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July/August 2015

Back to the future

The European Commission has set out proposals to establish a Capital Markets Union across its member states. If the proposals are successful, will the European financial system really be less bank-reliant in the future? Also, what role will FinTech play in making this happen? Treasury Today investigates.

The Corporate View

Mariano Tannenbaum

Corporate Treasurer
Arcos Dorados

Women in Treasury

Ciar Timon

Senior Regional Treasury Manager
Honeywell

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Understanding commodities finance

Bigger Picture
The legacy of Charles E. Merrill


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treasury issues
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Women in Treasury: not just for girls

It's a standing joke that the industry needs a 'Women in Treasury' initiative because every day at the office is just like a 'Men in Treasury' forum. And whilst one of the drivers behind Treasury Today's pioneering Women in Treasury campaign – which began in 2013 – was, and still is, to give women in the (male-dominated) profession greater recognition and a platform for inspiration, as counterintuitive as it might seem, it's not all aimed at the fairer sex.

In fact, we recognise that instilling a true gender balance in the treasury community means bringing men and women together to better understand the challenges that stereotyping or biases can give rise to within a corporate treasury environment. Rather than focusing on the negatives of outmoded ways of thinking, however, Women in Treasury is about building the best possible team and working environment by embracing diversity. That's why we're encouraging all treasury professionals – regardless of gender or job title – to attend this year's London Women in Treasury Forum, to be held on 10th September.

The event starts at noon with a pre-lunch networking drinks reception during which Angela Berry, Group Publisher of Treasury Today, will present a summary of the findings of our 2015 Women in Treasury Study, supported by RBS. This will be followed by lunch, during which a lively and no doubt controversial panel discussion will take place, focusing on the key issues highlighted by our Women in Treasury Study.

This year's panellists will include: Christine McCarthy, Senior EVP and Chief Financial Officer of the Walt Disney Company (Christine is also our Adam Smith Awards Woman of the Year 2015), Debra Todd, VP Global Treasury Services, BP and Jennifer Boussuge, Head of Global Transaction Services, EMEA, Bank of America Merrill Lynch.

Everyone attending the Forum will have an opportunity to put their own questions to the panellists, as well as joining in the wider discussion, and networking with their peers. And previous years' attendees will testify that for just a few hours of your time, the return on investment from this event is significant.

We look forward to seeing you there.

Book your place

If you or a colleague would like to attend the London Women in Treasury Forum, to be held at Plaisterers' Hall on 10th September, please contact our Head of Events, **lisa.bigley@treasurytoday.com**, for further information.

Alternatively, visit **treasurytoday.com/women-in-treasury/2015/events/london**

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Europe heads back to the future

In February this year, the European Commission (EC) set out proposals to establish a Capital Markets Union (CMU) across its 28 member states; a move that it is hoped will precipitate a major rebalancing of financial intermediation across the continent. But if the EC really wants the idea of a pan-European capital market to become manifest, it had better make sure it considers the powerful role that FinTech might play in making that happen.

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Ciar Timon

Senior Regional Treasury Manager

Honeywell

Although Ciar Timon, Senior Regional Treasury Manager at Honeywell EMEA Treasury, credits an early move into finance to being in 'the right place at the right time', in this interview, we discover that her success is largely down to an honest and hardworking attitude in an increasingly challenging workplace.

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The Golden Age of treasury?

Although corporates are operating in a world of tighter regulation and financial and political uncertainty, creativity in the treasury department is arguably at an all-time high. The annual Treasury Today Adam Smith Awards is thus perfectly poised to capture the essence of this moment; and to bring together some of the world's most inspirational treasury teams to celebrate all that is great about this profession.

in association with Bank of America Merrill Lynch

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Smarter Treasury

The art of the possible: future opportunities for treasurers

in association with HSBC

The art of the possible: future opportunities for treasurers

In recent years, treasurers across Europe have been faced with a constantly changing landscape. Increased regulation and tighter controls have seemingly ramped up the pressure and risk for treasurers. But as new developments in the European landscape unfurl, the smarter treasury operation can position itself to benefit from the very thing that others may fear.

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Safety in numbers

M&A deals are on the up in every region; 2014 saw M&A activity across the globe reach its highest tally since the financial crisis. What are the important legal, financial and organisational factors in making a deal and what role can the treasurer play to ensure success?

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The latest famous financial figure in this series is Charles E. Merrill, the man who brought Wall Street to Main Street. Merrill was one of the first New York stockbrokers to appreciate the importance of selling stocks to retail investors by providing sound financial advice.

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Mariano Tannenbaum

Corporate Treasurer

Arcos Dorados

In the treasury world, Latin America is a unique region with particular challenges. These range from infamous regulatory complexities to market volatility and the challenging treasury recruitment market. Although these might make the treasurer's job that bit harder, according to Mariano Tannenbaum, Corporate Treasurer at Arcos Dorados, the world's largest McDonald's franchisee, it also makes the job that much more fun.

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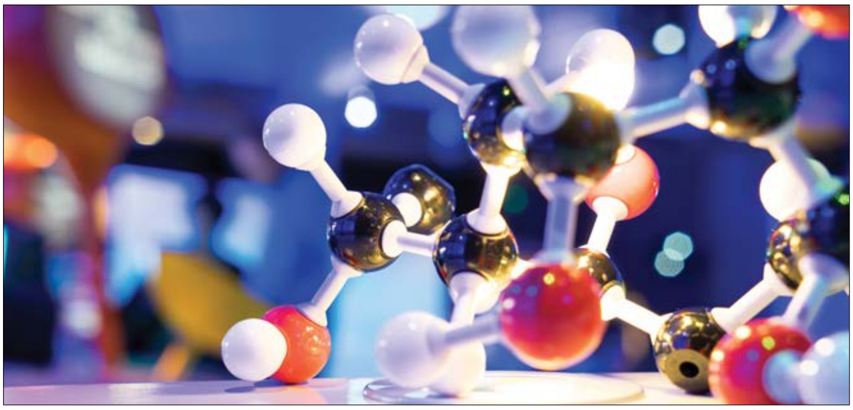
Structuring commodities

History is littered with examples of the transformational power of commodities. The Californian Gold Rush of the 19th century, for example, converted a handful of small frontier settlements on the US West Coast into big cities as hundreds of thousands of people travelled from around the world to make their fortune. In this article we explore the unique world of commodities financing.



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

Is it time to increase your political risk insurance?

There are some major political risks currently facing multinational businesses, including European elections, Russian trade sanctions, continued unrest in the Middle East, and resultant oil and commodity price fluctuations. In the light of such volatility, more multinational companies are purchasing political risk insurance to protect shareholder value, support growth in foreign markets, and help secure financing from lenders. But some companies are reluctant to discuss such risks until they pose an immediate threat; it is after all a cost that may not be needed. As with all insurance products though, it plays on the fear that by the time an event has escalated, it may be too late.

Watching the markets and issuing frequent reports is Marsh, an international credit insurance broker, specialising in helping businesses to manage risks such as political violence, government breach of contract, sovereign or commercial default, expropriation of investments or assets and currency inconvertibility. Its latest report, 'Political Risk Market Update' published in June, argues that corporate Boards and risk managers should consider how they can protect shareholders from potentially catastrophic exposures, including political risk, which can rapidly evolve from a small-scale event into a large-scale crisis, potentially across multiple countries.

Now is the time

"A just-in-time approach to political risk can leave a company highly vulnerable when it needs coverage the most," says Evan Freely, Marsh's Global Credit & Political Risk Practice leader. "Instead, multinational companies should plan ahead and take advantage of buyers' markets when they develop." He believes it is important for organisations that have not historically purchased political risk insurance to consider doing so now as the marketplace is currently favourable. And for companies that already purchase coverage, now may also be a good time to consider expanding a political risk insurance programme.

Despite growing concerns about global political and credit risks and a recent increase in loss notifications — which will likely translate into some losses for insurers later this year — insurers generally view political risk as an attractive line of business in which to compete, notes the report.

Extra market capacity

Capacity in the political risk marketplace has steadily increased over the last decade, particularly since the financial crisis, the report also notes. Globally, Marsh says market capacity now exceeds $2bn for a single policy, nearly double the available capacity just six years ago. "This increased capacity reflects a shift away from traditional property and casualty lines toward more profitable specialist classes of insurance. Insurers are finding those revenues in political risk insurance and other specialty lines that generally do not correlate with swings in the overall commercial insurance market."

"The global political risk landscape continues to be shaped by falling oil prices, geopolitical tensions, and regime change, whether as a result of constitutional elections or otherwise," says Freely. "But these trends have not yet translated into catastrophic losses for insurers. Combined with the lack of profitability in more traditional insurance markets, this has led many insurers to essentially 'double down' on their investments in political risk."

BNP Paribas takes on RBS customers

When RBS announced that it would no longer offer cash management and trade finance services outside of the UK and the Republic of Ireland, thoughts immediately turned to the question of what the next step would be for its corporate clients.

Many of the bank's larger multinational clients in the affected markets would, undoubtedly, be running their own RFPs. But what about the bank's other clients – midcaps and SMEs, for instance – that perhaps lack the same abilities and resources? Would the bank be doing anything for them to smooth their passage to finding a new transaction banking partner with the right products, people, capabilities and geographical footprint?

In July, following a competitive tender and due diligence process, RBS announced that it had selected BNP Paribas to act as a 'referral bank' for its cash management and trade finance clients affected by the scale back in its global operations. Speaking to Treasury Today, Marc Townsend, Head of Global Transaction Services (GTS), RBS explains that, under the terms of this agreement, it will be taking steps to simplify the transition process for clients wishing to migrate to BNP Paribas in order to minimise the disruption to their business.

"We were looking to see how we can best continue with our overarching responsibility to treat our customers fairly and, to that end, we have been looking at former competitor banks that operated in our space who had a similar product offering to us, operated in similar geographical locations, and had the appetite to take on RBS's affected GTS customers," says Townsend. "BNP Paribas will be doing their own KYC checks and their own credit checks. We are going to make it as easy as possible for the customer so that they have as smooth a transition as possible."

BNP Paribas, who Treasury Today understands were specifically identified by RBS as having the international reach, product offering and people to match the needs of their existing client base, say they will also be taking steps to ensure that those who choose to take their business to them will experience the simplest possible transition. "With this referral agreement with RBS, we have already invested in a dedicated onboarding programme to facilitate a simplified migration process and will continue to invest in the development of our cash management expertise alongside our colleagues on the trade finance side," says Pierre Fersztand, Global Head of Cash Management at BNP Paribas. "Our networks are joining forces to welcome, onboard and serve these new clients."

Beginning in early July, RBS will be calling all of its head office customers to inform them of the bank's plans and, in addition to that, talk them through what this will mean to them. "We will explain to affected Global Transaction Services customers that we are going to be issuing notice to them; and, should it be of interest, that we have this referral agreement in place with BNP Paribas," adds Townsend. "We are going to help and assist in every way we can. It is very much a case of us supporting our customers, helping them in any way we can, but it is always the customer's choice and it is our responsibility to support them and treat them fairly. We take the complexity of their arrangements into consideration. We think BNP Paribas is an attractive proposition to our customers, and if they want to take that option then it is available to them."

Basel III: counting the cost

How many corporate treasurers feel that the Basel III reforms are set to negatively impact the pricing and availability of the services and solutions they receive from their banks? According to the results of a recent survey, the answer is a very large number indeed.

The latest EuroFinance Basel III Index, published at the end of June, shows that over a third of the 227 treasury executives surveyed feel that the pricing and availability of their banking services have been negatively impacted by the regulation. Meanwhile, a further 48% expect they will deteriorate more in the future.

What might have been an interesting additional question for the EuroFinance team to put to the treasurers is whether they accept those extra costs on loans and other banking services as a fair trade for a banking system that's safer and more resilient than it was before.

If a safer banking system is indeed what Basel III has accomplished then one would expect many would do. But has it made the banks more resilient? Perhaps treasurers will be reassured to hear that Moody's thinks that it has. While acknowledging that the price of loans and other banking services are likely to rise as banks endeavour to bolster their balance sheets, the report 'Liquidity and Funding Considerations' published in June by Moody's says that any negative impact from that should be offset by a banking sector less vulnerable to the kind of market turmoil we saw back in the autumn of 2008. The ratings agency doesn't therefore see any impact on corporate credit ratings stemming from the new regulatory environment.

"The measures can be broadly viewed as beneficial to corporates, in that they will improve the banking system's stability and could reduce the severity of credit constraints by banks over economic cycles," says Carlos Winzer, Senior Vice President, Corporate Finance Group, and a co-author of the report. "However, it could also mean that banks will increase pricing for their services or possibly leaving unprofitable lines of business, while in some cases issuers could find it more difficult or costly to obtain debt funding."

Five areas are identified by Moody's where Basel III could affect relationships between corporates and banks including: arranging undrawn backup lines; accessing debt capital; managing surplus liquidity; arranging other banking products; and concentration of banking relationships.

Challenges and opportunities

For treasurers, much of this can be looked at both in terms of challenges and opportunities. The challenges are in finding ways to address the various implications on their business. The big opportunity is to use these challenges as a spur to drive meaningful change through the department: to find ways of making working capital efficiency gains, to diversify their funding sources, experiment with new liquidity management products. If treasurers can do all of these things then maybe, just maybe, they will conclude, when looking back in a few years' time that yes, the additional costs were worth it after all. ■

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

This much I know

Ciar Timon

Senior Regional Treasury Manager

Honeywell

Do you feel that women bring something different to the needs of treasury?

Everybody – whether they are male or female – stamps their individual personality on each role they undertake. I believe that the trick is to show confidence while endeavouring to exclude ego and I think that many women can do this very well. Moreover, I think women are more likely to be cautious and to consider the bigger picture before proceeding with any decisions.

What more can treasurers, male or female, do to make their voices heard within their organisations?

Within a treasury department, it is important to anticipate difficulties and risks. Successful treasurers will proactively flag these up to key individuals and departments. In addition, they should also aim to find solutions to potential problems – before they occur.

Not least because of current political uncertainty in many regions, treasury managers should be aware of changes to economic and banking environments as these will inevitably present different types of challenge. They need to share their knowledge and experience to demonstrate that they can provide alternative solutions when normal processes may not be possible.

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

A crystal ball! In my role, I'm often asked to predict events far into the future (sometimes beyond what the banks are prepared to predict), so this mythical tool would be invaluable.

Is there anything you would do differently in your career path to date?

I originally qualified as a secondary school teacher but, given the economic situation at the time, it was difficult to find a full-time teaching role. However, I seized other available opportunities, which, over the years, took me down a number of interesting and fulfilling paths. Accordingly, throughout my career, each role I have undertaken has led to other equally interesting and challenging positions. So, to answer the question, there isn't anything I would have done differently.

Finally, do you have a motto in life?

My policy is never to stop learning. I believe that, by taking an active interest in ideas beyond your current environment, you can extend your reach. Everything I've learned in my life so far has added to my experience and continues better to equip me to operate in both my professional and personal lives.

"Within a treasury department, it is important to anticipate difficulties and risks. Successful treasurers will proactively flag these up to key individuals and departments. In addition, they should also aim to find solutions to potential problems – before they occur."

ON THE WEB

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

Although Ciar Timon, Senior Regional Treasury Manager at Honeywell EMEA Treasury, credits an early move into finance to being in 'the right place at the right time', in this interview, we discover that her success is largely down to an honest and hardworking attitude in an increasingly challenging workplace.

Pave the way

Honeywell is a conglomerate multinational corporation (MNC) with a diversified product base and services associated with technology and manufacturing. Back in 2002, when the company was setting up its EMEA treasury team, it presented Ciar Timon, now Senior Regional Treasury Manager, with a challenge she couldn't resist "and I've never looked back," she says. "I really enjoy working in a corporate role that enables me to interact with colleagues in every strategic business group within Honeywell and to understand the different needs of each type of business," she explains. So – what led the committed treasury manager to the role in which she currently finds fulfilment?

Although receiving her original qualifications from Trinity College in Dublin, Ireland, with a view to working as a secondary school teacher, the career path she ultimately followed certainly doesn't seem a conventional one. Once Ciar found her feet in accounting, she then followed "a circuitous route into various finance roles in Canada, Ireland and the UK from the late 1970s onwards." What is evident is that her earlier experiences remain an influence to the present day. When asked what advice she would pass on to others, her desire never to stop learning is apparent. "I would always encourage others, in order to place themselves in the best positions, to take an active interest in opportunities that can add to both their careers and personal experiences."

Ciar herself continues to devote attention to important developments in the world of corporate treasury. "It's really interesting to work in a company that was implementing one of the most important enhancements in treasury, the automation of treasury systems, earlier than most." Automation, she explains, has made a big difference to treasury in recent years – even on a daily basis. "Daily investments, for example, are all carried out via online webtools and automated instructions (MT101s) to our banks."

Tackling the regulatory headache

But, whilst talk of automation and the introduction of new concepts such as 'digitisation' attract attention, the role of skilled people in the corporate treasury function to provide insight and awareness has never been more important. In recent years, for instance, regulation compliance has become a burden that corporate treasurers must tackle head-on. "At the moment, Honeywell is making great headway in areas exhibiting high growth rates, including the Middle East (ME), which falls under my responsibility," Ciar explains.

"When we are trying to set up cash management facilities and trade facilities for subsidiaries of the business, one of the toughest challenges is dealing with local regulations. These come from central banks and from government organisations. Additionally, sometimes the interpretation of regulations by local legal firms can present quite a challenge." Ciar's role, therefore, involves working closely with Honeywell's in-country managers and legal departments in order to find a way through the issues.

And, thanks to her efforts, in 2013, she was awarded the First Class Bank Relationship Management accolade in Treasury Today's Adam Smith Awards. Speaking at the time, Ciar explained that: "Our vision is a global one – we standardise wherever possible, but with a flexible approach, which takes into account the cultural, regulatory and logistical constraints in each country."

Her continued support of Honeywell's ongoing focus on regions of high growth led to Ciar winning another Adam Smith Award in 2014, this time for regional best practice. The judges felt that the regional implementation of new cash management banking arrangements, in support of Honeywell's growth initiative, showed an agile response to the inherent risks associated with doing business in Iraq.

Emblematic attitude

Of course, like for so many in the world of treasury, she admits "things are getting busier when trying to balance professional and personal lives." Given that the pace of treasury is likely only to increase, particularly in the regions where Honeywell has been directing its efforts, does Ciar seem fazed? Not in the least. And whilst she may joke about needing a crystal ball to predict future events, Ciar certainly has the well-placed priorities and business insight to optimise Honeywell's position in the current economic climate.

In a world where nothing stands still, Ciar considers that the best piece of advice she has been given is never simply to accept the existing state of affairs. "Question everything and ask yourself 'is there a better way of doing this?' If so, then try to drive that change." ■

Ciar Timon of Honeywell EMEA Corporate Treasury is Senior Regional Treasury Manager responsible for Treasury and Cash Management activities in the UK, Ireland, UAE, Saudi Arabia, Oman, Qatar and Egypt. She has 13 years' experience with Honeywell Treasury and previously worked in various finance roles, including positions in the motor and brewing industries. Ciar holds a Batchelor of Arts Degree and Higher Diploma in Education from Trinity College Dublin.

Trading in RMB

More and more Western companies are looking at using the RMB to carry out and settle cross-border trade deals. What are the benefits and challenges of trading in RMB? Also, have there been any recent changes which will make RMB trade settlement easier?

Deborah Mur

Western Europe Head, Treasury and Trade Solutions, Citi

While Hong Kong remains the most important offshore renminbi (RMB) hub, there is now competition from Europe, including Frankfurt, London, Luxembourg, Paris, Zurich and growing numbers of Asian cities, in addition to Toronto, Canada and Doha, Qatar. The markets have broadly adopted the currency in financial and capital markets transactions, and the UK and French governments have successfully issued their own RMB-denominated bonds. The RMB is now in the top five currencies by value according to the RMB Tracker published by SWIFT, surpassing the Canadian and Australian dollars.

The Chinese currency's adoption in commercial flows for goods and services also continues its strong momentum. Initial pilots with intercompany flows have expanded to third-party payments and collections in RMB. There are clear financial and operational advantages for onshore parties, from reduced hedging and transaction costs, simpler documentation requirements and faster payment cycle times. Commercial discounts are becoming the norm for settlements in RMB, according to market sources. Entire industry sectors transacting in foreign currency with China could benefit by redenominating flows in RMB.

RMB hubs serve as conduits for transactions between counterparties onshore and offshore for both commercial trade and financial purposes. Hong Kong has maintained its competitive edge with the largest pool of liquidity from retail and wholesale RMB deposits and financial products in RMB. Initiatives such as extended clearing hours for real-time gross settlement in Hong Kong to cover business hours in Europe and North America, and the Hong Kong-Shanghai Stock Connect, denominated in RMB, supports continuing growth in value and volume of RMB transactions.

Some of the hubs will play a role in facilitating specific RMB flows in their respective markets. The RMB leg of foreign exchange flows in London may be convenient to settle through that city's hub, if London's financial community fully supports it and participates. Likewise, the flows through the Luxembourg hub might be highly correlated to the investment funds business.

The challenge for China is the RMB user-experience. While economic considerations will be the main drivers, the RMB also needs to be as user-friendly as other currencies for adoption to continue. Provided that simple and clear payment instructions can be exchanged, processing time frames and value dates are defined and respected, the risk factors are clear, and transaction costs are minimised, adoption of the RMB should continue.

There is great anticipation from all parties for the China International Payments System (CIPS), which is expected to streamline the current process for global payments denominated in RMB by connecting to the China National Advanced Payment System (CNAPS), a domestic payments infrastructure platform. It is likely to reduce the flows through all but the largest hubs. The launch date for CIPS has still to be confirmed, but People's Bank of China and other Chinese banks are working diligently to upgrade CNAPS and simplify and standardise the routing instructions. The RMB needs operational efficiency as part of its global march towards internationalisation.

Cyrus Daruwala

Managing Director, IDC Financial Insights

The RMB is now the most active currency used by Asia for payments with China and Hong Kong. From 2012 to 2015, the Chinese currency moved from position number five to the top currency used in Asia Pacific to do business with Greater China. On average, 31% of payments in Asia Pacific with China and Hong Kong are now made in RMB. This growth is driven by the increase of RMB usage in most Asian countries to trade directly with China and Hong Kong. The new appointments of four clearing centres (South Korea, Malaysia, Thailand and Australia) within the region should also have a positive impact on RMB adoption, solidifying the important role of the currency within Asia Pacific but also abroad. Overall, the RMB remains the fifth most active currency for global payments, accounting for 2.07% of payments worldwide in 2013.

International usage of the RMB is in its early days. However, there are many benefits to be achieved through the liberalisation and promotion of the use of RMB beyond China's borders. Chinese corporates, in particular SMEs, can use RMB for cross-border trade instead of a foreign currency and avoid FX costs and exchange risks. In addition, foreign corporates paying in RMB can do business with more corporates in China, thus increasing the overall size of trade.

Large corporates can manage their RMB more globally and, over time, diversify their assets and protect against depreciation of one currency. From a macroeconomic point of view, a third 'world currency' could be beneficial – particularly one from Asia, in which countries could hold their reserves, especially as trade between Asian countries increases. During the recent financial crisis, banks in some Asian economies that use the US dollar experienced liquidity issues because of the increased cost of funding.

Recently, the Chinese FX market has expanded rapidly amid China's partial relaxation of its capital account and a jump in offshore RMB trading. The Chinese authorities have provided intraday funds of up to RMB 10bn to authorised institutions participating in RMB business in Hong Kong to ease concerns about CNH liquidity upon the launch of the HK-Shanghai Connect. This, along with the 'dim sum' bond market, has further opened up Chinese onshore equity and bond markets. These moves have led to greater international flows into RMB, driven by institutional investors and this jump in the volume of liquidity and foreign-market players has coincided with a reversal of bets on the Chinese currency as a one-way appreciation play.

Vina Cheung

Global Head of RMB Internationalisations, Payments and Cash Management, HSBC

Shirley Kwong

Head of Business Development, Global Trade and Receivables Finance, HSBC

Looking to the Western world, use of the RMB from a payment perspective is showing strong growth and rightly so – the benefits can be plenty. Potential price discounts continue to be the primary reason corporates choose to denominate their trade settlement in RMB. And according to HSBC's recent RMB Internationalisation Survey, some corporates are already enjoying meaningful discounts.

This year's survey also revealed two more drivers behind the decision to settle cross-border transactions in RMB. Firstly, more corporates are getting requests from their trading counterparts in China to settle in RMB. Previously, Chinese corporates were reluctant to consider their home currency but over the past few years, there's been a marked improvement in Chinese companies' understanding of the benefits of receiving payments in RMB. Thus, requests from trading counterparts in China are becoming an additional driver for Western corporates to consider RMB trade settlement.

Secondly, there is an increased interest in using the RMB to carry out and settle cross-border trade deals due to the associated reduction in FX risk and costs at both ends of the buyer/supplier chain. Using RMB becomes quite obvious when coupled with a potential pricing discount from a Chinese supplier as they can get rid of the FX premium built into the US dollar pricing. From an overseas buyer's perspective, if they are managing FX in offshore markets, they will have access to more sophisticated hedging products and greater pricing transparency if they agree to settle in RMB.

Of course, the RMB's journey to becoming an internationalised currency has not always been smooth – but the challenges can largely be categorised into three main obstacles.

One consistent challenge is educating global companies about the benefits of using RMB. Outside of China and Hong Kong, companies often have a lower understanding of the increasing liberalisation of the RMB. Indeed, one of the misconceptions we seek to address is that the aim of promoting the RMB is to replace the dollar as a settlement currency for trade. In reality, banks are providing RMB settlement as an additional currency option for companies to consider. For example, when Western corporates get a dual quotation from their Chinese supplier, their bank should be able to advise them on which currency is of greatest commercial benefit for them.

From an end-to-end operational perspective, preparing a company for the flexibility of RMB adoption means they need to take action on RMB settlement today, to ensure they are RMB-ready. Each business operation is different and being RMB-ready opens up opportunities for the future.

Another issue for corporates to consider is whether price discounts are available with their buyer/supplier relationship. Sometimes receiving dual quotations from Chinese suppliers typically used to pricing in dollars can be problematic. Price discounts might not be available in all instances and it is important to partner with a bank that is strongly positioned both within and outside China and that can undertake a benefit assessment with each client.

The good news is that recent changes are making trading in RMB increasingly easy. The Shanghai Free Trade Zone (SFTZ), for example, provides benefits for settling RMB with international markets with further streamlined processes, as well as providing SFTZ entities the choice between a CNY (onshore) or CNH (offshore) foreign exchange rate. Another upcoming change is the introduction of the China International Payments Systems (CIPS). Currently, due to local clearing systems being used to settle cross-border payments, RMB cross-border payment processing isn't considered internationally standardised. CIPS is an important infrastructure development for RMB clearing globally and is expected to launch in the later part of this year.

Finally, the potential inclusion of RMB into the IMF's special drawing rights (SDRs) is increasing confidence in holding and using the RMB for trade settlement, investment, financing, and for reserve purposes. ■

The next question:

"What can a treasurer do to maximise his or her chances of one day becoming CFO? Are there any particular qualifications or experiences that might be beneficial?"

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

Reading the signs

Slowing growth and rising interest rates in the global economy could be important signals for things to come. ECR takes a look at how diverging monetary policies, amongst other factors, across the world's various regions are having a knock-on effect on each other's economies – but not always in the best way.

A contracting US economy and weakening Chinese growth over the first quarter of this year have led international institutions to revise down their growth projections for the global economy in the past weeks. The OECD expects 2015 growth of 3.1% (instead of 3.6%) while the World Bank estimates that global growth will be 2.8% (instead of 3%). Simultaneously, bond yields have risen substantially in various countries. This combination of a growth slowdown around the world and rising interest rates bodes ill for equities and corporate bonds, which have seen price drops in recent months.

Addressing the contradiction

At first glance, weaker growth and rising long-term interest rates seem to contradict each other but there is an explanation. The growth expectations for the coming quarters to years are good and the US downturn was mostly caused by temporary factors. Over the coming period, higher consumer income and more borrowing (because consumers are growing in confidence and their net wealth has increased) will likely boost US growth. Expanding consumption will prompt businesses to up investment, as jobless rates fall and wage growth increases. This could generate an upward economic spiral in the US.

In Europe and Japan, too, growth prospects are improving. Akin to developments in the US, the Japanese labour market is tightening. This puts upward pressure on wages while incomes are on the rise. Although yen weakness and last year's sales tax are affecting purchasing power, rising asset prices are good news for consumers. A cheaper currency benefits Japanese exports.

Presently (the delayed effects of) euro weakness, lower oil prices, and accommodative ECB policy and low long-term interest rates are boosting the Eurozone economy. Asset prices rose as consumer confidence picked up. Many purchases are being made that had been deferred in the past years as businesses are more willing to invest. At the same time, a tightening labour market is a distant prospect in Europe. Consequently, the upward pressure on wage increases will be limited for the time being (except in countries such as the UK and Germany). The upside is that this will allow the ECB to continue with loose monetary policy for longer, which will stimulate the economy.

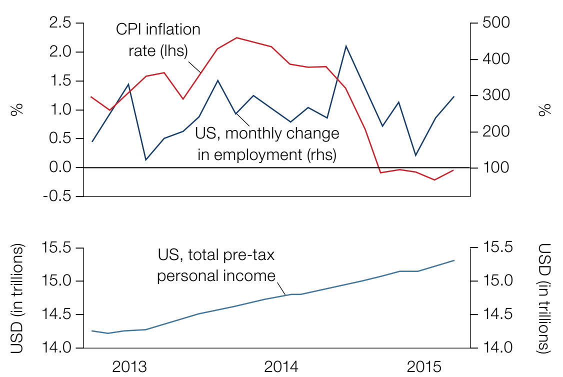
Focus on emerging markets

The Chinese authorities are taking measures to counter the growth slowdown. Recent data suggests that this is successful. However, because it would be dangerous to further inflate the credit bubble, they cannot stimulate the economy to maximum effect. This means China is unlikely to further drag down the global economy whereas the Chinese demand for resources and other import products will not increase considerably for now; it could even decline. This does not bode well for the (commodity-exporting) emerging markets (EMs). On top of this, many businesses in the emerging economies have large (dollar) debts. Presently, economic growth is slowing, the dollar is appreciating, and dollar interest rates are rising (in anticipation of Fed tightening). Therefore, borrowing is stagnant in these countries. This is hampering growth.

Monetary policy concerns

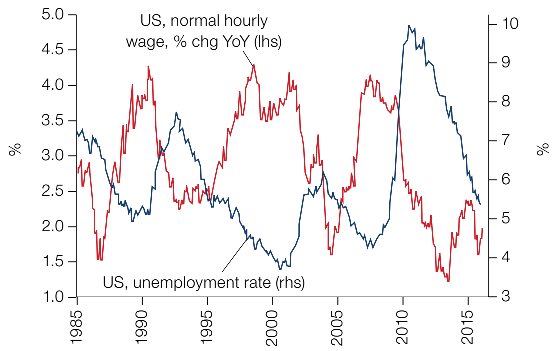
For the moment, the EMs are a source of downward pressure on global economic growth, whereas growth prospects are

Chart 1: Total income in the US has risen considerably due to an improved labour market and low inflation rate



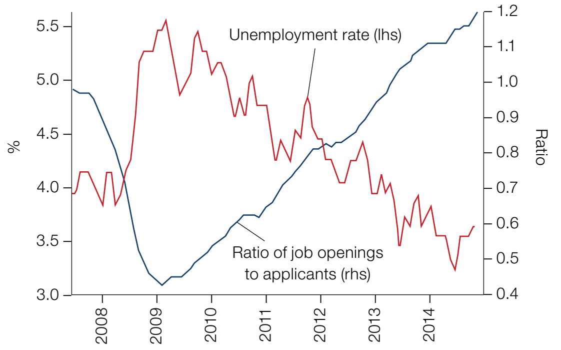
Source: Thomson Reuters Datastream/ECR

Chart 2: A further decline in the unemployment rate will push up wage growth (and inflation)



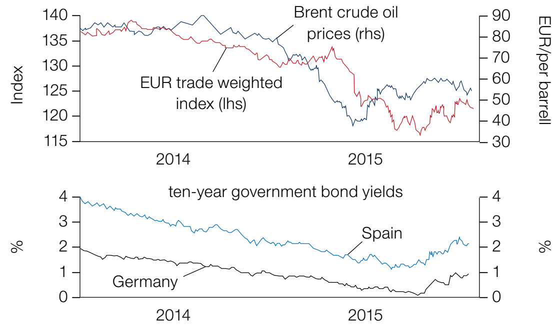
Source: Thomson Reuters Datastream/ECR

Chart 3: A tight labour market gives Japan hope on higher wage increases



Source: Thomson Reuters Datastream/ECR

Chart 4: A weaker euro combined with low rates and low oil prices will provide a boost to EMU economies



Source: Thomson Reuters Datastream/ECR

improving in the developed countries. Here, deflation fears have eased while inflation risks are on the increase. This points to less accommodative monetary policy around the world over the long term, for instance:

- In countries where central banks have immediately pulled out all the stops (the US and the UK), the economies have recovered the most and monetary tightening will start in the not too distant future. By contrast, the authorities in the Eurozone and Japan will wait longer.
- Owing to the downward pressure on growth and inflation theoretically, central banks in the EMs are in a position to open the liquidity spigots. However, we expect them to exert caution as monetary easing would weaken their currencies against the dollar. If so, dollar debts would become a bigger burden. As debts have already soared in many emerging economies, many are not keen to step up borrowing.

It is not immediately clear what effect this will have on the financial markets. In any case, a positive is that global monetary policy will continue to be loose. The European Central Bank (ECB) and the Bank of Japan will keep the money tap open, while central banks in the EMs will be inclined to ease rather than tighten their policies. As soon as the Fed or the Bank of England (BoE) increases interest rates, the dollar and/or the pound could appreciate substantially. This could act as a drag on growth in these countries. In other words, once the Fed and/or the BoE tighten their policies, they will do so gradually.

Knock-on effects

Also relevant is that weaker growth and overcapacity in the EMs could put 'the right amount' of downward pressure on US inflation. In that event, the Fed will not need to substantially tighten its policy – initially, at least. In the West, this will be good for growth and it will create more export opportunities to Western countries in the EMs. If so, the global economic growth will improve due to better growth prospects, low inflation, and accommodative monetary policy.

On the downside, ultra loose monetary policy around the world has driven stock prices beyond their equilibrium levels whereas long-term interest rates are far below equilibrium. Under such conditions, a minor deterioration of the monetary climate is often enough to trigger a trend reversal. Especially if further tightening is in the air. Of course, if asset prices plunge and long-term interest rates soar, central banks will refrain from (further) tightening at first. Even if there is upward pressure on inflation. Simultaneously, a large-scale monetary stimulus is unlikely as it would drive up inflation expectations further. In other words, many investors may have unrealistic expectations of future central bank interventions to boost asset prices.

Liquidity also gives cause for concern. Many markets have become more illiquid, due to new regulations. And there is another factor at play. As long as central banks continued to create extra money in order to purchase government bonds – which forced investors to buy more and more risky assets – asset prices kept rising and credit spreads kept dropping. There were always enough investors willing to sell their assets in order to take profit. This will change once one of the most important demand drivers in the asset markets (monetary policy) loses momentum and gradually disappears. Whereas numerous investors will want to sell their overly expensive assets, there will not be enough buyers. As a result, asset prices will plummet and long-term interest rates could spike.

Lastly, the negative implications of less accommodative monetary policy – first in the US and the UK and then in Japan and the EMU – will come to the fore over the coming quarters. The recent bond yield rally is an initial signal. Diverging monetary policies could stir up volatility in the currency markets, too. Further rising long-term interest rates and a stronger dollar are developments to be reckoned with. ■

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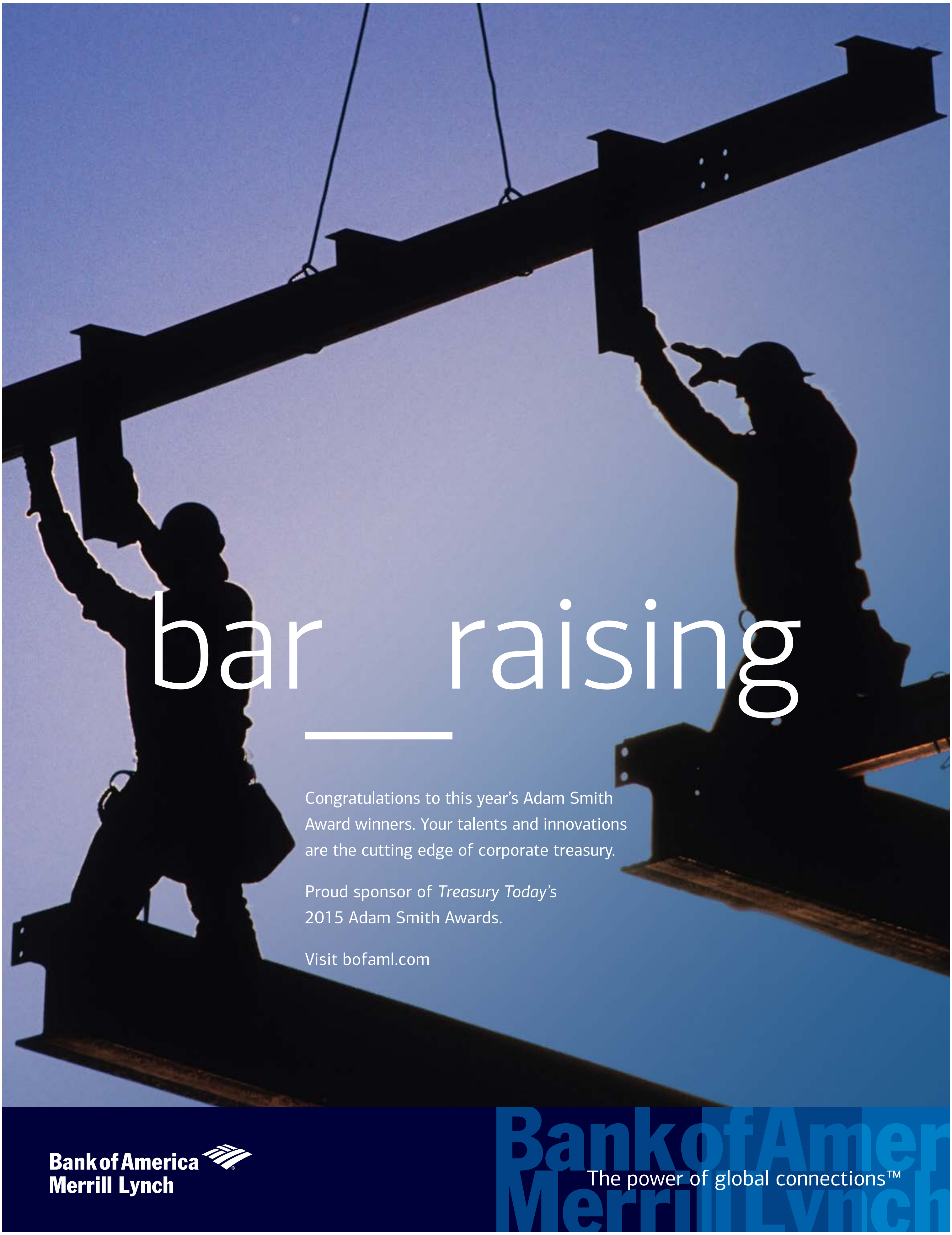

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Adam Smith Awards 2015

in association with Bank of America Merrill Lynch

The Golden Age of treasury?

Now in their eighth year of marking the pinnacle of treasury endeavour, Treasury Today's Adam Smith Awards bring together some of the world's most inspirational treasury teams to celebrate all that is worthy about this profession. There is much to celebrate as creativity continues to flourish in an environment that has seen tighter regulation and financial uncertainty unsettle the markets.

With the effort and ingenuity of its best practitioners steadying the course, today is arguably the 'Golden Age' of treasury. More regulation, more political and financial uncertainty and more risk make for a somewhat choppy ride. But for treasurers, seemingly limitless creativity, ever-increasing professionalisation and unprecedented levels of boardroom attentiveness have seen their stock rise to perhaps the highest ever level. The annual Treasury Today Adam Smith Awards is thus perfectly poised to capture the essence of this moment. For those who get to take home a coveted award it is rightfully seen as the embodiment of all they have achieved to date in their chosen profession.

Of course, industry recognition and appreciation of success have an enduring appeal. The Adam Smith Awards are more than just a pat on the back for a job well done. They are about recognising and sharing experiences amongst fellow practitioners from all levels of the profession. They are about forging camaraderie amongst a peer group that fully understands the challenges and pressures faced by each. And, ultimately, about raising standards to new levels, striving to deliver the most complete service, working with and for business colleagues in a world that is in a constant state of flux.

For this, the eighth year of the Adam Smith Awards, a record 210 nominations from 23 countries were submitted, spanning a broad spectrum of treasury activity in terms of size, industry sector and geography. The level of diversity, scope, depth and quality of these submissions never ceases to surprise as treasurers continue to push boundaries. All of this, of course, makes choosing the winners that much harder for the panel of judges. But with much consideration (and not a little anguish) the best of the best were selected across this year's 17 categories.

To bring it into focus, the Adam Smith Awards Gala Presentation Lunch, held this year on 18th June, returned to the appropriate splendour of the City of London's Plaisterers' Hall. As one of the largest and finest livery halls in London, the venue served as the backdrop to what one attendee described as, "a truly important event for the treasurers present."

For the third consecutive year, Bank of America Merrill Lynch supported the Awards. Jennifer Boussuge, the bank's Head of Global Transaction Services EMEA, said that to be a truly successful treasurer takes courage and determination. "Simply talking the talk isn't enough. Treasurers need to step outside their comfort zone and push boundaries. An effective treasury team can make all the difference between a company that simply survives and one that truly thrives." This year she acknowledged that "the bar has been set very high."

If proof were needed that the event encourages such progress, one of this year's winners – the Microsoft team led by Anita Prasad, Jayna Bundy and Shreyas Kulkarni – scooped the inaugural Best Trade Solution Award, having forged their winning submission in the white heat of discussion at last year's event (where Microsoft scooped a trio of awards and Prasad collected the Woman of the Year accolade).

"We then had a series of meetings here in London right after the Adam Smith Awards," explained Prasad. "We followed up in Finland (home of Nokia) the following week, and a year later we are live with the programme. It was very inspiring for us and we are looking forward to inspiration this year."



In the words of a winner…

Each category in the Adam Smith Awards has an outright Winner and Highly Commended Winner. The judging is monumentally difficult and nothing is clear cut except that all who progress thus far are exceptional treasury talents. Treasury Today will be presenting the individual case studies in detail as part of the 2015 Adam Smith Awards Yearbook. As a taster of what is included, here is a brief overview of selected category winners and how they stood out in an outstanding field.

Hyundai Capital America

Treasury Today's Top Treasury Team

In recognition of those who have made the world of corporate treasury that much better, the Top Treasury Team Award is a highly coveted accolade. This year it was presented to Eric Senay, Vice President and Head of Treasury and Frank Boroch, Director Treasury Investor Relations from Hyundai Capital America (HCA).

Key elements of HCA treasury's work include the diversification of funding channels to support business expansion, deepening of liquidity sources to soundly manage the inherent volatility in the business, de-risking of the balance sheet through sophisticated liability management, reduction of interest expenses through improved financial community management, optimisation of funding instruments, and enhancement of flexibility for the business to finance incremental asset classes. The bottom line of all this is that the company has reduced its reliance on bank credit lines, reduced bank charges, made significant cost savings, improved its credit rating, driven productivity gains, delivered process efficiencies, secured interest savings, and removed or mitigated risk. Quite an effort – and a substantial payback.

On being handed the award, Senay said it is "a validation of the core belief we all share that a successful treasury organisation must earn a seat at the table helping drive sustainable business growth." To do this, his team "found the courage" to profoundly change the treasury function at HCA. "We did so by assembling and developing a team capable of playing both tactically and strategically." Boroch added that the Award was "important recognition" of all the hard work and significant investment made by the company. "It is also another way for us to measure ourselves against our peers and know that we are on the right path."

Intertek Group

Best Cash Management Solution

From a simple single country/single bank solution to multi-country/multi-bank solutions, the Award for Best Cash Management Solution is all-inclusive. This year's winner, Intertek, is one of the very first European companies to be able to sweep cash from China to an account in the UK on a weekly basis. With Matthew Clarke, Group Treasurer, at the helm, the solution demonstrates an entirely new way of moving trapped cash out of China, made possible by recent changes in regulation. As part of the solution, Intertek is also one of the very first European companies to have an RMB tranche in its wider syndicated loan facility, allowing it to treat RMB just like other global currencies in its day-to-day treasury management.

"We embarked on the journey about five years ago," said Clarke. On the way, a skilled team was brought together enabling the project to come to fruition. Clarke described receiving the award as "very satisfying to attain something that is best in class." With a global treasury talent pool that is "extremely competitive," he believes it will place Intertek at the forefront when recruiting new team members.

Merck

First Class Relationship Management

Previously this award category focused on core bank relationships but it has been expanded to incorporate any relationship managed by the treasury function, such as investor relations, employee relations, ratings agencies and procurement. Notwithstanding the wider remit, Merck's Group Treasurer, Rando Bruns and his team submitted an entry that showed how well bank relationships can be managed. The submission described the goal of having all relationship banks participate in Merck's financing in order to further strengthen their relationships, whilst at the same time avoiding any 'elbow-mentality' and competition amongst them for certain financing roles. A financing strategy was developed to have a fair share of the wallet and name recognition amongst the banking group.

The plan also ensured Merck had a highly transparent syndication and take-out financing process at all times. The roles for each bank in the acquisition financing as well as the take-out financings were determined by Merck prior to announcement and signing of the credit facility. As Bruns recalls, "we were able to do so as we had arranged regular market updates and hypothetical pitches by our banks in the 12 months prior to the acquisition financing and had a very good understanding of bank's capabilities."

The Adam Smith Award, he said, is "recognition of all the hard work and dedication we put into the project," adding that it not only reflects the level of collaboration throughout the organisation but it also provides a means for treasury to show the rest of the company, which has built its reputation on creative research, that "we also can be innovative."

Honeywell

Harnessing the Power of Technology

Technology inevitably becomes a key component in many of the submissions entered in other categories, but sometimes the intelligent use of technology becomes worthy of recognition in its own right. Honeywell's Belgium-based treasury team, headed up by Séverine Le Blévennec, Director,

EMEA Treasury, have created a unique solution that truly is a masterclass in Harnessing the Power of Technology. Their project integrates the best of several technologies with customisations to fit the company's needs precisely.

"We think a lot about our strategy, our projects and the best way to use resources and this Award tells us we are going the right way," said Le Blévennec. She described the project as "a long journey for a company the size and complexity of Honeywell," but attributed its success to "vision, energy and control." She believes that the Award will help Honeywell attract the best people to the business, demonstrating that it encourages employees "to challenge the status quo and make things change." She added, that it also reinforces the view amongst senior management and the Board "that what we do makes sense."

Health Care Service Corporation

Judges' Choice

Creative and innovative treasury has been celebrated as part of the Judges' Choice Award since 2012. With a remit to look for something just that little bit different, each year the Adam Smith Awards have shone the spotlight on one submission that shows more than just a little star quality. For this year, Health Care Service Corporation (HCSC) led by David Deranek, Senior Manager of Treasury Operations and Control, caught the panel's attention.

Although HCSC submitted several entries in a number of categories, the judges felt the scale of projects undertaken warranted a most deserved winner as Judges' Choice, given the manner in which the team had gone about responding to the challenges of the US Affordable Care Act (ACA – also known as 'Obama Care') that was passed into law in 2010 and came into effect in 2014.

The solution required a three-year transformational programme, which incorporated treasury process improvements spanning treasury operations – cash management, cash forecasting, investment management, corporate governance and audit controls, treasury systems architecture, balance sheet management, business continuity practices, and most importantly, staff development and enrichment.

The completeness of this treasury transformation project embodies best practice. It allowed HCSC to restructure the staff to emulate a centralised financial services model. This now serves as a treasury knowledge centre by assigning staff-resources to their business-partner teams, providing specialised levels of treasury talent and financial support to the organisation. With this pioneering spirit, 100% of the treasury team now is deployed to support the business enterprise.

"To win the Adam Smith Award is a tremendous honour; it validates the great work we've done within our corporation, especially among the peer group we are with today," said Deranek. He described the hard work put in by the team, citing their collaborative effort as "the key to our success." He added that the Adam Smith Award creates a positive "brand image" for HCSC's treasury not just within the company but also with its vendor and banking partners.

Christine McCarthy, The Walt Disney Company

Woman of the Year 2015

In tandem with the Treasury Today Women in Treasury programme, the Treasury Today Adam Smith Awards' Woman of the Year is open to any woman operating in the corporate treasury environment who demonstrates real innovation and achievement and who is seen as an inspiration in her current role. Christine McCarthy, Senior EVP and Chief Financial Officer, The Walt Disney Company, delivers on all criteria. Describing her award as "a privilege and an honour," McCarthy says personal achievement comes from "integrity, hard work, dedication and being able to take opportunities whenever they present themselves." On a professional level, she feels success becomes very much a matter of building a strong team, something which she has clearly achieved.

She also believes that at certain points in an individual's personal and professional life it is essential to "give back what you can, when you can." McCarthy places great importance in mentoring and motivating younger colleagues, particularly but not exclusively women. She is also committed to reaching out to those still on the path of education. In this respect she offers her support to the STEM programme which encourages and develops school-age talent in science, technology, engineering and maths. She is the consummate professional.

The Golden Age?

This is just a small sample of some of the success stories heard as part of the 2015 Adam Smith Awards. In the final analysis, in spite of – or perhaps because of – continuing issues around regulation, financial uncertainty and all manner of risk, treasurers have clearly risen to the challenge. Some of their solutions, whether tackled in-house or in partnership with banks, vendors or consultants, are ingenious and will outlive any such market turmoil. So is this is the Golden Age of treasury? If it is, treasurers will not be content to rest on their laurels. As each year's Adam Smith Awards event comes around and the panel of judges are presented with the unenviable task of selecting winners, it is obvious that this is one profession that is constantly on the hunt for the next improvement. ■

in association with Bank of America Merrill Lynch

Europe heads back to the future

In February this year, the European Commission (EC) set out proposals to establish a Capital Markets Union (CMU) across its 28 member states; a move that it is hoped will precipitate a major rebalancing of financial intermediation across the continent. But if the EC really wants the idea of a pan-European capital market to become manifest, it had better make sure it considers the powerful role that FinTech might play in making that happen.

Most readers will by now be well acquainted with the story. A global recession combined with a financial crisis, followed by a more localised European financial crisis and recession, led to a deluge of strict banking regulation that stifled the supply bank credit to European firms. As access to banking channels dried up, larger corporates turned to the capital markets and, in unprecedentedly favourable borrowing conditions, drove bond issuance to new record highs. Those companies in the Eurozone that are too small to tap bond investors for funding have not, however, been quite so fortunate.

They are not small in number. A YouGov survey of 218 medium and large European companies and published by the law firm Allen & Overy in 2014, shows that 43% of corporate funding comes from banks, a figure which has changed little from the 44% that was reported when the survey was first conducted five years before. Correlation does not always equate to causation, of course. But the way that a less bank-reliant economy like the US managed to avoid the sustained malaise still affecting Europe has been used by some commentators as testimony that Europe is too reliant on its banking sector for financing and needs to beef up non-bank finance.

A capital markets union

The vision of a single European market for capital did not begin with the ideas set out in the Green Paper 'Building a Capital Markets Union', published earlier this year by the European Commission (EC). From the very beginning, the principle of free movement of capital has been at heart of the European project, shaping the policy agenda. The consultation recently kicked off by the EC, which sets out the case for the creation of a single European-wide capital market, is just the latest hopeful example of its influence on policy.

The first mention of the need to develop European capital markets was actually made in a paper written by Brussels policymakers nearly 50 years ago. It is striking to hear the similarities in language between now and then. "In all the member states, the financing of economic growth is coming to depend more and more on the capital market, and the establishment of wider markets, and close co-operation of economic policies would facilitate this growth," the report declared.

Does it sound familiar? The underlying motivation for pursuing the goal of a pan-European capital market is different, perhaps more urgent, now than it ever was before though. Back then the explicitly stated intent of capital market reform was to lay the groundwork for the unification of foreign exchange markets. Today, the single currency is already a reality. Unfortunately, though the very concept of monetary union is in increasing jeopardy as a consequence of the debt crisis in the Eurozone periphery and a far from convincing economic recovery almost everywhere else. The purpose of CMU now, then, is no longer to pave the way for the euro, but to save it.

Rebalancing finance

Reading the Green Paper it is clear that policymakers have their work cut out if they are to succeed in their ambition. A number of issues are identified in the document. These include the barriers to access the capital market, the need for sustainable securitisation activities, and the differences across legal jurisdictions that continue to impede companies who wish to issue private placements outside of their domestic market.

In a study by the Association for Financial Markets in Europe (AFME) published in February 2015, the latter, in particular, was found to be a significant impediment to investment in European companies. The AFME report, which surveyed global investors holding around €9trn assets under management, revealed that 65% of investors blame market fragmentation (lack of information and understanding of the differences across markets) for holding back investments in Europe. A further 60% cited discrepancies in rules across member states.

In the Green Paper, the EC also cites – albeit briefly – the role that new financial-technology (FinTech) companies can play in driving this integration. If one looks at these areas of focus in tandem with the banking union reforms also currently being implemented, then it quickly becomes clear what basket European policymakers are putting their eggs in. It is not with the bank-dominated financial intermediation.

"The ECB has supported research that concludes that Europe is overbanked," says Nicholas Véron, Senior Fellow at Bruegel, a European think-tank specialising in economics. "It is pretty clear that if you have a deep capital market you can mitigate this vicious circle between banks and sovereigns somewhat because you have an alternative for credit allocation if banks become impaired."

For the corporate sectors of certain countries, like the UK, that have relatively small capital markets these initiatives could be particularly beneficial. It is widely acknowledged, for example, that the UK capital market is not big enough for large UK-based corporates and, as such, many have to look to international markets when they decide to issue debt. That gives companies based in the US, for example, a material advantage when it comes to financing. So CMU, while a very important step, is perhaps more important for some countries than others.

In the digital age

If the EC and ECB are serious about making a success of the CMU initiative, however, the two bodies would be well-served to give more thought to what role new technological innovations might play in all of this. Although, as noted above, the paper did acknowledge that European law has so far "insufficiently (integrated) the benefits of digitisation," solid proposals around how to redress this issue for the benefit of digital innovators were in scant supply.

This shortcoming was highlighted in a paper published this year by the European Digital Forum, a think-tank and policy network led by the Brussels-based Lisbon Council and innovation charity Nesta. "I was really surprised to see that the digital technologies challenge was not fully addressed in the Green Paper," Sergey Filippov, Associate Director at the Lisbon Council and author of the report told Treasury Today. "What we believe, and what we say in our paper, is that it is not really possible to regulate separately for a CMU and to facilitate digital innovations in the European market."

The two ought to go hand in hand, because if the fundamental objective of the CMU is to reduce the European financial system's over reliance on the banking sector then FinTech might have a lot to offer to that end. We have seen how, in recent years, developments in digital technology have led to the emergence of new types of financial service providers and new funding vehicles (see, for instance, the rise of P2P lenders who have had such great success filling the bank void in SME financing space of late). Policy initiatives integrated into the CMU framework that would help such firms grow and intermediate more in such areas – channelling funding to SMEs who have had bank credit lines withdrawn, for example – would, arguably, be very much in accord with the CMU objectives.

As such, The Lisbon Council is calling for a "stronger technology mandate embedded in the forthcoming CMU proposals" and, secondly, for capital markets to be given a more prominent status in the Digital Single Market strategy. "The European Commission directorate-general for financial stability, financial services and capital markets union (DG FISMA) and directorate-general for communications networks, content and technology (DG Connect) should work together energetically to drive a policy agenda forward," the report demands.

Innovators and collaborators

It is important to emphasise that nobody, least of all the EC is suggesting we replace an overdependence on one type of financier (the banks) with another (capital markets investors and FinTech). It is merely that a more diverse financial system with more non-bank funding and more non-bank financial providers will be a safer, more stable system that is better placed to fund growth. The point that the likes of Filippov are trying to make is that capital markets should be for everyone: start-ups and financial services incumbents alike.

Indeed, far from seeing the rise of new digitally-enabled alternative finance providers as a competitive threat, it is becoming increasingly clear that the banking sector – or at least the greater part of it – see opportunities for themselves in the space. Disruption is, increasingly, giving way to collaboration.

"Some banks have swum against the tide, but a lot of the others are actually reacting in quite a positive way," says Filippov. "They genuinely think it is a good thing for the financial system; they can collaborate with them and access some niche market that is not their market."

We have seen numerous examples of such collaboration of late. One might recall, for instance, that in recent years both RBS and Santander have struck up partnerships with P2P lending firms like Funding Circle which will see them refer customers they have turned down for business loans. But collaboration between banks and FinTech is not stopping at investment into already established innovators. The banking industry has also been investing increasing resources into helping new financial companies with novel ideas get off the ground.

For instance, every year since its launch in 2011, SWIFT's Innotribe Start-Up Challenge has served as a venue through which start-ups can present their ideas to leading banks, financial institutions, technology vendors and other professional services providers to attract potential collaborators. SWIFT rates and screens those start-ups using a network of over 500 volunteers, bankers, consultants, and academics. They also work with a network of approximately 20 industry experts who coach those start-ups in pitching their ideas to banks.

Needless to say, Fabian Vandenreydt, Head of Markets Management, Innotribe, the SWIFT Institute and Partner Management at SWIFT, believes banks and other financial institutions have a big role to play in fostering the innovations being developed by start-ups in the Fintech space. "I think the word 'disruption' is sometimes a bit abused. I don't think many (Fintech companies) are there consciously to disrupt anything. They may facilitate some reengineering of some functions in banking but, as we have seen, many of them are also willing to work with the banks.

"Ultimately, all banks have to comply with regulatory requirements," Vandenreydt says. "They are seeing a changing landscape, however, and in areas where there are themes that they see as important, they want to do something, but often they don't have the internal resources to support it. So instead, many are opting to work together with some of these Fintech start-ups.

The rapid rise in interest in this space has been triggered by the requirements of the end customers – be that individuals or corporates – for transparent rapid, and low cost solutions," he adds. "I think what the Fintech companies do is they make building blocks that can then be assembled to address some of those requirements for the end-customers. If you take, for example, big data or distributed systems, or P2P lending, these are all building blocks that when assembled may make the life of the end-user easier. Now, whether these will be revolutionary remains to be seen. But P2P lending, clearly is starting to have traction, to the point that a lot of banks are wanting to be part of what is going on the space as well."

Many of the large international banks have also established their own FinTech accelerators. Back in 2011, for instance, Citi was one of the first to launch such a service with creation of various Innovation Labs (which now number five globally). Like SWIFT's Innotribe, the ultimate objective is to explore new ideas and service concepts and collaborate with start-ups (and the bank's corporate and institutional clients) to develop, test, pilot and launch new solutions.

"One way to think of the digital challenge is as a threat," says Rajesh Mehta, Managing Director, EMEA Region Head, Treasury and Trade Solutions, Citi. "But the other way, the way we prefer to look at it, is as a massive opportunity to provide more value added services and products to our clients. Clients are increasingly becoming more digitally savvy. Because of this, we need to consider how we can use and develop new capabilities that will benefit corporate treasurers and CFOs. Many of these clients are commenting on the dichotomy between their personal financial lives and the way their institutional banks still operate. We are working to bridge that gap."

Baby steps

Predicting the future is always a risky undertaking, but can we determine, on the balance of probabilities, the extent of the change we are likely to witness in Europe over the coming years?

AFME, who in November 2014 published a report outlining potential objectives for a future pan-European capital market, is among those who caution that the road to CMU will be a long one. Some of the issues highlighted in the EC's paper such as tax, insolvency reform and securities law will need to be negotiated with member states. This can take some time, says Paul McGhee, AFME's Director of Strategy. "It has identified some issues that are really long term. For example, in the case of withholding taxes and the taxation of debt interest relative to equity, member states are responsible for those levers. So there are going to be some big political challenges ahead."

If it were easy to reach the sort of agreements between member states then a CMU might have been accomplished nearly half a century ago when the idea was first mooted. Had that been the case the financial history of Europe might have been very different. Perhaps, as a deep, pan-European debt market developed, companies would have had a much more diverse set of funding sources to choose between. That was not to be, however, and instead Europe continued, right up until the financial crisis, to become more and more bank dominated.

Other experts agree that the rebalancing of financial intermediation in Europe will be a gradual process. "Financial intermediation changes very slowly," says Bruegel's Véron. "The dominance of the banks in Europe is so extreme that even if it was massively corrected over the next five years it would still probably be excessive. There is no way that in the course of just a few years you could have the same level of capital market activity that we see in the US, because the EU is probably the most significant bank dominated economy in the world."

But gradual though it may be, change will eventually come. Part of this transformation is likely to be policy-driven, as evidenced by the proposals set out in the EC's recent Green Paper. But part of it will also be organic, coming, as we are already witnessing, from a burgeoning FinTech sector ready to fill the void left as banks retreat from certain, no longer profitable, segments of the market.

It doesn't mean that the bankers will find themselves in any way redundant in the future European financial market. But that the sector's role will change. Just as banks play a vital role in the functioning of capital markets – as book runners or lead arrangers on behalf of issuers, to name but one example – they are, through accelerator programmes and other forms of collaboration, also becoming increasingly important to the nascent FinTech sector.

In the end, the degree to which Europe can rebalance financial intermediation will largely depend on the extent to which legislators are able to agree new rules consistent with a vision of Europe in which the free movement of capital is a central, indisputable principle. That was the vision European policymakers had for the future European financial system back in the 1960s. It remains the vision today. ■

The art of the possible: future opportunities for treasurers

The one certainty in the current economic environment is that change is firmly on the agenda. Many may equate this with increased pressure and even risk, especially where the regulatory agenda is seen as one of tighter control. But as new developments in the European landscape unfurl, the smarter treasury operation can position itself to benefit from the very thing that others may fear.

SEPA has not had an easy ride. The Eurozone took quite some time to get used to the idea of standardised payment processes. The protracted but necessary cross-border discussions between the various stakeholders ensured that many would view it as an exercise in bureaucracy not efficiency. Indeed, now that it is a reality, some are yet to embrace the strategic and transformational benefits SEPA can bring, with focus in the main on tactical implementation and compliance. The truth for all concerned is that the hard work and expense that brought SEPA into being will remain; banks, corporates and vendors need to work together to unlock its potential. For those that do grasp 'the art of the possible', a world of treasury optimisation and opportunity awaits. Not least of that potential lies in the increased scope for centralisation.

Centralise, rationalise, optimise

Companies have for some time been able to globally, regionally and domestically centralise their liquidity using a wide range of tools, such as zero-balancing and cross border sweeping. But what SEPA, and the XML data format in particular, has brought is standardisation. This gives corporates the opportunity to more readily explore the centralising, rationalising and streamlining of their accounts payable (AP) and accounts receivable (AR) processes – even combining these with their existing liquidity structure.

It is perhaps fair to say that most of the market focus, up to the point when SEPA officially went live, was on ensuring compliance and that businesses would be able to carry on with payments and collections. A lot of time and effort was expended on this and once they had made it happen, many felt they needed a break, notes Ian Blackburn, Regional Head of Commercialisation Europe, Payments and Cash Management. The value-adding SEPA benefits that were promised could wait. "I think that hiatus is now reaching an end and corporates are starting to look at how they can use that commonality."

Many businesses are reviewing their account structures and considering what operational gains can be put in place. "The promise around SEPA is that although it is not perfect, there are further chapters to the harmonisation story – with niche products and specific payment types in certain countries – customers realise that they may not have to have so many accounts in one country," says Michèle Zaquine, Senior Proposition Market Manager, Europe, Payments and Cash Management. "Businesses may not be able to rationalise as much as they'd like, but they might be able to make operational gains."

In terms of rationalisation and centralisation, SEPA has in effect become a great enabler although it remains essential to assess what is the most appropriate course of action in the light of existing business models. At the highest level, a couple of different scenarios have arisen, says Blackburn. There are companies that do not necessarily have 'bricks and mortar' outside of their home market and SEPA has allowed them more easily to reach an increased number of markets whilst retaining their accounts in one place.

Those that do have a distributed physical presence will have had the benefit from day one of potentially lower prices for payments execution. The fact that SEPA gives a region-wide standard maximum clearing cycle of D+1 (a payment execution time at the latest by the end of the next business day) has equally allowed them not only to have certainty around the timing of their payments but has also facilitated the migration of non-urgent transactions away from the real-time gross settlement system (RTGS) to D+1, bringing cost efficiencies.

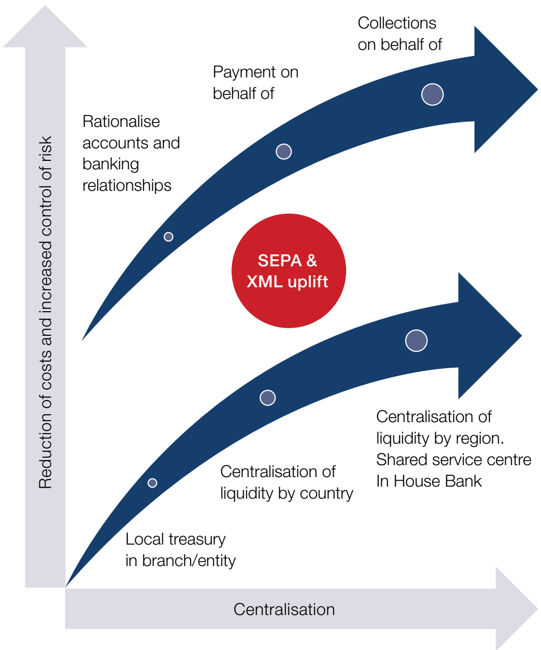
"What corporates are now looking at is a broader picture," says Blackburn. "They are asking if they really need to have as many accounts around the region, how they can reduce their account maintenance fees, and how they might be able to rationalise accounts to simplify their liquidity management." However, it may be a bit too soon for companies to consider placing all activities under one account, albeit theoretically possible under SEPA. Corporates are understandably focused on counterparty risk, which precludes the 'one bank, one account' approach. Also, for certain types of payments, most corporates would want to have accounts in-country. SEPA does not cover cheque or cash and in some markets local clearing systems – such as LCR in France or RIBA in Italy – where if a client is undertaking transactions through those mechanisms, a local account is required.

For banks, this is all part of the exercise of discussing with customers the precise nature of their payment and collection flows, and therefore whether or not certain accounts need to be maintained. This discussion may also include a technology review, considering if an existing ERP module, for example, can be enhanced to cover all operations or if the business wishes to maintain other instances of that system in-country. Zaquine comments that this has become "a much broader discussion" requiring not just an understanding of payment flows but also any issues around working capital optimisation before it is possible to use the available tools effectively.

in association with HSBC

Chart 1: SEPA, XML and treasury uplift

Treasury fit for strategic activity



Opportunities today

Rationalisation

- Borderless payments markets across Europe

Standardisation

- A common euro automated clearing house system for the SEPA zone countries

Centralisation

- Internal operations and processes
- Visibility and control with enhanced reconciliation

Working capital accelerator

- Receivable and/or supply chain financing built into efficient centralisation structures
- Visibility and control of cash positions and FX management through account and liquidity structures

Maximised cash efficiency → Optimised risk management → Automation of processes → Enhanced focus on strategic activity

Payments, collections and working capital optimisation

For companies that do opt for centralisation, even if some accounts must sit outside of that model, a business can still go a long way to optimising its processes and reducing administrative costs. "But, it is easier to centralise the payments side than the collections," says Blackburn. "Payments information is easier to track (just by extracting payment run files and sharing that information with the unit that is making the payment) whereas receivables are more challenging if the business is not able to control how the cash comes in (reconciliation is a challenge if, for example, the client does not quote references)."

There are signs that the status quo is rebalancing as the emergence of the 'on-behalf-of' model becomes more applicable to collections, facilitated by easier global harmonisation of invoice numbering. "Corporates are also keen to learn more about new banking techniques on the receivables side," says Blackburn. Of note here is the 'virtual account' concept. Here, a corporate sets up a central account, or a smaller number of header accounts, on the receivables side. Appended to these accounts will be any number of virtual account number which are uniquely allocated to each counterparty. Each payment can only be routed via the counterparty's unique account number and this always links back to the relevant main account. This offers a major improvement on the normal reconciliation process.

Other developments have been around data enrichment. Many corporates have realised that XML can be used beyond the SEPA landscape. Zaquine feels that it "really opens up the parameters for them having more useful data." Combining SEPA XML data with information from outside that process has definite advantages. "By packaging a consolidated receivables management reporting tool for customers that puts all their credit receipts in one place and on one report, it gives clients that enriched data."

By allocating this data back to their TMS or ERP system, it is possible then to start managing receipts by exception. Consolidation of information facilitates auto-reconciliation in the back office; the system is positioned to inform what has not been received and what is yet to be applied. The potential to lower overheads previously employed on sales ledger management is clear. Further, integrating data into their ERP system allows the corporate to more easily deploy that data for control, reconciliation and working capital purposes (quicker clearing cycles, reduced fees and lower overheads for allocating and matching against the sales ledger).

There is a forecasting and liquidity benefit too. If a corporate can combine the cash side with a more strategic way of looking at Days Sales Outstanding (DSO) and its payments processes, and look to reduce the cycle, this too ties in with working capital improvements. In preparing the ground for a supply chain finance or receivables finance programme that can reduce the time it takes to collect the money, there is potential for an immediate impact on cash flow. Processes such as dynamic discounting can have a similar effect.

"The centralised and rationalised treasury model is also solid ground on which to build a more robust internal governance structure," says Blackburn. Scalability of risk and control systems becomes more challenging for companies that grow rapidly through acquisition. "But those that have taken the leap and have started to centralise will reap the benefits in terms of governance and future scalability."

Further opportunities

By moving to a more centralised treasury model with fewer accounts, it becomes much easier to consider these improvements. "There are many components involved but as the corporate moves along the curve towards centralisation it will see more opportunities to manage its supply chain and business flows," Zaquine notes. "SEPA and XML are just the foundations for what can become a more optimised model." She feels that because many corporates have realised that XML is not specifically limited to payments and collections and that it is a global format that has a much wider use. Indeed, the decision by the European Central Bank (via the Euro Retail Payments Board) to press for a region-wide roll-out of an instant payments-type product (similar to Faster Payments in the UK) takes SEPA to the next level.

Specific to SEPA is the Additional Optional Services (AOS) concept. These have been permitted as a means of fine-tuning SEPA's relevance to specific jurisdictions; extended remittance information required by Finland or France's Change Account Identification. Some AOSs are very market-specific but if an AOS has the potential for full European reach then Zaquine believes it has the chance to be adhered to by other communities – but it will be the community operating as one, not an individual corporate or the banks, which will make this happen. For this reason, she believes that there will not be a flood of AOS requirements as SEPA gains momentum; they will arise only when the need arises and when the market pushes for it. The real question then around any AOS is its reachability. "If there is not sufficient reachability it will create market fragmentation," she warns.

The changing face of European payments

The whole story, notes Blackburn, then moves further beyond SEPA, becoming one of the European authorities' FinTech-driven desire to create a level playing field. Although typically consumer-driven, these technologies can quickly impact the corporate space. In addition to promoting the efficient use of existing SEPA tools (SEPA Credit Transfers and SEPA Direct Debits), concepts such as mobile and e-commerce are gaining ground as a means of enabling corporates to access information and to transact in real-time. In part, the new FinTech landscape will be facilitated by proposed revisions to the European Commission's first Directive on Payment Services (or PSD1) which now has political agreement, at least in principal, to move ahead. Subject to further discussion and final approval by the European Parliament – possibly by September 2015 for a Q3 2017 implementation – PSD2 will mainly affect access to payment accounts, liability for process failures, transparency requirements on charges, and customer authentication measures.

One of its key aspects is the introduction of a regulatory framework 'conducive to the emergence of new players' known as third-party providers (TPPs). "It is something we welcome," says Tony Richter, European Head of Regulatory and Market Delivery, Payments and Cash Management. "We recognise the need for competition; we are working with the authorities in order to make that happen." In welcoming TPPs, Richter acknowledges that existing regulated payment service providers (PSPs) need to consider how best to work with them as market participants. The PSP view of the TPP concept is not one of out and out defensiveness; indeed there are new opportunities presented. For example, there is nothing to stop a PSP taking TPP status, potentially broadening its product proposition for customers that wish to operate through this channel. Not discounting any approach, HSBC is running an "innovation work-stream" to tap into the new opportunities coming through.

On 6th May the European Commission announced its detailed plans to deliver by the end of 2016, a Digital Single Market for Europe with 16 key initiatives grouped under three pillars:

1. Better access for consumers and businesses to digital goods and services across Europe.
2. Creating the right conditions and a level playing field for digital networks and innovative services to flourish.
3. Maximising the growth potential of the digital economy.

"The objective is to open up competition in the European landscape to allow for digital opportunities to thrive within a clear framework and in the EU Single Market."

Raising the game

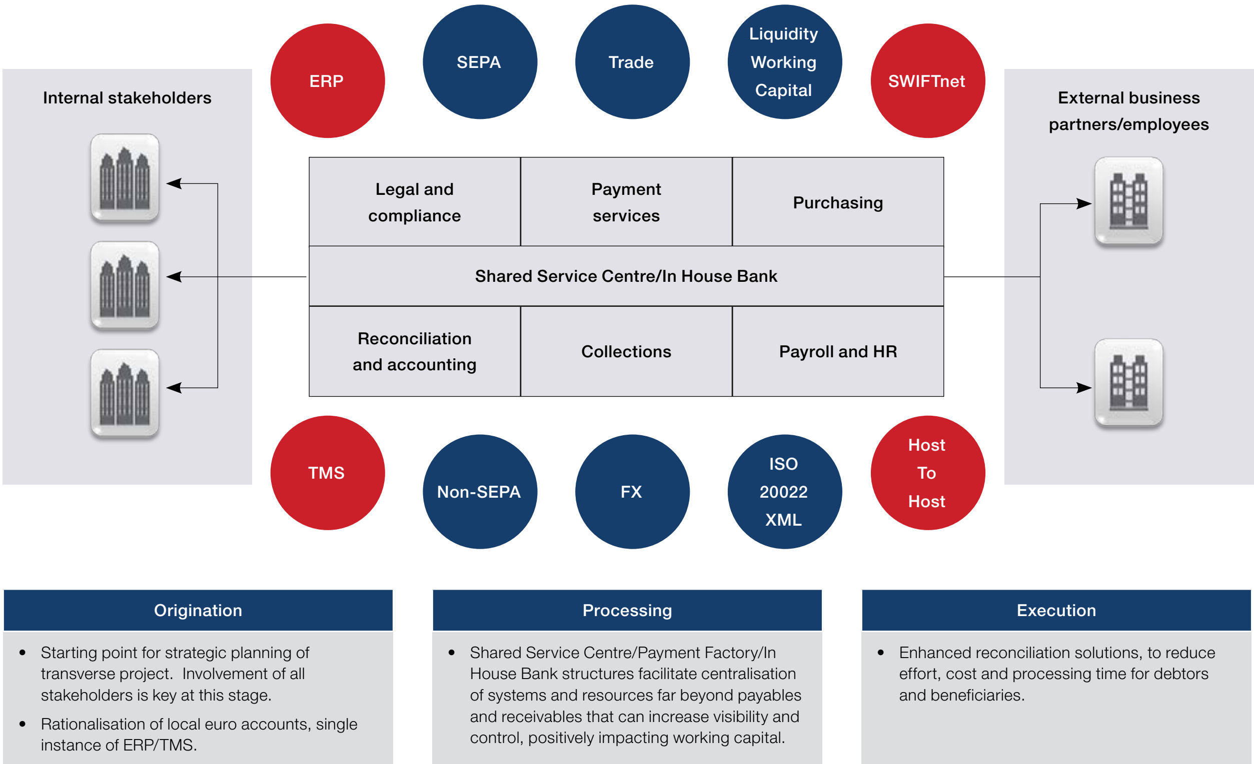
The coverage of TPPs by PSD2 is also viewed by Richter as a positive step for the overall market in that all newcomers must match the standards to which current PSPs are required to adhere. For service users, this is an important point. "We want to work with the TPPs to develop the market, but there are some areas that we must tackle together, to make sure that other issues are not introduced," he says. Changing the relationship of the bank with its customers to add, in some cases, a third party which will be transacting on behalf of the customer but over accounts maintained with their bank, demands that the new relationship has at least the same level of security.

With liability for process failure also tabled as part of the new Directive, Richter believes that if a customer has a query about a payment from their account, irrespective of whether they are using a TPP or not, almost inevitably they will contact their account-holding institution (the PSP) to seek redress. "This is a new aspect that will come into play in managing our payments business and we will need to build that into our overall proposition and processes," he notes, adding that there may be a cost associated with this. With the additional focus in PSD2 on price transparency, all PSPs will need to review how they manage any such changes. As Richter says, a bank cannot just increase prices to cover an increased cost base. "We need to become more efficient in other ways to make sure we can continue to be profitable in the market." But ultimately, this is good for the market.

Managing the broadening scope

Another area that is covered by PSD2 which needs further investigation is the so-called 'one leg out' transaction, the implications of which are "uncertain," says Richter. The PSD1 was concerned only with payments made within the EEA, involving EEA currencies. PSD2 enables transactions where either the remitting or beneficiary bank is outside the EEA and using non-EEA currencies. Whilst the reach of the Directive itself clearly relates only to that portion of the transaction which takes place within the EEA, what is not yet clear is whether a payment can in practice be managed in this way, considering the need for transparency, security and all the other demands of the Directive. If, for example, a USD payment goes from Europe to the US, how can that portion that is in the EEA potentially be managed differently to that part which is being settled in the US?

Chart 2: Centralisation: a transverse project



These changes may seem primarily to impact PSPs, but as Richter notes, they will mean changes for the relationship with the customers, particularly around documentation. "We will need to review terms and conditions," he states. "PSD1 was prepared with consumer protection in mind but also applied to corporates. Because corporates have different requirements to consumers, the option of a 'corporate opt-out' was included for certain provisions, negotiable between a PSP and its corporate customer. These must be reviewed again in light of PSD2."

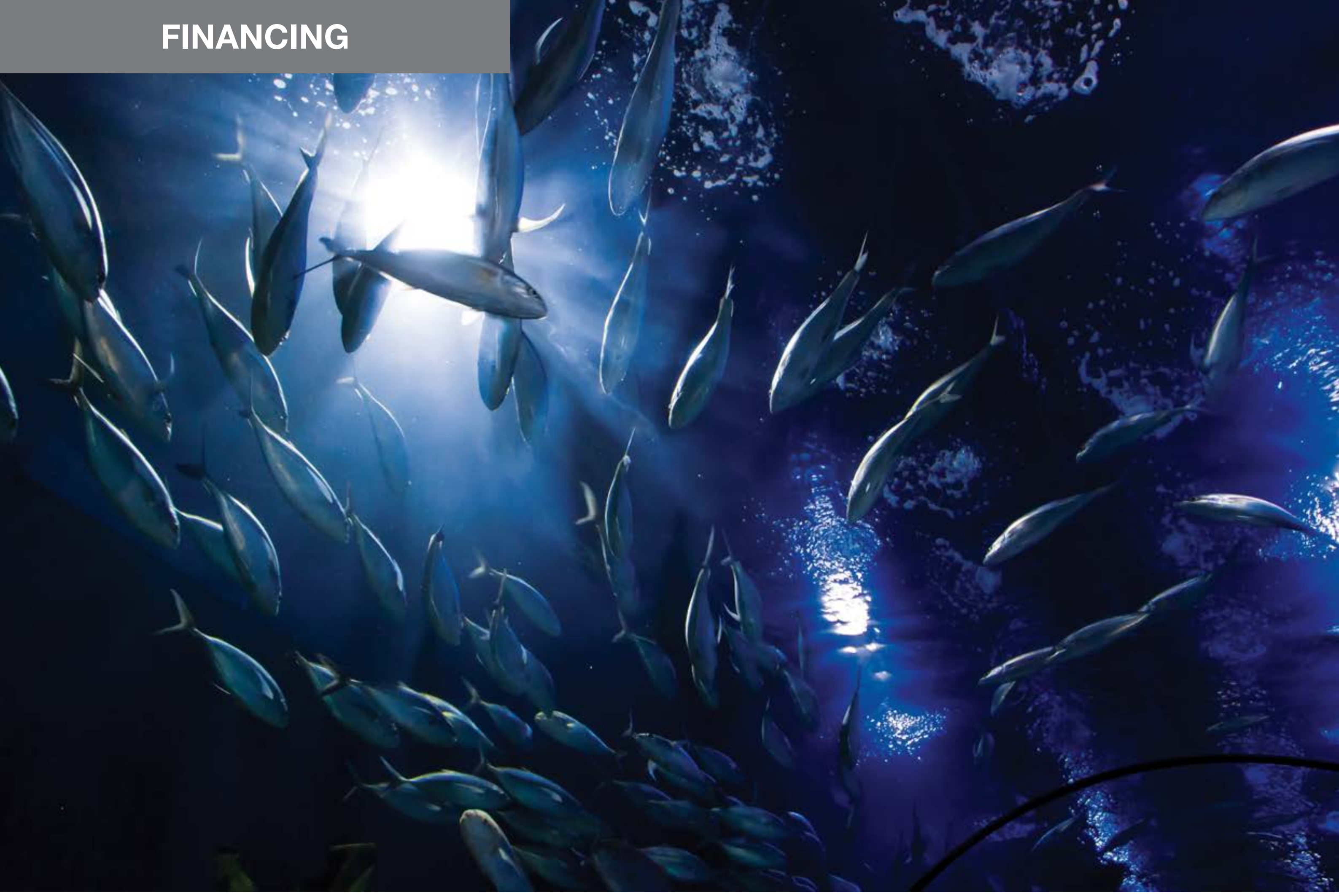
For all stakeholders, only when the Directive is in place will the analysts be able to consider the changes, both in terms of technology and processes. "We are beginning to get a feel for it but there is a lot more work to do," says Richter. The fact that PSD2 is a 'work in progress' does not however detract from the need for discussion to start now. Corporates are advised to keep a watching brief with banks such as HSBC who are well-positioned to provide market intelligence on this topic. Richter has built a team to study the "quite substantial" regulatory developments and changes in the European payments space "so that we can better work with our clients and become a trusted advisor to them." This creates a space where the bank can reach out to its clients "in a way that gives them an understanding of what's happening in the industry and the impacts that may be coming their way in due course."

Tony Richter
European Head of Regulatory & Market Delivery, Payments and Cash Management

Ian Blackburn
Regional Head of Commercialisation Europe, Payments and Cash Management

Michèle Zaquine
Senior Proposition Market Manager, Europe, Payments and Cash Management

HSBC



Safety in numbers

M&A deals are on the up in every region; 2014 saw M&A activity across the globe reach its highest tally since the financial crisis. What are the important legal, financial and organisational factors in making a deal and what role can the treasurer play to ensure success?

The point of mergers and acquisitions (M&A) is often to ensure growth and stability; in the current economic climate both are attributes that sit well with boardrooms and investors alike. Perhaps this is why the level of M&A activity has increased significantly in the past couple of years as corporates that have stockpiled cash in a low interest world seek to bring on board new customers, products and R&D effort through acquisition.

The growth of M&A itself is confirmed by Dealogic's 'M&A Review Full Year 2014'. It reports that global M&A volume reached $3.60trn in 2014, up 26% year-on-year (from $2.85trn). This was the third highest volume ever recorded, behind 2007's $4.62trn and 2006's $3.91trn. The figures for Asia Pacific (excluding Japan) show a market very much alive to the opportunities of acquisition. Although Japan's M&A volume of $74.3bn was the lowest since 2002, the region's overall figure realised a targeted M&A volume of $656.8bn: the highest total on record. China dominated with $307.4bn of deals, its appetite for acquisition not letting up on overseas deal-making activity (including many in Europe). According to data from research firm, Mergermarket, China registered a 21.3% increase in the value of its total M&A activity during 2014.

However, increased activity means more failed deals too. The FT Press book 'The M&A Paradox: Factors of Success and Failure in Mergers and Acquisitions', states that "many research studies conducted over the decades clearly show that the rate of failures is at least 50%." In April 2015, China Daily News (CDN) reported "a slew of troubled overseas deals" for the country; this exposes the increasing risks and potential losses faced as M&A activity increases.

One of the causes of the breakdown of outward bound deals is the failure of companies to fully understand the cultural, legal and political environment of their foreign target businesses. Of the 120 failed outbound Chinese deals between 2005 and

2014, CDN claimed that about a quarter were due to political reasons. The China Centre for International Economic Exchanges cites a "lack of talent familiar with international practices" as being a "major shortcoming" for Chinese companies in overseas markets. This signals the need for qualified input from a range of functions.

A legal perspective

The complexity of international commercial law is such that it requires expertise not just to get the best deal but also to avoid making potentially costly mistakes. A frequent error of judgement is to try to iron out contractual details of a merger before legal counsel has had a chance to advise on suitability. "Not involving counsel early enough can mean issues are not raised in good time which can lead to later difficulties," warns Emma de Ronde, Partner and corporate lawyer for Norton Rose Fulbright Hong Kong. Businesses are understandably reluctant to incur legal fees before they know they have got a commercially viable deal in place but agreeing to any commercial or legal terms without recourse to legal advice could ultimately prove more costly. It is often the case that once a client has sent a set of pre-agreed terms to its lawyers, it then falls to the lawyers to point out the consequences of going ahead under such terms and even try to extricate the client from unfavourable terms.

Even with this in mind, some companies may still be comfortable tackling the preparation of key high-level commercial terms themselves, only bringing in legal counsel when they want to document what has been agreed commercially. For others, there may be a need to consult at an earlier stage, particularly if there are complex structuring, legal, regulatory or taxation issues, or if there is a cross-border element with which to contend.

Of course, each deal will have its own legal peculiarities but there will be some commonalities too, notably when structuring a deal from a due diligence perspective. There will be an initial investigation of the scope of the business being bought or sold, looking at areas such as ownership, how the sale will take place and the regulatory requirements that must be met to enable the sale to go ahead. The target business will be subject to commercial and legal due diligence, typically including considerations such as its financials, business model, existing legal contracts (with key suppliers and customers, for example), employee and pension issues, intellectual property rights and, increasingly, any anti-bribery and corruption issues. The latter, notes de Ronde, is a big issue in Asia right now, especially in China. Once these point have been satisfied, the preparation of documents may commence.

In addition to the sale and purchase agreement, other documentation may include the acquisition financing agreement with banking partners, and perhaps a transitional service agreement where the seller provides services to the buyer, post-sale, for an agreed period. The final stage for counsel would be signing and completion. "Often there will be a gap between agreeing terms and completion where there may be a series of further external conditions that must be satisfied," notes de Ronde. "These may be regulatory. For example, we might need to make Merger Control filings if there are competition or anti-trust issues, or there may be conditions specifically related to the business that need to be resolved; a financial services business, for example, may require prudential regulatory approval for the sale to go ahead." Satisfaction of all conditions should lead to completion of the transaction at which stage counsel can advise on the mechanics of the transfer, guiding the new owner through a number of responsibilities it now has around filings, registrations, how it implements its own governance structure within the new business and so on.

Most developed jurisdictions with stock exchanges will have separate rules that apply to the acquisition of a listed company, notes de Ronde. The Hong Kong Takeovers Code, for example, is regulated by the local Securities and Futures Commission which governs the terms under which a buyer can acquire a listed company. It covers aspects such as the timing of the transaction, what has to be documented and what can and can't be said to shareholders pre-sale. In addition to Takeover Code rules there are also controls on insider dealing and market abuse issues that must be adhered to.

The process is far from straightforward though, the diversity of legal systems found in Asia often presenting issues for cross-border mergers. "On private deals, where parties are in different jurisdictions, each side will typically want to use the law of its own jurisdiction as governing law," notes de Ronde. Some jurisdictions might dictate the applicable governing law for transfer of a particular asset, so it is essential to be aware of local rules.

However, it is when a deal takes a turn for the worse that the real "hot debate" starts. It can be a major challenge to agree which jurisdiction will hear a claim; although arbitration is increasingly used in preference to the court system, even this raises the question of where arbitration will be heard and under which arbitration rules. It is strongly recommended that guidance on dispute resolution is tackled and finalised in the initial contract phase.

On the regulatory side, Charlotte Robins, Partner and financial services regulatory lawyer at Norton Rose Fulbright Hong Kong, notes that whilst buyers and sellers are much more aware of their regulatory obligations around M&A than they were a few years ago, some still do not think about them "fully enough and early enough." Where companies need to secure change of ownership approval from the regulator, for example, they should understand that this can take time. And where outsourcing is deployed, either at the transitional services stage or as part of the subsequent integration, it will inevitably invoke rules around the transfer of data – another hot topic in Asia.

Tackling the breadth and depth of regulation means that M&A teams will have more people and agencies to deal with. But, says Robins, it is as much about getting the timing right as it is knowing the regulators and the best approach to take with them. Whilst she acknowledges that it may sometimes be more appropriate that the business, not the lawyers, deal with the authorities, she believes that knowledge on the ground "can be key in getting the necessary approvals in the time that you need them." Ultimately, Robins feels that the diversity of legal and regulatory environments across Asia does not necessarily make M&A more difficult, "it's just different." Having the right legal counsel onside is clearly an advantage.

How can the banks help?

In terms of preparation for a deal on the finance side, there are many different dynamics to consider, explains Alexandre Huet, Global Head of Strategic and Acquisition Finance, Société

Générale. As a banker, he naturally considers it more provident for buyers to prepare well in advance wherever possible, allowing time to consult a number of internal and external advisors – including banks – who can help draw out the most appropriate deal structure. However, he acknowledges that sometimes a deal runs short of time and although this can often make the process "very challenging," a sense of urgency can help "crystallise" the terms of engagement. From a tactical point of view, he comments that a short time frame is thus "not necessarily a bad way" to approach M&A.

That said, although each deal must be tackled on a case-by-case approach, Huet believes that seeking bank advice ahead of a deal, besides early engagement with the preparation work, allows their involvement much earlier in the process on the financing side. This is of particular benefit in the case of a hostile takeover or where there are competing bids as funds "must be accessible at the point of need." Where a listed company is the acquisition target, he notes that the process will almost certainly benefit from advanced planning to head off the kind of regulatory demands seen in the UK, for example, where a buyer's proof of funds is essential for approval to be granted (it becomes a case of 'put up or shut up' in order to protect the target from destabilising exploratory approaches). On the buyer side, such a need illustrates the importance of drawing together as much information as possible pre-deal, says Huet. Treasurers obviously have a key role to play here, (whether the target is listed or not) but banks can also play a vital part in the practical management of an M&A deal, as financier or advisor (or both).

When bank finance is required it may come in many forms but a common way to fund a merger is to use a bridge loan, says Huet. This allows an interim phase that supports the bid and any regulatory requirements to prove funding. If the merger is successful, this facility can either be entirely refinanced on the bond or equity markets or subsequently partially syndicated and turned into term loans. The large corporate and investment banks that typically seek out positions as the book-runners or lead arrangers for a financed merger will steer the funding process, managing refinancing following a bridging loan or securing the participation of other banks where the loan is syndicated.

Ultimately, for Huet, if the terms are agreeable and the market supports those terms, and if the shareholders find the deal attractive, the industrial rationale is there and there is chemistry between the management team, then the deal has a good chance of success. But he accepts that there are many 'ifs' here and suggests that failure on any one of these points can reduce even the best laid plans to rubble.

The treasurer's role

Anecdotal evidence suggests that some treasurers are not involved in deals as early or as deeply as they would like or feel necessary. Just knowing the geography of a deal, for example, means being able to better manage bank relationships. Firms such as AstraZeneca, the Anglo Swedish pharma giant, know the importance of treasury involvement. It has a targeted M&A strategy to build upon its scientific work, said Ian Brimicombe, Group Head of Tax & Treasury, AstraZeneca speaking at last year's annual ACT event in Glasgow. Part of that approach demands that its treasury personnel are ready to position the function for each proposal that comes along. These ideas tend to happen very quickly because it is an extremely competitive market, he explained. "If the treasury team isn't ready to stand together with the management executing and implementing these acquisitions then we will lose out."

Brimicombe believes that treasury must adopt a collaborative stance, not only with the management teams of the business development and corporate strategy groups that formulate the ideas on what they want to buy and how they wish to implement the acquisition, but also with specialist colleagues in areas such as tax, insurance and group reporting. "It all has to be linked together in order to create a coherent finance perspective on the deals."

Finding the right seller or buyer and putting the finances in place involves much work but the failure rate of deals must be borne in mind. Tom Greene, Group Treasurer at another pharmaceuticals firm, Shire, knows this only too well.
He pointed out at the same ACT event that as a pharma company, Shire uses the acquisition of early stage products as a key source of product development. At any given time it may have up to 20 opportunities on the table, covering companies of various sizes and stages of development, without knowing which will come to fruition. "Acquisitions can be a bit like busses; there's nothing and then several come along at once."

For treasurers, not knowing about deals in advance is a disadvantage; forewarned means forearmed and being able to position finances in good time can facilitate a successful deal. "I'd rather be in the loop than outside it," said fellow panellist, Alan Dick, Director of Tax & Treasury for international engineering firm, AMEC. However, Dick also believes treasurers should seize the initiative. "It requires proactivity; you can't sit and wait to be invited to take part."

Until a deal has been completed, understandably, the level of data imparted by the company being acquired may be limited; this could frustrate the acquiring treasurer's good intentions to move forward. It may be possible to include a contractual element of disclosure post-signing but prior to completion that provides for the needs of treasury. To this end, John Grout, Policy & Technical Director of the UK ACT suggests that it should be part of the training for a company's M&A negotiators to understand treasury needs and to try to incorporate these at the earliest stage. He also suggests that whilst normal due diligence processes may to an extent be paper-based, a face-to-face meeting of respective treasurers (and between counterparts from other functions) can reveal so much more, potentially heading off any unpleasant surprises.

Communication is the key

Ensuring the timely communication of all relevant information to all the parties involved in the deal is essential. Achieving a satisfactory result may be more difficult for a business that has either not engaged in an M&A deal before or does so infrequently. This raises the importance of finding reliable advisors to supplement internal resources. Internally, treasury has come to play a crucial role as the intermediary between external bank partners and the other business units involved, acting not just as the risk advisor and efficient expeditor of funding but also as the informed challenger for any advice that is forthcoming from those external partners. Working as a team is essential throughout the M&A process; it is not a stretch of the imagination to suggest that a merger without the input of treasury could be a risk too far. ■

Charles E. Merrill: the importance of an optimist

Charles E. Merrill was one of the first New York stockbrokers to appreciate the importance of selling stocks to smaller investors by providing sound financial advice. The tough reality of attempting to 'bring Wall Street to Main Street', however, meant he passed away before being witness to the remarkable effect his insight had on America.

Some financial figures achieve recognition because of the age at which they start their achievements, whilst for others, it is the sheer size of their financial success (or deceit) that makes them famous. Merrill's achievements warrant a place in this series of articles looking at figures who have shaped the financial world because of the enormous impact his radical thinking made.

He is responsible for taking the difficult first steps down the path of advocating the American stock market's availability to the masses that endures today. Few other financiers have affected the lives of normal Americans to the same extent as Merrill.

Merrill's adolescent years were quite different from the life he carved for himself, however. Having been forced to leave college two years into his studies due to a lack of funds, it was Merrill's proactive approach to life and enduring optimism that led him to be known as the man who made America the shareholder nation – and himself, well, very wealthy.

Vital statistics

Full name: Charles Edward Merrill

Born: 19th October 1885, Florida

Died: 6th October 1956, New York

His first financial coup

On the way to a Sunday-school picnic on 8th May 1898, 13-year old Charles spent all of his pocket money ($5) to buy a hundred copies of Times-Union and Citizen with the headline 'Dewey tells story of his victory'. With the Spanish-American war raging, patriots willingly paid 25 cents each for the breaking news.

Finding his niche

However, it certainly wasn't a straightforward path. In the years following his shortened education at Amherst College, Merrill tried his hand at numerous occupations – including selling advertising at a local newspaper and semi-professional baseball – before later finding his fit in the business world. Having spent the summer of 1907 playing baseball in Mississippi, Merrill's popularity earned him a rail ticket to New York – paid for by the whole team.

At the time he arrived in late 1907, New York City still had more than 2,000 working farms in business. The tall buildings lining the bottom of Manhattan were only beginning to shape the city's landscape and new industries were cropping up almost daily; armies of clerical workers were growing and Merrill took a position as an office boy in a textile firm.

But the ambitious individual's sights were set higher. Influenced by his mother – who reportedly taught him 'you can get anything in the world you want, as long as you want it bad enough' – Merrill achieved a rapid promotion through the company, being a director by the time he left in 1909. Other employments that followed included: the creation and management of a bond department at a commercial paper company and his recruitment as a sales manager for Eastman, Dillon and Company, an established Wall Street firm, in 1913.

> It was Merrill's proactive approach to life and enduring optimism that led him to be known as the man who made America the shareholder nation – and himself, well, very wealthy.

Just a year later, in January 1914, Merrill decided to start his own investment banking firm – the company, initially founded as Charles E. Merrill and Co, was based in an office sublet from Eastman, Dillon and Company. By April of that year, Merrill was in a position to move the company into its own offices and after six months, Edmund Lynch joined the firm and it became Merrill Lynch and Company. Reports and recollections emphasise that the two made a great partnership: Lynch had a cold approach to figures that could turn Merrill's aspirations into realistic achievements.

The pair initially earned Merrill Lynch its reputation through the successful underwriting of chain stores that grew large and profitable – the largest triumph being that of Safeway Stores. Merrill orchestrated the 1926 merger which gave way to the food chain giant, and his firm continued to provide investment banking services to Safeway. As part of his commission, Merrill took stock warrants, so, whilst building up the business value, he could also profit by selling his shares when their value rose. By the time of his death, he had amassed an impressive personal fortune. The income from Safeway securities alone was predicted to be at least $500,000 annually during the 1930s.

Devotion to education

Earlier unfortunate experiences with funding his own education meant Merrill felt empathy for those facing similar issues and he used his wealth to assist. In 1927, he donated $100,000 (now equivalent to circa $918,000) to his former college, Amherst, on the condition that it would be used to help financially disadvantaged students. His continued contributions helped fund numerous scholarships. Moreover, his vastly improved financial position also meant he could complete an honorary Doctor of Law degree himself at the school in 1943.

Foresight only appreciated in hindsight

But, ever focused on his business and the environment it operated in, Merrill never lost direction. In 1928, the market analyst became convinced that the stock market was overpriced and overextended; he believed speculation in the market had driven prices up to unreasonable levels. It was time for prudent investors to retrench. Merrill therefore was the first big name from Wall Street to predict the crash of 1929 – in the months prior, he had pleaded with President Calvin Coolidge to speak out against engaging in risky financial transactions to no avail.

As well as advising clients to reduce stock possession, Merrill, in February 1929, liquidated Merrill Lynch's stock portfolio. During this time, there was no legal protection in place and the market had no securities laws – so when the crash finally came in October, this act made him famous across the country. Merrill had managed to protect himself and others from severe financial loss.

An extract from the letter Merrill sent to all customers (31st May 1928)

We think you should know that with few exceptions all of the large companies financed by us today have no funded debt. This situation is not the result of luck, but of carefully considered plans on the part of management and ourselves to place these companies in an impregnable position.

The advice we have given important corporations can be followed to advantage by all classes of investors. We do not urge that you sell securities indiscriminately, but we do advise in no uncertain terms that you take advantage of the present high prices and put your own financial house in order. We recommend that you sell enough securities to lighten your obligations.

His achievements are by no means limited to this one insight. After the crash, the American attitude towards the stock market had been soured; investors, having been encouraged to speculate so wildly, felt fleeced. Prevailing views of 'buy low, sell high' had backfired when everyone followed the herd and there was a lack of educated investments. But who would seek to tackle the disillusionment with Wall Street? Merrill took it upon himself to restore the country's faith in the stock market.

Setting the precedent

Early on, he had positioned his view that the stock market should be an avenue a broad mass of Americans could be involved in, not just Wall Street insiders. In an article he wrote in 1911 for business journal Leslie's Weekly, the forward-thinker proposed that stockbrokers needed to start paying more attention to their clients' aims when recommending investment opportunities. "And so it has come to pass that a new guild has sprung up in the banking profession, whose members despite not the modest sums of the thrifty, men who give the same thoughtful and careful attention to the wise investment of $100, $1,000, $10,000 as to the funds of the opulent," wrote Merrill.

The stock market, however, remained a daunting place for those with limited knowledge of investment procedures and most people – except Merrill – seemed keen for it to stay that way. It was some years before he could put these ideals into practice, but his earlier philosophy later guided his own company. Merrill aimed to make the stock market accessible to all; but as humans typically have the wrong instincts when it comes to the stock market, often lacking the discipline to resist impulses, how do you encourage wise investments?

"Demystification had been the key to my father's great success," explained James Merrill, Charles's eldest son, in his memoir. "No more mumbo-jumbo from Harvard men in panelled rooms; let the stock market's workings henceforth be intelligible even to the small investor." The markets' undeniable ability to create wealth, Merrill felt, should be available to all without the concern of being scorned. He promoted the value of stocks as a prudent long-term investment vehicle for all, aiming to clue-up individuals on the importance of developing a temperament opposite to that prevailing in the market – avoiding overpriced companies, for instance.

For that purpose, Merrill Lynch provided an abundance of educational tools. The firm published reports, magazines and pamphlets guiding would-be investors through the maze of the market – 11 million publications were created in 1955 alone. Merrill Lynch also gave seminars across the country, providing childcare where needed to ensure maximum turnout. The company did all it could to bring the common investor back to the market. Once, the company even gave away stock in a contest sponsored by a brand of cereal, Wheaties.

Moreover, Merrill also aimed to demystify the workings of his own firm, providing the public guarantee that it would conduct itself in a way that both met the demands and dispelled the fears of its clients in the company's 'Ten Commandments', published in a 1949 annual report. Given that the first commandment was that the interests of the customer always come first, they may seem obvious now but, at the time, they were a revolution in terms of how larger firms treated their small clients. Indeed, commandments seven and eight were to do with disclosure of interest in offerings and advanced warning should the firm be selling securities.

Infectious confidence

By applying the notion of putting clients first, educating them about a sphere they may have been previously wary about, Merrill started one of the most profound financial trends. Only 16% of America's households invested in 1945 but just over 50 years later, in 1998, nearly half had investments in the stock market – notably because of greater trust in the stock market.

> Merrill promoted the value of stocks as a prudent long-term investment vehicle for all, aiming to clue-up individuals on the importance of developing a temperament opposite to that prevailing in the market – avoiding overpriced companies, for instance.

Small investors responded in droves to the newly available information – Merrill Lynch was soon positioned as the largest brokerage firm in the world. By the time of Charles E. Merrill's death in 1956, the firm had 115 offices in the United States, more than 100 partners and 570 employees. It doesn't logically follow, however, that just because Merrill Lynch was leading the way in best practice, that all of Wall Street was ready to follow. The firm's innovations were limited on Wall Street. Merrill's claim of a new day was just too early and he sadly died before he could witness the full effect of his efforts.

Nevertheless, the basic message Merrill Lynch preached resonates in the investment strategy many Americans follow today: educate yourself to ensure you have a clear understanding of the companies you are investing in. Investor confidence has followed the path Merrill set up by taking on the obligation of guiding well-informed investments and insisting respect for all. Merrill could be proud that the principles of responsibility and duty he stood for are now more prevalent in the country's stock market. ■

Charles E. Merrill quotes

"If the supplying of capital to the nation's industries and, for that matter, to the nation itself is a game, then the time has come to rewrite the dictionary."

"Money, of course, is not everything, but, my friend, emergency after emergency comes up in this world of ours, in which for a few brief moments, at least, and maybe longer, money is the equivalent of everything."

"I have no fear of failure, provided I use my heart and head, hands and feet – and work like hell."

Running a supersized treasury

Mariano Tannenbaum
Corporate Treasurer

Arcos Dorados

Ask Mariano Tannenbaum what is different about treasury in Latin America and the treasurer of Arcos Dorados begins to roll off a long list that includes everything from the region's infamous regulatory complexities to the treasury recruitment market. One immediately wonders, whether it would have perhaps been quicker to have asked what is similar.

What is different about corporate treasury in Latin America? According to Mariano Tannenbaum the list is a long one. In this article, he describes what it is like being a corporate treasurer in this notoriously diverse and complex region. He then explains how he and his team at Arcos Dorados were able to establish an almost completely centralised treasury function covering all 20 Latin American markets.

Arcos Dorados is the world's largest McDonald's franchisee. Headquartered in Buenos Aires, the capital of Argentina, the company has exclusive rights to own, operate and franchise McDonald's restaurants in 20 countries and territories across Latin America and the Caribbean. Since 2011, the company has been listed on the New York Stock Exchange (NYSE: Arco). For the 12 months ending 30th March 2015, the company's revenues reached $3.5bn.

There is one salient distinction, however. Press him and he will tell you it's the rapid mutability of markets in this corner of the world. "Latin America is much more volatile compared to

Europe or North America," explains Tannenbaum (an observation he is certainly qualified to make having worked in all three aforementioned regions). "Things can change here dramatically from one day to the next and exchange rates move much more than in other regions. But at the same time, it is also much more fun working in this region."

The golden arches

Arcos Dorados might not be immediately familiar to readers in other parts of the world. Its business certainly needs no introduction, however. A New York Stock Exchange (NYSE:ARCO) listed firm, headquartered in the Argentine capital Buenos Aires, the company is the master franchisee for McDonald's restaurants in 20 countries across Latin America and the Caribbean.

Tannenbaum has been working at the company since 2008 and his role has grown considerably during this time. Beginning with pure cash management, he now also oversees the company's insurance, financial planning, risk management and capital markets operations. If you think he has a lot on his plate now though, this is mere small fry compared to the task that confronted him when he first took up the job.

Before he'd barely managed to get his feet under the table at Arcos Dorados, he was given a target that up until that moment many people thought was near-impossible to do in Latin America: successfully build a functioning centralised treasury operation covering an area ranging from northern Mexico down to the southern tip of Argentina.

Vital experience

More about that in a moment. First, it is worth mentioning that this was not the first time that Tannenbaum had been involved in the building of a treasury department. That initial experience actually came in his very first treasury job after being hired by the Swiss multinational Tyco.

Tannenbaum recounts that the break came while he was studying for his Masters at London Business School (he had returned to academia after a spell post-graduation working for Argentina's Ministry of Economy in the capital researching mergers and acquisitions (M&A) and privatisation – the latter very much a hot topic at the time). It was a job interview that first got him thinking about a career in corporate treasury. "During my MBA I was invited to an interview with General Motors (GM)," recalls Tannenbaum. The director who interviewed him, it turned out, was an inspiring individual who, after spending the day with Tannenbaum introducing him to the company's various financial functions, had convinced him that treasury was the place to work.

Although GM ultimately decided not to hire MBA candidates for that particular role, Tannenbaum had obviously made a strong impression on the interviewer. Not long after, he was contacted by the same person, now working for security systems multinational Tyco International, about a treasury vacancy. "Tyco was building an entirely new treasury structure, and he convinced me to go and work with him on that – first in the US and then in Switzerland," he says. It didn't take long for Tannenbaum to realise this was exactly the right profession for him. "I decided to go and right away I loved it," he exclaims. "What I like about treasury is the view it gives you of a company. You are in the middle of everything."

Down south

During his time at Tyco, he had learned what it took to build a new treasury structure and discovered he had both a taste and aptitude for the work. Building a new treasury in Europe is one thing though, doing the same in Latin America is, as Tannenbaum will tell you, something else entirely.

In late 2008, right when most of the financial world were contemplating the frightening new financial realities that manifested in the wake of Lehman Brothers, an unexpected opening back in Buenos Aires led to Tannenbaum and Tyco parting ways. The company he went to – Arcos Dorados – had begun operating in August 2007 when it acquired most of McDonald's operations in Latin America and the Caribbean in a buyout transaction led by the company's controlling shareholder, Woods Staton, who is also the company's current CEO and chairman. When Tannenbaum arrived, work was already underway on building a first-class treasury department that could provide services to the newly established multinational company. It really was starting from scratch. "There was no treasury function here before that, of course," Tannenbaum says. All that they had to build on was the decentralised legacy model McDonald's had before in which cash management, borrowing and investment were conducted locally in each country. "We were just a subsidiary of the McDonald's Corporation and so we had been reporting to Group Treasury in Chicago. So after Arcos Dorados was created there was a need to create a corporate treasury function, and the intention was to build one with a very centralised structure."

Knowing Latin America though he was never under any illusions about the challenge facing him in overseeing this project. The motivation for establishing centralised treasury activities is easy to understand. In most cases it means greater process consistency and efficiency, which in turn gives rise to greater treasury control. It also enables the central purchasing of financial services and bank relationship management. Most treasurers then, as benchmarking studies consistently reveal, prefer a centralised set-up where one is feasible.

But Tannenbaum must have wondered, initially at least, whether one would indeed be feasible in these markets. After all, he knew from experience that building a central treasury can be extremely complicated, even in Europe where there are fewer legal, tax and regulatory discrepancies to navigate and, of course, a single currency across 19 markets.

As we have already learned though, Latin America is very different. Even the things that are relatively straightforward in Europe or the US can prove to be real hurdles in these markets. Finding and recruiting experienced treasury staff was the first one they would need to clear. Although there are obviously many multinational companies operating in Latin America, Tannenbaum explains, most of them are headquartered in other regions. This means the pool of professionals with extensive treasury experience is not a particularly large one.

"The other corporates who have headquarters here in Argentina, Brazil or Chile – we compete for the same resources and there are not as many treasurers here as there are in the US or in Europe," he says. "You need to phone a lot of people. Luckily we have an excellent team here, but they didn't have corporate treasury experience initially. That was why Arcos Dorados looked internationally for a group treasurer as they were unable recruit one here." Then, even if that first hurdle can be successfully negotiated, there was the question of how a highly centralised treasury set-up in Latin America would operate in practice. How would the markets with strict capital controls in place – like Venezuela and Argentina – fit into a centrally controlled FX risk management strategy? In what currencies is it possible to hedge and what currencies is it not? And how would treasury keep on top of multitude of complex and rapidly changing national tax regulations?

Putting these factors together it is really quite incredible what was ultimately achieved in the building of this treasury function. Over the 20 Latin American markets in which Arcos Dorados operates they have only one country treasurer in Brazil (which requires country support due both to its size and regulatory complexity). The rest is run entirely from headquarters in Buenos Aires by Tannenbaum and his team, a feat which he is understandably very proud of. "A lot of people thought that was not possible in this region," says Tannenbaum. "But we did it."

Centralising also allowed the company the opportunity to scale down their banking relationships significantly. When Tannenbaum took charge of treasury at Arcos Dorados, the company was working with around 50-60 different banks across the region, a number which has now been reduced dramatically. Following an RFP issued shortly after Tannenbaum joined, the company now works with just ten banks in total, predominantly international institutions able to offer the kind of pan-regional support a highly centralised treasury needs. "All the main banks were interested in gaining our account," he says. "We are a unique company: a Latin American company with a presence in 20 markets. There are not many companies like that in Latin America."

Everyday volatility

These days, the challenge for Tannenbaum is no longer building a centralised treasury operation in Latin America, rather it is the day-to-day running of one. In good times this is not straightforward in this region, but when market conditions take a turn for the worse – as they did in fact do recently – the job can become extremely testing indeed. "This year didn't start well for the region," he confides. Top of a long and growing list of concerns is the foreign exchange markets, in particular the strengthening greenback. As the US recovery solidified in the early part of 2015, the dollar appreciated against all the Latin American currencies (and indeed others like the euro too, a currency which Arcos Dorados is exposed to in the Caribbean). In fact, some of the currencies to which Arcos Dorados has the greatest exposures were the worst hit during this spell of volatility. The Argentine peso, for example, has lost 27% of its value against the US dollar since the beginning of 2014.

A stronger dollar is an ominous prospect for a company that is listed in New York but whose revenues are denominated in an array of EM currencies (especially when opportunities to hedge in some currencies are limited. "We manage a lot of currencies with a lot of volatility. Of course we have a hedging programme in place but that is only for our imports, not our profits," says Tannenbaum, adding that this is not hedged at least partly because investors who buy shares in Arcos Dorados tend to be looking for a Latin American risk.

Beyond the worsening volatility, the region's general economic downturn is Tannenbaum's other main concern. As a retailing company, Arcos Dorados is naturally highly sensitive to the business cycle. Revenues are generally higher in periods of strong economic growth and prosperity, and lower in periods of contraction. But knowing the region well is also an advantage for local companies. "We have been in the region for many years and we know that after tough years always come the good ones as part of the region's volatility and we should be ready to take advantage of this," Tannenbaum says. "It is true that Brazil had a couple of tough years without significant growth and accounts for 50% of our revenues but it is during these times that we need to strengthen our base and be ready for the upcoming recovery. While many competitors might leave the region we are here for the long term and we know how to manage this volatility."

Fighting back

Tannenbaum knows he is powerless to affect the external conditions he is faced with. What he does hold influence over, however, is the financial resilience of the business in the face of these macroeconomic and currency headwinds. In this environment, he believes it becomes even more important to get the basics right, particularly with regard to managing excess cash and cash shortages in the business. And for that a reliable cash flow forecast is critical.

"I have been spending a lot of time on cash flow projections," he says. Technological enhancements have helped the company's cause in this area (treasury have just seen the completion of a new TMS provided by a well-known cloud based provider) as has the rationalisation of banking relationships. Tannenbaum is not complacent, however, and hopes to see continual improvements in this area. "At this particular time, and this year, specifically because of all the complications we are having in the region we are looking very carefully at our forecasting and I discuss that quite a bit with my team." Deteriorating economic conditions has also meant Tannenbaum has been devoting more of this time and energy into refinancing the company. At present, the company has in issuance a $475m ten-year bond maturing in 2023 at 6.625%. The company also has on its books a separate bond of R$675m issued in 2011, that is bearing interest of 10.25% and, although denominated in Brazilian real, is payable in US dollars.

Work has already begun on refinancing the debt due to mature next year. A number of different options are being assessed and no firm decision has been made. "Interest rates are still very low in Europe and, for the time being, in the US, so there is still great appetite for the Latin American story. Of course, you always need to have a good story as a company too, but we have one of them as well."

Taking stock

After such a testing baptism at Arcos Dorados it's perhaps no wonder that Tannenbaum now thinks it time to take a step back and reflect on the journey. Right now, having put in place what he deems to be the correct banking structure, he intends to think carefully about how these achievements can be built upon going forward. And the football-fanatic 'Porteño' (native of Buenos Aires that is) draws on an analogy from his favorite sport to illustrate the point. "Now it's time to stop the ball, look around and think carefully about the next move," he says.

"The first four years were hectic but the company has a very good, solid financial position at the moment. I feel very comfortable with the structure we have and I think during the course of next year and the years ahead we will need to fine tune and start reviewing all the things we have done," he adds. ■

Structuring commodities

History is littered with examples of the transformational power of commodities. The Californian Gold Rush of the 19th century, for example, converted a handful of small frontier settlements on the US West Coast into big cities as hundreds of thousands of people travelled from around the world to make their fortune.

Today, crude oil, nicknamed 'black gold', is the world's most prominent commodity. Oil is the commodity of the modern age and plays a vital role in every part of an industrialised economy. It can be used to generate heat, fuel vehicles and manufacture nearly all chemical products. As such, its transformational power has surpassed that of gold and any other commodity before it.

Oil and gold fit perfectly into the dictionary definition of a commodity: a raw material that can be bought or sold, at any time, anywhere in the world. As a rule, commodities are uniform in nature – in other words, you should not easily be able to tell who or where it has come from by its look, taste, feel or smell. A product (made out of commodities) on the other hand can usually be identified as being created by a certain company.

Commodities are big business, and so is financing them. To the point where the market has developed its own nuanced ways of financing players in the commodities market.

Heavy users

In some way, all companies are users of commodities, either directly or indirectly. But not all companies are users of commodities finance, because although they might purchase commodities such as fuel, they do not then produce something from this which is a commodity. By using the fuel to power an airplane or oil tanker the commodity is being transformed into a product or a service. Once the commodity is in the hands of these companies, who are end-consumers, it can no longer be banked as a commodity and this is where commodities finance slips away.

The traditional target market for commodities finance can therefore be broken down into three categories:

- Commodity trading firms such as Vitol, Glencore and Cargill.
- Producers of commodities, for example: Saudi Aramco, Adecoagro and BHP Billiton.
- Processing companies, such as: Reliance Industries, Sinopec and ArcelorMittal.

Built to fit

The unique nature of the commodities market, in respect to the size of the deals, the need to often raise financing quickly, the risk levels and its cross-border nature, has seen it develop its own nuanced approach to financing. This is commonly referred to as structured financing.

Structured financing is different from traditional trade financing because the lender takes security (this can vary from the commodity itself, to contracts, shipping documents etc) in return for the cash. In doing so, the credit risk is removed for companies along the supply chain, because the lender (often a bank) is the trusted entity in the transaction who will guarantee payment to the producer/seller.

This is important in the commodities business because many of the companies involved are not rated in their own right, or are operating in countries with below average ratings, and therefore find it difficult to access affordable financing. Other advantages of this arrangement include:

- Working capital is freed up – this benefits the entire supply chain and allows the flow of commodities and cash to continue.
- Commodities are very liquid and banks are therefore willing to lend against unprocessed goods because they can be liquidated should need be.

Within the scope of structured finance there are several different key methods of financing during the commodities lifecycle (see Chart 1). And many of the products that are used in these methods of financing are those typically found in traditional trade finance.

Pre-export finance

Pre-export finance is often raised against the producer's projected future export revenues, but it can also be based on existing orders along with the buyer's payment risk. In most cases, these deals are short-to-medium term, with a tenor between one and five years and can be amended or restarted during this period.

In a typical pre-export finance agreement, the funds will be provided by an individual lender or a syndicate for all manner of working capital reasons, including:

- The purchase of raw materials.
- Manufacturing and production costs.
- Transportation and storage costs.
- Sales and admin expenses.

In a pre-export structure, the loan is secured by a security assignment of the relevant delivery contracts between the producer and 'offtakers', and the receivables generated under those contracts following the delivery and sale of the relevant goods. Also, there will be a charge over a collection account (belonging to the producer) into which the proceeds of the sale are paid. After deductions for debt service, excess funds are made available to the producer. It is worth noting that there a number of ways a structure can be enhanced,

Commodities financing: a short history

Just like any corporate, commodity producers, processors and traders require financing to ensure that the tools which help build and maintain industrialised economies keep coming. This vital function is, on the whole, provided by the banks, primarily the large European, Japanese and American banks, who have been active in the commodities market for centuries.

But it is an evolving relationship. Original financiers of commodities would have done so by issuing letters of credit to the commodities firms which were secured against the commodity. This relationship largely existed unchanged until the 1980s, and the deregulation of the financial services industry. This provided the banks with an opportunity to explore new avenues of revenue – primarily becoming brokers and market makers in the world's largest commodities exchanges. In the 1990s, the relationship further changed, as commercial banks expanded into the commodities trading business as a way to capitalise and meet new regulatory requirements, going in direct competition with the companies they had been financing.

While this proved a prosperous adventure for the banks, the onset of the global financial crisis in 2008 and the regulatory changes since, have again reversed the banks' relationship with the commodities world. A large number of banks around the globe, such as Barclays and J.P. Morgan, have sold off their commodities trading businesses and returned to their original remit of providing financing for the commodities sector.

including introducing hedging products to protect against commodity price fluctuations and interest rates.

The overall benefits of using a pre-export financing solution include:

- The ability to enhance liquidity and produce goods.
- Lower interest rates in different countries can be leveraged.
- The solution is resilient to country default or capital controls.

Prepayment financing

Prepayment financing is similar to pre-export financing in many aspects. However, in these arrangements the producer receives the cash directly from an offtaker as an advance payment under the export contract. Lenders can fund the offtaker and share the risk of non-performance by the producer.

The typical tenor of such a facility can vary between a few months and up to five years for the strongest producers. In regard to the security used during the deal, this includes a security assignment by the offtaker of its rights under the export contract with the producer, including the right to have the prepayment advance repaid.

In the case of pre-export or prepayment finance, the primary risk is placed in the producer's ability to deliver the commodity. To the extent lenders are comfortable with the performance risk of the producer, the offtaker who is extending the finance, can account for this line of credit as 'credit limit neutral'.

Aside from this, other benefits include:

- The ability for the producer to access credit from lenders that do not bank the producer directly.
- Buyers can negotiate term supply contacts in return for the provision of finance.
- Mitigation of transfer risk as funds are paid into an offshore account as shipments are made.
- Legally resilient against country default.

Borrowing base financing

The final key financing structure related to commodities is borrowing base financing. This is a structure unique to commodities and is used primarily by traders and processing companies. In these arrangements the borrower's assets – typically accounts receivables or commodity type inventories – are used as security. Once the security is in place, the solution is flexible, an upper credit limit will be agreed from the onset, but the actual amount of financing will be directly correlated to the value of the pledged commodities or receivables. Borrowers can therefore access more financing as commodity prices increase and their needs change. These facilities are revolving in tenor and typically exist for one to two years, after which they are extended at the discretion of the lenders.

To calculate the financing that can be offered to a borrower against their collateral, the lender will carry out the following calculation: the net value of the accounts receivable (accounts receivable less deductions such as those which are overdue, doubtful, or which can be contested) plus the net value of the goods (goods less deductions such as trade payables). This represents the total collateral value against which haircuts will be applied to determine the amount available for funding.

The benefits of such an agreement include:

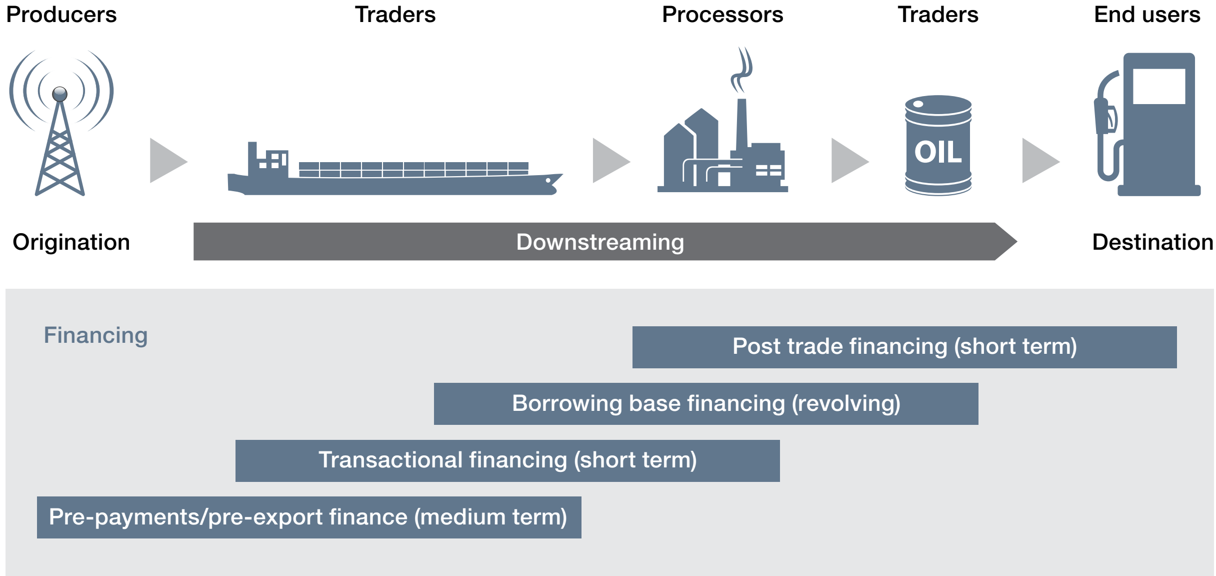
- Continuity of a credit line that fluctuates with the commodity price and hence the financing requirements.
- Reduced cost and better access to funding through collateral cover.

Is the well running dry?

There are some commentators in the commodities space who argue that traditional commodities finance provided by major global banks is dying. It is an understandable argument when we look at the major banks' relationship with commodities post-crisis. As mentioned, many have pulled the plug on their commodities trading business, and following the crisis banks reduced their lending quotas because of their reduced access to dollar funding and the scarcity of balance sheet assets.

Since the crisis, regulatory pressure from Basel III has further added to the argument. Banks are having to focus more and more on risk weighted assets and ensuring that these are used efficiently. We are also seeing some of the world's global banks realign and pull out of countries and regions where they don't have material presence and scale. Finally, many commodity financiers have become slow to react to the needs

Chart 1: Different stages of financing



Source: Galena Asset Management, 2013

of the market in respect to extending finance as the internal process around approving these is now more complicated.

The stats also make a compelling argument. According to the Bank for International Settlements, which published a report which stated that before the crisis, 80% of global commodities trade financing was provided by banks, and primarily those in Europe. But more recently this number has shrunk to 50%.

As a result of these changes, many firms in the commodities world have already seen their costs of financing increase.

There is some relief, however, provided by the cyclical nature of the commodities business. In times when commodities prices are low, as we have seen with oil this year, there is less for banks to finance. In fact there was almost 50% less oil business to finance since the summer of 2014, but on the whole, lines of credit were unchanged. This means banks have to process double the amount of transactions to make the same revenues, which puts popular borrowers in a stronger position when looking to achieve financing.

Despite this, there is a shortage of bank financing for some commodities players, especially for mid-sized commodities firms in emerging markets. In many cases, the deals being made by these companies are too small and also the 'know your customer' processes are often so heavy that it makes it more challenging for the bank to onboard the client.

There is some relief for those companies that are struggling to find financing in the post-crisis world, namely smaller regional and local banks. Over recent years a number of banks from Asia, Africa, the Middle East and Latin America have begun to be active in the market as both providers of short-term financing and as part of RCFs. The caveat is that these banks are primarily looking to support firms that are providing growth to their country or region, a bank in Brazil for example will offer financing to top firms only in Europe, but may look to help smaller firms in its own country – something which has been called the regionalisation of trade finance. These firms are also in the business of cross-selling off the back of their financing.

Since the crisis, commodities firms have also looked to diversify their funding sources themselves and reduce their reliance on traditional bank financing. Some of these firms have, for example, further delved into the capital markets. A handful have taken this even further and established their own asset management business as a way to take advantage of the different types of investors looking to pump liquidity into the market.

There are other sources that commodities firms can tap, such as private equity firms who are looking to provide financing in areas that have always been out of the scope for banks – agriculture in emerging markets, for example. Yet, these firms normally have a high cost of capital and demand higher yields to justify their involvement.

Whether these developments point to traditional trade financing dying remains a topic up for debate, and this may just be the argument used by those no longer able to compete in the space. But one thing that does seem certain is that post-crisis commodities financing has changed for good. ■

Thanks to Kris Van Broekhoven, Global Head of Commodity Trade Finance at Citi for his help in providing information towards this article.

COMING NEXT MONTH

INSIGHT AND ANALYSIS

Innovation in cash and payments

The move to cashless payments is a trend that can be seen in many markets globally, as new ways of paying are developed by both banks and technology firms. In this article, Treasury Today explores what have been the most significant developments in cash and payments of late and what solution, if any, has a real opportunity to push physical cash out of the picture.

TRADE

New global trade corridors

Over the last two decades, global trade corridors have shifted dramatically. Where once trade was primarily conducted between developed Western nations, Asia is now at the heart of global trade, with trading relationships extending further afield and encompassing a broader range of companies and geographies than ever before. But what does all this mean for corporate treasurers?

TECHNOLOGY

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

Ian Blackburn, Regional Head of Commercialisation Europe, Payments and Cash Management, HSBC; **Frank Boroch**, Director, Treasury Investor Relations, Hyundai Capital America; **Jennifer Boussuge**, Head of Global Transaction Services EMEA, Bank of America Merrill Lynch; **Rando Bruns**, Group Treasurer, Merck; **Vina Cheung**, Global Head of RMB Internationalisations, Payments and Cash Management, HSBC; **Matthew Clarke**, Group Treasurer, Intertek; **Cyrus Daruwala**, Managing Director, IDC Financial Insights; **Emma de Ronde**, Partner and corporate lawyer, Norton Rose Fulbright Hong Kong; **David Deranek**, Senior Manager of Treasury Operations and Control, Health Care Service Corporation; **Sergey Filippov**, Associate Director, the Lisbon Council; **Alexandre Huet**, Global Head of Strategic and Acquisition Finance, Société Générale; **Shirley Kwong**, Head of Business Development, Global Trade and Receivables Finance, HSBC; **Séverine Le Blévennec**, Director, EMEA Treasury, Honeywell; **Christine McCarthy**, Senior EVP and Chief Financial Officer, The Walt Disney Company; **Paul McGhee**, Director of Strategy, AFME; **Rajesh Mehta**, Managing Director, EMEA Region Head, Citi Treasury and Trade Solutions; **Deborah Mur**, Western Europe head, Treasury and Trade Solutions, Citi; **Anita Prasad**, General Manager, Treasury Capital Management, Microsoft; **Tony Richter**, European Head of Regulatory & Market Delivery, Payments and Cash Management, HSBC; **Charlotte Robins**, Partner and financial services regulatory lawyer, Norton Rose Fulbright Hong Kong; **Eric Senay**, Vice President and Head of Treasury, Hyundai Capital America; **Mariano Tannenbaum**, Corporate Treasurer, Arcos Dorados; **Ciar Timon**, Senior Regional Treasury Manager, Honeywell EMEA Treasury; **Kris Van Broekhoven**, Global Head of Commodity Trade Finance, Citi; **Fabian Vandenreydt**, Head of Markets Management, Innotribe; **Nicholas Véron**, Senior Fellow, Bruegel; **Michèle Zaquine**, Senior Proposition Market Manager, Europe, Payments and Cash Management, HSBC.

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