be a good contingency in the case of a deposit rate cut – which is of course what we got – and in the event of that still offer a gross positive yield. The differential to the rated fund is around plus five to six basis points.

What is interesting about how we extract that return is that if you were to lift the bonnet on the rated versus unrated versions you'd see they are very similar; there is not one asset in the rated fund that is not in the unrated version. For all intents and purposes we are buying the same assets with the same outer boundaries; we are not going longer and we are not dropping in quality. The funds are both 60/120 in terms of weighted average maturity and weighted average life, and they are both CNAV.

We use the UCITS framework for the unrated fund and this allows us to concentrate, to an extent, in a few names. UCITS permits up to 10% in one name as long as anything over 5% is added together and in total is less than 40%; this is often called the 5/10/40 rule and really means a fund can have four names at 10% if it wants to. This suits a universe which is very much reduced in terms of the number of high-quality names.

Ultimately, if investors accept that we can get our credit risk management right in the rated fund, then they should be comfortable that they will not have a credit event in the unrated fund because they are not actually taking more risk. In essence, it is just the structure of the fund that varies, using a bit more concentration to get those extra basis points. Naturally, the way we achieve that higher yield still takes some explaining but the aspect that takes a bit longer for the corporate client to manage is getting their policy rewritten to enable such an investment. Unrated MMFs are quite common in the US but I'm sure in Europe they will gain some traction. Our fund is currently around €1.2 billion and there are a number of our existing corporate clients invested; they may not have jumped in with both feet but they have understood the benefits.

The EALF has been designed for the environment we are in now, a world where corporate treasurers and other clients are uncertain as to what their next move is, and where some of the core bill rates and the overnight markets in Europe are in negative yield territory. Market conditions are going to become more challenging and, based on today's outlook, I think the industry as a whole should expect to see lower yields. Most corporate treasurers are already aware of, or are on the cusp of understanding that they will have to face change. As such our product innovation is something that is always in flux, driven by market environment and regulation.

With the SEC having announced its plans for MMF reform and its European counterparts still debating the issue what has been the effect on investors?

In the US, so far it is business as usual. Investors are digesting the changes and evaluating the new rules against their cash investing needs. We have two years before the reforms really impact but work is already under way to address the structural changes at the asset managers. The first big thing for the industry to solve in the wake of US reform announcements is the operational piece around same-day VNAV. The US certainly has the pricing element sorted. It is much more of a same-day market than in Europe and so in that sense the US is ahead of the game. In fact, Europe seems to be moving to a three-day market. That said, even in Europe, the pricing in money market instruments has improved noticeably. CP and CDs were always difficult to price as they are OTC instruments but there are providers out there who do it, and do it well. I believe the market is aware and is evolving to meet the needs of same-day pricing. Change is under way and the industry as a whole seems hopeful of achieving a satisfactory outcome.

From a market investment point of view do you see any divergence between sterling and euro?

There are definitely some diverging central banks themes right now. Mario Draghi (President of the European Central Bank) was very dovish at the annual central bank symposium in Jackson Hole (and thus keen to maintain low interest rates), but there is worry about deflation. The UK meanwhile has more than 3% growth and there is an acceptance that there will be a rate hike, albeit a small one, probably in Q1 next year. In the US too, the market is clearly starting to challenge the 'low for a very long time' view and it also has a recovery in place. It will be interesting to see – and it is one of the key themes we are focused on in the medium term – how the European curve reacts to or survives a rate-rising environment in the biggest benchmark country in the world.

With all this in mind, is tomorrow's investment market one treasurers should fear or look forward to?

We think tomorrow's investment market is more that of accepting change rather than one of fear. There are obviously a number of headwinds in the euro market but with challenge brings opportunity and from a BlackRock perspective we had been preparing for this difficult backdrop for some time and we think we have got the right products in place and expect more active engagement with the client base as matters evolve. ■

Treasury outsourcing

To outsource or not to outsource is a question which many corporates will have faced over the years. For a number of reasons, the answer for the majority has been 'not'. However in recent times treasury outsourcing has made something of a return and is offering an option to corporates looking to reduce costs and increase efficiency. In this article, Treasury Today looks at what treasury outsourcing actually is, its uses, and the debate surrounding the practice.

Outsourcing, the process of transferring a portion of a business's operations out to a third-party provider, is something which generates an eclectic mix of opinions. For some, outsourcing an area of business responsibilities can be seen as a way to reduce costs, improve efficiency and free time to perform value-add duties. For others, it can be perceived as a threat which can cause a loss of control, loss of power and a loss of jobs. Despite this, outsourcing is something which many businesses participate in, primarily outsourcing high-volume functions such as human resources and IT, and have done for many years.

Treasury is another area where outsourcing was touted to be a revolutionary concept, redefining the role of the function when first introduced in the late 1980s. However, for a number of reasons the adoption of treasury outsourcing was neither widespread nor long-lived (in the main). In more recent times outsourcing has made a return, not as the revolutionary concept it once claimed to be, but as a genuine option for companies to consider when looking at ways to improve their treasury function. However, many still are not fully aware of what treasury outsourcing actually is and what it can offer.

What is treasury outsourcing?

Simply put, treasury outsourcing is the outsourcing of all or part of the treasury function to a third-party outsourcing provider, or shared service centre. However, within this simplistic definition there are many nuances. "The industry still hasn't been exactly defined," says Gautam Dhillon, Founder and CEO at treasury outsourcing provider, The Treasury Outsourcing Company (TOC). "Many companies offer treasury outsourcing services," says Dhillon. "Banks for example offer netting and pooling services, some companies offer front office outsourcing solutions and others middle and back office. The scope and variety of services is large and occasionally fragmented. To overcome this problem we have a simple model where we offer a complete tactical and operational outsourcing solution. The client can choose to outsource its entire front, middle and back office or components of each; with each activity being performed on world-class TMS."

Treasury outsourcing services can generally be viewed along a spectrum of treasury operations. "At one end you have the bottom-end, high-volume processes, such as payments processing, which treasurers can outsource on an operational basis," says Jackie Bowie, CEO at financial risk consultants J.C. Rathbone Associates. "At the other end of the spectrum there are the high-end acute decision-making processes which require technical and current market expertise, such as hedging strategies, which can also be outsourced on an ad-hoc/project-by-project basis."

Just as there are two forms of outsourcing, discretionary and operational, there are two major types of third-party outsourcing provider. Firstly, banks can offer a range of treasury outsourcing services. Although this section of the market has been scaled back in recent years, one bank which still offers these services is Bank of America Merrill Lynch (BofAML). "Our outsourcing services complement the products which we offer," says Suzanne Janse van Rensburg, Regional Head of Liquidity and Investments, GTS EMEA, BofAML. "And we are able to offer these services with the expertise and support of the bank fully behind it."

The second type of outsourcing service provider is independent companies that focus on treasury as a key competency. "It is important that a treasury outsourcing provider has a treasury orientation," says Pat Leavy, Executive Director at FTI Treasury, a provider of treasury outsourcing solutions. "The concentration should therefore be on practical corporate treasury risk management and for this corporate treasury expertise and knowledge are required in addition to treasury technology and best practice processes, which third-party providers like us can deliver."

Providers of outsourced treasury technology, known as Application Service Providers (ASPs) are also regarded as third-party treasury service providers. These offer companies the ability to hire costly treasury technology such as a TMS, thus allowing the corporate to avoid many of the costs associated with these. The trade-off comes with the limited flexibility and customisation offered by many ASPs.

What can be outsourced?

Theoretically, all aspects of the treasury function can be outsourced. However it is extremely rare for a company to outsource all of its treasury activity. Due to this the treasury function is divided into three broad areas which can be outsourced; front office (execution), middle office (accounting and reporting) and the back office (settlement and reconciliation). The treasury can decide to outsource the entire office or alternatively some functions within it, keeping the others in-house.

How much of and what a treasury decides to outsource is very much based on the organisation's individual circumstances and what can provide the most value. However, as FTI Treasury's Leavy explains, there are four fundamental models of treasury outsourcing:

1. Full suite treasury outsourcing – this model sees the organisation outsource the front, middle and back office to a third party.
2. Back and middle office outsourcing – through outsourcing the back and middle office the treasury can focus its in-house recourses on strategy and execution.
3. Regional treasury centre outsourcing – this model will see the outsource service provider manage the organisation's regional cash and intercompany financing without the need for it to establish its own treasury function in the region.
4. Standalone activity outsourcing – a company may choose to outsource a single activity should they not have the capabilities to carry it out in-house. Intercompany netting and intercompany lending provide good examples of these standalone activities.

A new and relatively undeveloped area which can also be outsourced is a company's disaster recovery. "Our research suggests that many treasuries do not have a satisfactory disaster recovery policy in place," says TOC's Dhillon, "so, if for any reason a company is unable to get into the office or the systems crash, there can be large ramifications." For Dhillon, outsourcing provides a logical safeguard against any disaster scenario and ensures that the risk of this is mitigated. "This is further boosted with the advent of cloud technology, allowing outsourcing services to be hosted in the cloud, meaning regardless of the disaster the data will still be remotely accessible and useable."

While many aspects of treasury can be outsourced, our experts agree that there are some areas which should be retained in house. These include core competencies such as strategy development and any decisions around treasury management such as key performance indicators and service level agreements with its outsourcing provider (OSP). Bank relationships and treasury controlling are another two areas which a treasury should keep firmly in-house.

Why outsource?

So far we have looked at what treasury outsourcing is and the areas of treasury which can be outsourced; but why would a treasury want to outsource its operations? The answer is primarily to reduce costs. There are however a number of other drivers which may lead a treasury to outsource its operations, which include:

1. Technology – if a company is looking to purchase or update its legacy technology it may look to outsourcing as an alternative. In this relationship the set-up will be quicker and the ongoing maintenance of the technology removing the need for this expertise in-house.
2. Specialist expertise – a treasury may not have the expertise in certain areas and may therefore look to outsource these processes.
3. Processes – many treasuries with limited resources will often find they have a number of inefficiencies and an inadequate segregation of duties. Outsourcing some areas of the treasury function can help to resolve this.
4. Location – if a company looks to expand to a new region it may wish to outsource its regional treasury for that region rather than build its own infrastructure.

The wide range of drivers for outsourcing means that it can offer value to companies throughout its life cycle. For example, a start-up looking to acquire a centralised treasury function can achieve this quickly, with support and without the costs associated with establishing its own through outsourcing. Alternatively a company which is in the growth stage of its life cycle may wish to outsource some of its processes to help with its development and then look to insource these at a later date. Finally, a mature company may wish to outsource to radically change the culture of the treasury.

> "Our research suggests that many treasuries do not have a satisfactory disaster recovery policy in place, so if for any reason a company is unable to get into the office or the systems crash, there can be large ramifications."
>
> Gautam Dhillon, Founder & CEO at treasury outsourcing provider, The Treasury Outsourcing Company (TOC)

Benefits

Other than the simple advantage of reducing costs, an outsourcing arrangement has the potential to deliver a number of additional benefits to the treasury and the organisation as a whole. These include:

- Allowing treasury to focus on strategy – as the treasury is being called upon to be more of a value-add strategic business partner, outsourcing the day-to-day activities can provide the in-house team with more time to focus on this.
- Increased focus on the activities which remain in-house, thereby increasing efficiency.
- Organisational benefits – outsourcing can allow the treasury to improve its organisational structure and create an improved segregation of duties, mitigating the risk of fraud and error between back and front office activities.
- Reducing costs – the outsourcing provider should be able to make use of economies of scale and provide certain services at a lower cost than they would be if performed in-house.
- Speed of implementation – following fundamental shifts in the organisational structure of the company, a merger and acquisition (M&A) for example, outsourcing can be used as a method to introduce the required new treasury activities more quickly than establishing these in-house.
- Flexibility – the outsourcing provider may be able to adapt to a corporate's changing requirements quicker and more efficiently than if completed in-house.
- Data quality – very often an unanticipated outsourcing benefit is that the quality of the data that is produced is higher. The challenge for the corporate receiving the data is therefore how to use it.

Concerns around outsourcing

Despite the benefits which outsourcing can offer corporates, there are a number of issues which are highlighted by treasury

professionals about the practice which historically have prevented greater uptake.

The fear of relinquishing control surrounding treasury operations is the main issue around the practice of outsourcing. Although it is inevitable that by outsourcing a certain degree of control will be lost, the fear may often be overstated. "Despite the perceptions, in the outsourcing world most, if not all, the decisions and control remains in house," says Leavy. "All actions taken by an outsourcer occur within discrete parameters and with very limited discretion from the provider's point of view. The main decisions remain in-house – it is just the processes behind these which are outsourced."

The seeds of this mind-set may be found during the early days of treasury outsourcing where it was promised to be revolutionary. "The initial vision of outsourcing was to outsource everything including decisions and strategy," says Leavy. "This ultimately never happened and in reality shouldn't." For Leavy the mind-set remains because the purpose of outsourcing hasn't been fully communicated to the treasury community.

Another area of potential concern regarding outsourcing is around security and this is something which should be considered carefully by treasurers when looking to establish an outsourcing arrangement. "Ensuring the client's data is secure and confidential is critical and corporates need to be sure that the right security is in place," says BofAML's Janse van Rensburg. TOC's Dhillon agrees. "There needs to be strict controls regarding who can access the data both within the OSP and once it is sent back to the client. If a service is web-based then encryption will also be required."

In addition to the loss of control and security fears there may also be wider effects caused by outsourcing treasury operations which can cause issues for the department. One of these is job restructuring or job losses which can affect both the efficiency and moral of the treasury. A second area of potential concern surrounds the relationship which the treasury has with other operating units. By outsourcing, these relationships may be altered, so the impact of these should be carefully assessed by the department.

Full value

If a treasury decides to set foot into the outsourcing world, how can it ensure it receives full value from the arrangement? "An outsourcing relationship is very much like a marriage," says TOC's Dhillon. "Regardless of the client's outsourcing motivations there should be constant dialogue between both sides with each understanding the scope of work, KPIs and SLAs. Once this happens the relationship is then on a firm footing." For Dhillon this is the key to obtaining the most out of an outsourcing agreement and insists that a lack of dialogue and strategic scope alignment is a serious problem. "The clients who get the most out of the arrangement are the ones that enter the relationship with a clear scope. This then enables the OSP to deliver and be measured against demanding KPI and SLAs.

If, on the other hand, the client has not fully scoped the requirements and proceeds to outsource treasury activities, this will be problematic even if the OSP is meeting all the KPIs and SLAs, since the strategic scoping exercise was incorrect. This means the client will ultimately be unhappy with the venture," he says.

Engagement in the process and asking questions is also seen by Bowie as key to the treasury obtaining the most out of the arrangement. "This allows us to understand their concerns and tailor a solution to fit their individual needs," she says. If they step back then often the outsourcing service provider will not feel fully briefed." Many outsource providers are now also now able to provide flexible bespoke agreements to suit the diversity of corporate needs. This is, however, something which again can only be arrived at through dialogue.

> "Ensuring the client's data is secure and confidential is critical and corporates need to be sure that the right security is in place,"
>
> Suzanne Janse van Rensburg, Regional Head of Liquidity and Investments, GTS EMEA, Bank of America Merrill Lynch

Future outsourcing

"Corporates will say that they are outsourcing more now than ever before," says Bowie. "However, this is rather misleading; prior to the financial crisis corporates were heavily reliant on their banks for both ideas and strategy. This may not have been perceived as outsourcing because there is no explicit fee for the services but in reality this was a form of quasi-outsourcing in itself."

Despite the evolution of the market outsourcing is not yet a mainstream treasury practice and is still viewed by many through an outmoded lens. To change this, the industry is required to communicate the scope and benefits of outsourcing more efficiently to the treasury community. On the other hand the developing role of treasury may see the popularity of outsourcing increase. "Traditionally treasury has been seen as a cost centre," says Dhillon. "If you outsource treasury processes the activity that was once seen as a cost centre becomes a profit centre for the OSP, this shift can be transformational for the treasury function and the captive organisation as a whole."

It must be noted that a potential barrier to the greater use of treasury outsourcing in the future comes from the fact that operating costs have been able to be reduced, not through outsourcing but through automated cash management solutions. This has allowed corporates to remove a large degree of the recurring daily duties from their operations, although it must be noted that not all the benefits which can be obtained through an outsourcing agreement can be accessed this way.

Ultimately, outsourcing remains polarising amongst the treasury community. For some, outsourcing is a great way to reduce costs and create greater efficiencies in the treasury. For others, it is something which will lead to a loss of control. Then there are those that sit in the space between the two. So while not being the revolutionary solution it once promised to be, outsourcing must be regarded as another option open to treasurers when looking at ways to reduce costs and increase efficiency. ■

Turning change into opportunity

Niall Kelly
Head of Group Treasury
DCC

Ahead of the forthcoming Irish Association of Corporate Treasurers (IACT) Annual Summit in Dublin on 6th November, Treasury Today catches up with Niall Kelly, Head of Group Treasury at DCC – a FTSE 250 listed international sales, marketing and distribution business.

DCC is an international sales, marketing and distribution business with revenue of circa €14 billion. Headquartered in Ireland, most of DCC's revenue is generated internationally, in the UK and in Continental Europe. The Group now has over 10,000 employees and operations in 13 countries across three main divisions – energy, technology and healthcare.

Although DCC's ongoing international growth means that the Group primarily looks to international economic indicators, Kelly notes that "the Irish economy is turning a long-awaited corner and measured optimism is the order of the day for investors, individuals and businesses alike. Employment rates are rising, GDP growth has picked up significantly and tax revenues are also increasing. In short, all the key indicators are trending positively."

Strategic treasury

According to Kelly, DCC's expansion in Continental Europe has benefitted from the Group's experience in the UK and its strong relationships with the oil majors and its other supply partners.

Here, he stresses the importance of long-term relationships to DCC, and explains how the Group's conservative financial strategy has always been a significant plus point for its suppliers. "As a Group, we are very focused on having a strong balance sheet. Having long-term debt and strong liquidity positions on the balance sheet has, over the years, proved to be a competitive advantage for us: in terms of our relationships and negotiations with our key suppliers and partners," he says. "When we buy distribution businesses from the oil majors, they are replacing a diversified stream of smaller cash flows with a single cash flow and it's important to clearly demonstrate the ability to readily meet monthly product payments."

So how does DCC manage this? "Well, we are and have always been well-funded. We tightly manage our working capital and we maintain a relentless focus on Return on Capital Employed (ROCE). We go to the markets well ahead of needing funding and we think strategically about when to issue," Kelly points out.

Testament to this is the fact that the Group has been to the US Private Placement (USPP) market seven times since 1996. The two most recent issues, in February 2013 and March 2014, raised $525m and $750m respectively.

Sharing knowledge

Historically a dollar-denominated market, Kelly reveals that there are now significant direct currency capabilities in the USPP market, a market which now includes increasing numbers of UK and Continental European investors. "Even US debt investors now have the ability to provide local currency by putting in place their own hedges," he explains. DCC included sterling and euro tranches in its USPP this year: some of which was provided by investors who had natural balances in those currencies; some of which was provided by US investors who undertook swaps in the background.

Kelly will be talking more about developments in the USPP market – and sharing the secrets of DCC's long-term success in that market – at the IACT's Annual Summit in the Gibson Hotel in Dublin on 6th November. A keen supporter of the IACT, Kelly appreciates the organisation's focus on both disseminating best practice and representing corporate treasurers in an environment of continuing change. SEPA and EMIR are two good examples here, he notes. "The IACT has done a great job of keeping its members informed of developments and also in representing them in the context of fairly significant changes in the industry."

These changes will no doubt be discussed at length by attendees during the IACT Summit, where regulation, evolving technology and the increasing sophistication of payments fraud, are likely to be talking points around a comprehensive conference programme, says Kelly. But "rather than lamenting the challenges that change brings, this evolution is actually an enormous opportunity for treasurers to revisit legacy structures and processes and strategically position their businesses for ongoing growth," he concludes.

Rethinking connectivity

Tackling the key themes of integration, security, and mobility, this workshop, held at BNP Paribas' 7th Cash Management University in Paris, analysed the latest trends – and challenges – around corporate connectivity. Where should treasurers be focusing their attention and budget? Which technologies are game changers and which are simply gimmicks?

The role of the treasurer is becoming increasingly complex and the tasks that treasury professionals perform on a daily basis are now far more sophisticated than ten, or even five, years ago. In turn, this evolving remit calls for technological innovation which will support treasurers to complete their day-to-day tasks, while simultaneously adding value to the wider business.

One such innovation is cloud computing. According to an informative presentation given during this workshop by Marcus Hughes, Director Business Development at Bottomline Technologies, cloud computing is now more important than ever. There are several significant drivers for this, he believes, such as the fact that many banks are reducing their cross-border lending, or deleveraging, and reducing their international networks as a result of Basel III, or in some cases, political pressure.

An unintended consequence of this banking 'de-globalisation' is that corporates will need even more banking partners to achieve global coverage, noted Hughes. This could exacerbate a longstanding problem for many corporates: too many smart cards and tokens for connecting with multiple banks, using different standards and different file formats. This situation could quickly become quite a headache to control and a major security risk, he said.

Little surprise then that more and more corporates are looking to use bank-agnostic SWIFT connectivity services – largely through the use of a SWIFT bureau. And as Hughes pointed out, SWIFT service bureaux were created originally to provide secure connectivity to SWIFT but now the best bureaux offer much than just connectivity: cloud-based applications for payment factories, SEPA DD mandate management, reconciliation, data transformation, compliance, cash forecasting, sweeping and pooling.

Regulatory pressure

In addition to de-globalisation, banks are also becoming more selective about which companies they lend to and at what price – again as a result of Basel III. The types of deposit that banks will take is also coming under greater scrutiny since the new Liquidity Coverage and Net Stable Funding Ratios mean that retail deposits are more attractive than corporate deposits, unless they are operational balances as part of cash management services, or unless the deposits are committed to the banks for longer periods. This is precisely why, Hughes explained, efficient cash forecasting, sweeping and pooling arrangements are going to be even more valuable to avoid unnecessary overdrafts and optimise interest.

To meet these requirements, and the added burden of regulations such as the European Market Infrastructure Regulation (EMIR), it is important for corporate treasurers to find a multi-channel platform which is adaptable, scalable, secure, resilient, proven and flexible. And increasingly, noted Hughes, these platforms are in the cloud, offering connectivity to multiple banks and multiple networks and a stack of software applications.

In short, with the arrival of cloud computing, corporates need to think not just about connectivity, but about 'connectivity plus' – in other words, accessing value add software applications, hosted in the cloud.

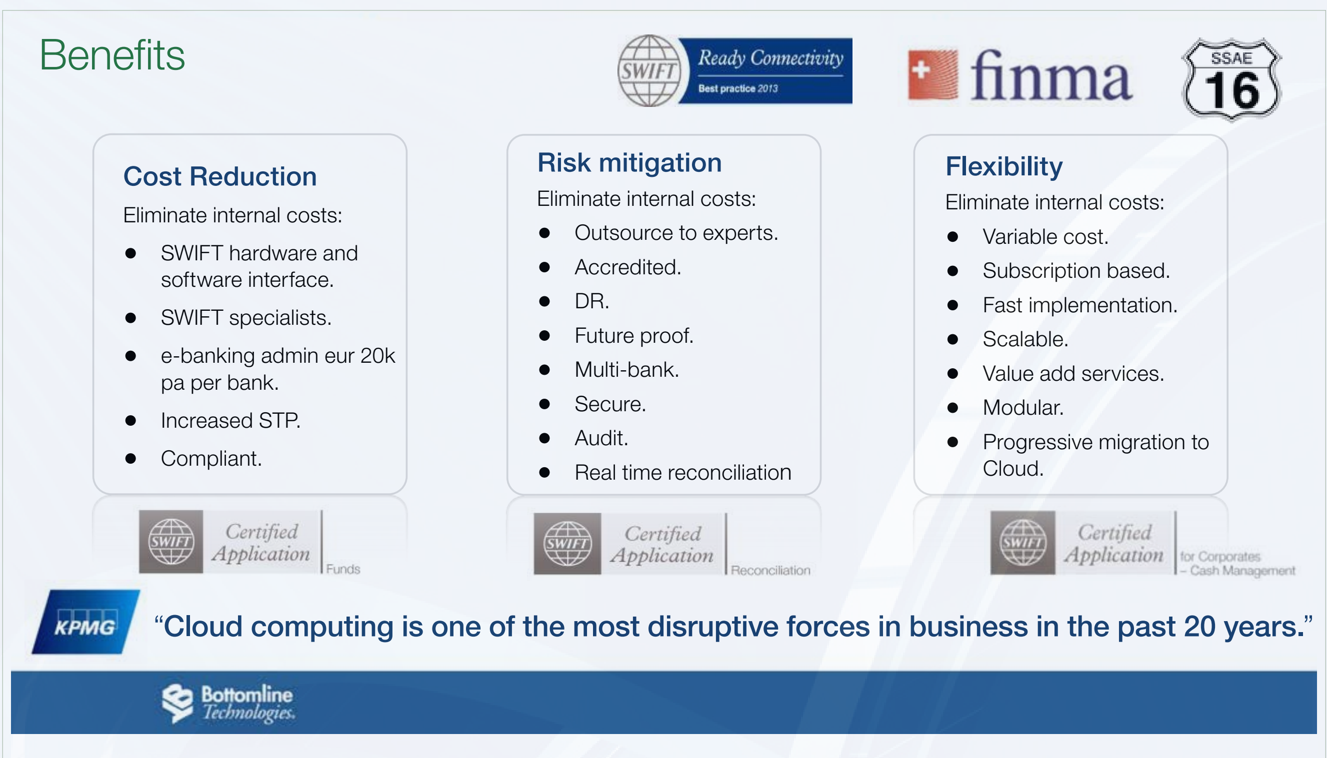
Cloud computing in practice

During the session, Hughes also provided a detailed case study on Scor, the French re-insurance group, a customer of Bottomline's teams in France and Switzerland. The company was looking to migrate from ETEBAC to SEPA and was also tasked with a number of strategic decisions around multi-bank connectivity and security. It was looking for a smart solution to solve its multiple operational and strategic challenges in one – it approached Bottomline.

Today, Scor achieves secure and resilient connectivity with multiple banks and counterparties internationally by outsourcing to Bottomline's SWIFT service bureau in Geneva, using GTExchange multi-network interface. Scor also uses SWIFT's 3SKey to approve and authenticate outgoing messages. This is a single token to securely authenticate and approve transactions with multiple banks, using multiple channels, such as SWIFT and banks' own e-banking platforms. 3SKey uses PKI and ensures a clear audit trail of who has approved a transaction. This, Hughes explained, is additional security on top of a SWIFT BIC which indicates which legal entity initiated a transaction.

In addition, Scor has automated data transformation of legacy formats into and from ISO 20022, to comply with SEPA and other message types using XML, which improves STP. For this, Scor uses BT's GTFrame data transformation solution. Conducting all the data transformation on one platform means that Scor does not need to update its formats in different platforms; instead they simply update once for all their systems. Elsewhere, the company also uses Bottomline's enterprise reconciliation solution GTMatch, which reconciles payments, bank statements, FX and MM transactions, as well as statements of securities holding.

The benefits of these solutions are wide and varied, but centre around cost reduction, risk mitigation and flexibility:



Source: Rethinking connectivity, BNP Paribars. BNP Paribas Cash Management University, Marcus Hughes, Director of Business Development, Bottomline Technologies

Technology for excellence

Another company that has reaped significant benefits from an overhaul of its treasury technology is Valeo, one of the world's leading automotive suppliers. The so-called TOTEM (Tools for Treasury Excellence in cash Management) project was led by Thierry Hamon, the company's Treasury Controller. With more than 100 treasury staff and 600 signatories spread across 26 countries and four continents, 60 ERP systems, numerous payroll systems, and more than ten bank groups, the group's connectivity challenges were manifold – and something had to change.

The graphic opposite illustrates the sheer scope of the project, and highlights how the challenges were overcome – primarily through the integration a software-as-a-service platform and the implementation of SWIFT connectivity.

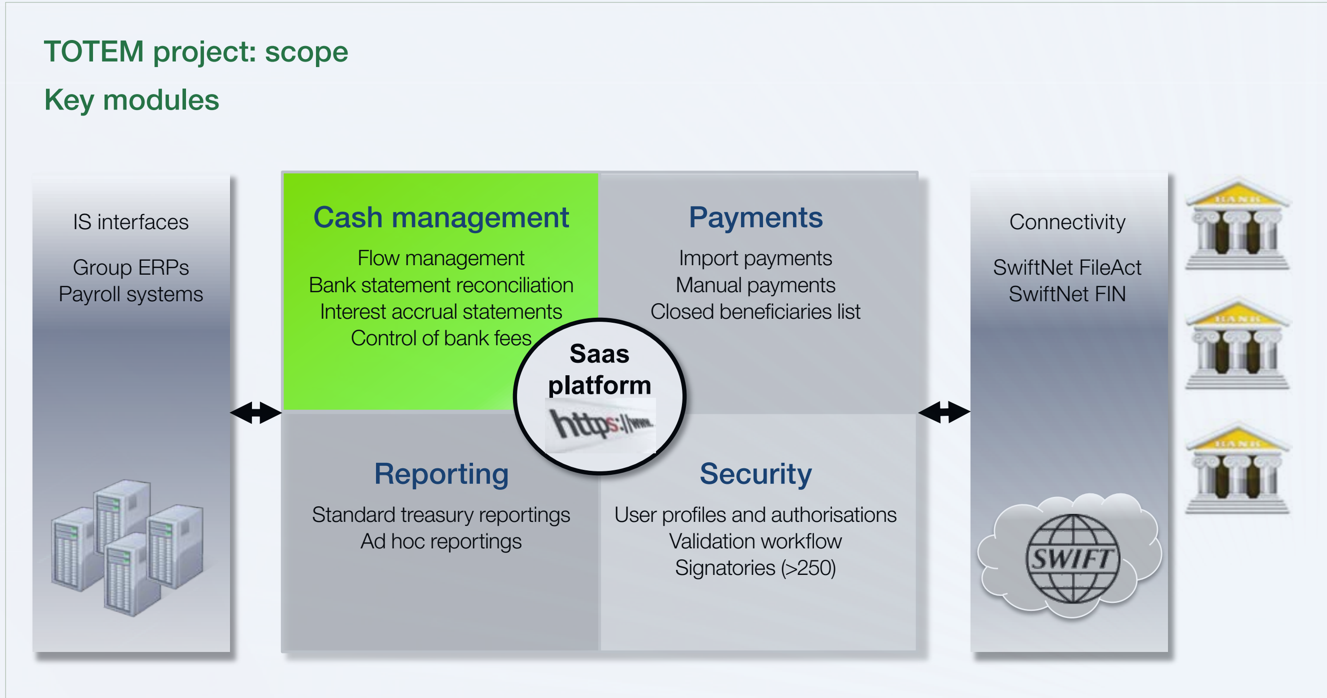
As Hamon outlined, the all-in-one Saas platform offers the company a number of benefits, including: automatic forecasts after payments; integrated reporting statements and automatic controls over bank details. The core treasury team manages user access and profiles for the platform, meaning that they can be updated as and when necessary, with no delay.

In addition to the platform, the implementation of a centralised database with secure web access means that updates, disaster recovery planning and backups are no longer the treasury function's responsibility. Also, multiple treasury staff can access the database simultaneously. And due to the cloud nature of the solution, payments validation is now both mobile and flexible.

Moreover, having a standard technology tool worldwide has led to better communication amongst treasurers and more reliable treasury reporting at Valeo. Benchmarking of best practices has also become far simpler with the new set-up, according to Hamon.

Lessons learnt

But, of course, garnering the benefits of the TOTEM project meant overcoming a number of hurdles along the way – and these provide interesting learning points for the wider treasury community. Take, for example, the fact that XML is not actually standardised. As Marie Laurence-Faure, Head of Marketing Product Channels at BNP Paribas explained during the connectivity workshop, despite XML being a standard in its own right, there are often small differences in fields and options at a national level and SEPA XML is a good example here. Certain banks may also use XML differently.



Source: Valeo

To mitigate any such confusion or complications caused by potential XML inconsistencies, Hamon had consultants lead a workshop with all of his banking partners to get them on the same page. Other key lessons Hamon learned from the TOTEM project included the need to have: a single named point of contact at each bank, as well as one SWIFT SCORE contract by bank; a strong co-ordination plan to ensure all stakeholders are involved and on-board; and a rigorous testing programme with local experts to ensure all local specificities are covered and that the set-up works in all environments.

With a limited budget and timescale to implement TOTEM, Hamon also explained that success was ultimately dependent upon his team remaining focused solely on the defined scope of the project.

Security is paramount

Additional advice given by Hamon during the session centred largely around improving security in treasury systems. He suggested four key action points:

1. **Control your data**. This not only means protection through means of firewalls but the activation of automatic controls in the ERP.
2. **Secure your workflow**. Segregation of duties will be vital here, as will internal controls.
3. **Connectivity**. Use the robustness of the SWIFT network to improve reliability. Where possible, remove any unnecessary actors from the connectivity loop.
4. **Define service level agreements**. This is particularly important for the TMS. Pinpoint where backups will be hosted. Outline expected levels of response time when problems arise. Ensure you have a 24/7 hotline number for all regions – and that the necessary languages are spoken by hotline staff.

Going forward, Hamon's team will be investigating 3SKey as a means to further improve its security processes.

The future of connectivity

According to BNP Paribas' Faure, mobile technology will continue to gain traction in the corporate treasury field. And this will stretch beyond simple payments verification to wider cash management tasks, as well as treasury-related information. To illustrate this point, Faure explained that the new Cash Management Atlas app from BNP Paribas provides comprehensive cash management information on 48 countries globally. This includes information on permitted pooling techniques, payment and cash management instruments in use, clearing systems, the tax and regulatory environment, and local market practices.

Other connectivity innovations that will positively impact the treasury landscape in the near future include the ongoing development of additional bank-agnostic messaging systems, such as SAP's financial services network (FSN). While the panel felt that the SAP's FSN would not present a threat to SWIFT as such, the development of FSN was widely viewed as beneficial for corporates and banks alike.

Additional key connectivity trends identified by the panel included the outsourcing of activities to banks or vendors. Where companies recognise that they do not have the necessary expertise in-house, there is a growing move towards leveraging strategic business partnerships to provide specialist knowledge or services, said Faure. This might range from reconciliation services to data transformation. Citing an example here, Hughes noted that to overcome the issue of 'local flavours' of SEPA corporates can use solution providers, especially SWIFT service bureaux, to act as hubs connecting them with their banks and providing data transformation services to ensure STP.

Elsewhere, for Hughes, the emerging use of predictive analytics in improving the accuracy of cloud-based cash forecasting is another development to watch. He also drew attention to the adoption of payment sanction filtering by corporates. While banks retain ultimate regulatory responsibility for AML, he explained, corporates are starting to see the benefit of screening their payment instructions before submission to banks, thereby reducing the number of false positives that banks have to handle and minimising any reputational risk issues for their own entity.

Faure, on the other hand, highlighted reconciliations as a significant area of connectivity focus in the immediate future. The ultimate goal of straight through reconciliation, she said, will require deep, process-level, integration between corporate clients and their banks – but the continued move towards treasury centralisation should help to foster this. Virtual account solutions will also help to smooth the path towards automated reconciliation, helping to eliminate errors and reduce the need for manual intervention.

Finally, Hamon brought the session to a close with some simple yet powerful advice for his fellow treasurers: strive for continuous improvement. No matter how good your connectivity set-up is, he said, there will always be room for improvement – and that is what makes it so very interesting.

(Left to right) Marcus Hughes, Bottomline, Marie Laurence-Faure, BNP Paribas, Thierry Hamon, Valeo, Eleanor Hill, Editorial Director, Treasury Today

2014

CORPORATE TREASURY & CASH MANAGEMENT **CONFERENCE**

Thursday 6th November

Gibson Hotel, 02 Point Village, IFSC, Dublin 1, Ireland

www.corporatetreasury.ie

Conference Treasurer **Speakers**

Dympna Donnelly

VP Treasury, SAP

Niall Kelly

Head of Group Treasury, DCC plc

Colm Moriarty

Group Funding Manager, ESB Group Treasury (current IACT President)

Sean McKeon

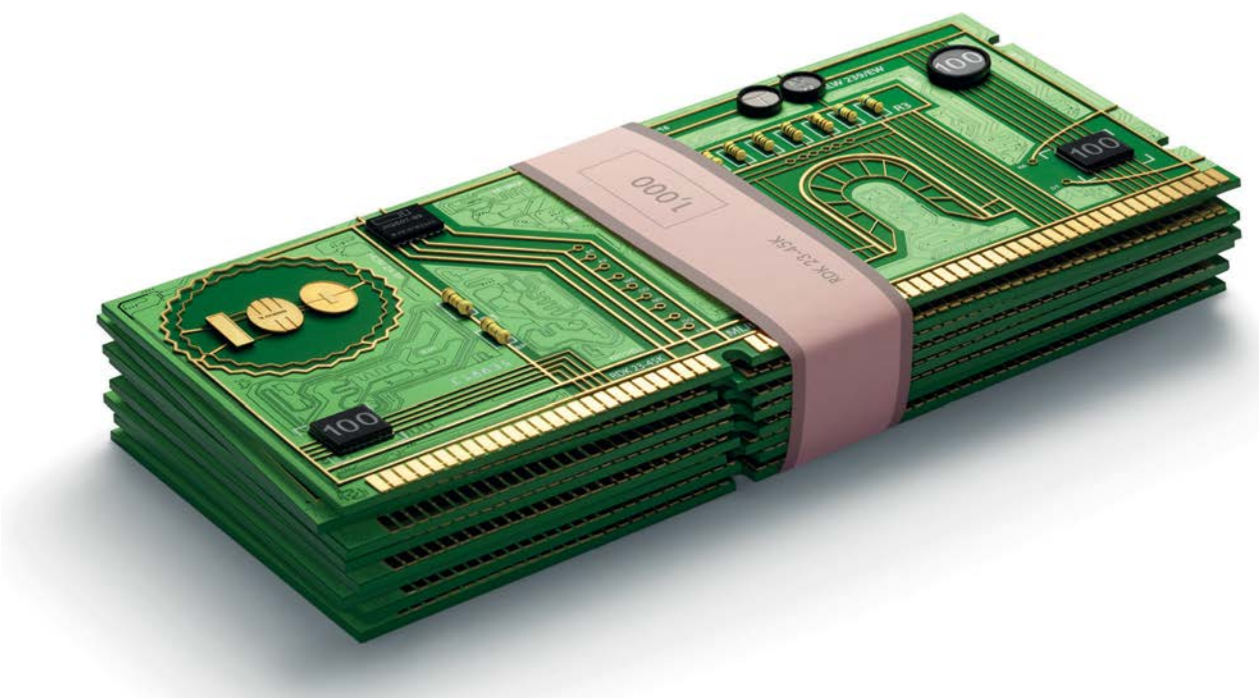
Chief Financial Officer & Company Secretary, Dalata Hotel Group plc

Lorcan Travers

Senior Manager Investment and Treasury, Johnson and Johnson European Treasury Company

tel: + 353 1 524 2375
email: info@summitfocus.com
www.summitfocus.com

SUMMiT FOCUS
PLANNING PROMOTING PRODUCING



In the future, data will be the most valuable currency.

Dollars are digital, Sterling silicon and the Renminbi is wireless. The volume and complexity of transaction data is accelerating across markets, time zones and currencies.

HSBC provides the technology to help international businesses manage global currency flows and complex supply chains.

On the ground in over 70 markets, we have the infrastructure and data management expertise, combined with online solutions, to optimise working capital and deliver to the bottom line.

Discover more at www.hsbcnet.com

Issued by HSBC Holdings plc. on behalf of the HSBC Group members which are regulated in the jurisdictions where permitted. Approved for issue in the UK by HSBC Bank plc. AC24782