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September 2015



## The innovation imperative

Although much of the visible innovation in payments can only be found in the retail space, banks and other providers are now working increasingly hard to develop creative solutions to bring similar developments into the corporate world. Will treasurers soon catch up with consumers?



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# Is your treasury fit for purpose?

This issue of Treasury Today coincides with our attendance at EuroFinance's International Cash and Treasury Management Conference 2015 in Copenhagen, Denmark. Indeed, we expect many of you may be attending the conference too. The theme this year is 'keeping treasury fit for purpose, fit for growth and fit for the future' – something that many treasurers will be thinking about as they take the time to step away from their desks and look towards 2016.

As we have reported frequently throughout 2015, companies continue to face major challenges with regard to new regulations, compliance and threats to security on a number of levels. Currency, stock market and commodity price volatility only compound these issues. Add to the mix economic and political uncertainty and the role of the treasury function gets harder still.

Despite all the barriers that exist though, we still see remarkable companies doing remarkable things, especially where corporate treasury is concerned. We view the majority of treasury departments we see as striving for continuous improvement and doing the right thing to ensure they remain fit for purpose. Nonetheless, we can all learn from best in class solutions and the best practices being deployed by our peers; corporate treasury is no exception as you will see from many of the articles in this edition.

Our 2015 Adam Smith Awards, now in their eighth year, are always a good barometer of best practice and innovation and this year's submissions were no exception. A record 210 submissions from 23 different countries were received. Some of the winning entries are being showcased, commencing 30<sup>th</sup> September, as part of our educational Adam Smith webinar series. For more information please visit [treasurytoday.com/webinar/coming-soon](http://treasurytoday.com/webinar/coming-soon). The benchmarking studies we have conducted in recent years also help to inform us, and therefore you, about what is happening in the treasury space, what is being measured and the actual metrics being achieved. Find out more at [treasurytoday.com/benchmarking](http://treasurytoday.com/benchmarking).

If you are attending the Copenhagen event, please do visit the Treasury Today stand and talk to us about the steps you are taking to get your treasury fit for purpose. Also, pick up your copy of our new Digitisation Handbook and take the opportunity to tell us what else we can do to make your professional life easier. Our MD, Richard Parkinson; Group Publisher, Angela Berry; and Research Director, John Nicholas will be pleased to discuss your needs and bring you up-to-date on what we already have planned for 2016. Why not have your say and influence what we will be doing? If you are not planning to be in Copenhagen we would still like to hear from you, so please email [john.nicholas@treasurytoday.com](mailto:john.nicholas@treasurytoday.com).



## The innovation imperative

The payments world is vast and expanding rapidly. While much of the visible progress can only be found in the retail space, banks and other providers are now working increasingly hard on developing creative solutions to bring similar innovations into the corporate banking space. Can treasurers catch up with consumers on the innovation curve?

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## Trading places



The world of trade is changing. Where once flows were dominated by Europe and the US, emerging markets, especially Asia, are at the heart of international trade. As a result of this shift, trading relationships have extended further afield and are encompassing a broader range of companies than ever before. Treasury Today explores what the impact of this has been on corporate treasurers.



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## The Corporate View

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**James Koh**  
Group Treasurer

**VERTU**

James Koh, Group Treasurer at Vertu, has enjoyed a rich and varied career working in numerous industries and countries. Along this journey Koh has accumulated a wealth of knowledge, experience and friendships that have shaped his treasury philosophy. In this article, Koh outlines his career and his knack for always being in the right place at the right time.



**INVESTING 28**

**Mapping the new liquidity landscape**

Liquidity management is increasingly becoming a challenging task for treasurers. Regulatory upheaval, banks becoming more selective around deposits and rates diving into negative territory in some geographies has caused some treasurers to go back to the drawing board regarding their short-term investment policies.



**TECHNOLOGY 34**

**A tangled web**

The headlines have been besieged by stories of cyber-crime and fraud of late. Fraud is of course nothing new, but despite the adoption of sophisticated anti-fraud technologies, it remains a major commercial issue. We consider the threat and ask what role the treasury profession has in defending corporate cash and reputation.

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**Nordea**

**THE INDUSTRY INTERVIEW 25**



**Bea Rodriguez**  
Managing Director, Co-Head of International Cash Management and Chief Investment Officer for the Sterling and Euro Cash team

**BLACKROCK®**

It is a challenging time to be a corporate investor given the regulatory upheaval, negative interest rates and the increasingly scarce liquidity in money markets. But this environment can also create the opportunity for alternative investments to be explored as Bea Rodriguez, Managing Director, Co-Head of International Cash Management and Chief Investment Officer for the Sterling and Euro Cash team at BlackRock explains in this interview.

**THE BANK INTERVIEW 31**

**Erik Zingmark**  
Deputy Head of Transaction Products



For treasurers, understanding the trends both of today and tomorrow has become vitally important in the post-crisis world. In this interview Erik Zingmark, Deputy Head of Transaction Products at Nordea provides an insight into new strategic imperatives for treasurers and reveals key insights from Nordea's Treasury 2017 Survey.



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](http://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](http://treasurytoday.com)

## Handling China's RMB regime shift

In 2014, China's central bank warned the market to expect more "two-way volatility" in the renminbi over the coming years and, in August, that was exactly what we got. The week following the Peoples Bank of China's (PBoC) 2% downward 'adjustment' was something of a rollercoaster for those who trade in the currency. After three days of steep falls, and much speculation that this represented the first shots in a new round of 'currency wars', implied volatility for a three-month options contract against the dollar shot up to 7.93 on Wednesday 12<sup>th</sup> August, from 1.5625 just the day before.

This move may not be a one-off, but rather the birth pangs of what is going to be much less stable renminbi as the PBoC allows market forces to play a bigger role in determining the value of the currency. Moving forward, a research note published by Deutsche Bank last month noted: "What transpired is not only a seismic shift relative to the currency's historical movement, it is also a regime shift that warrants recognition that the currency will be more volatile from now on."

### Time to hedge?

Firstly, it should be noted that, with respect to Chinese corporates at least, the warning voiced by the PBoC last year did not fall on deaf ears. "There were Chinese corporates who were doing the carry trade (borrowing in dollars and arbitraging the low dollar interest rate) but there is evidence in the market that the trade is unwinding," David Blair, Managing Director, Acarate, told Treasury Today. "They already started backing off from that quite noticeably after last year's two-way volatility." But prepared or otherwise, the corporate market did not escape unaffected by the move, as the large stock sell-offs seen in China testify. Industry experts believe a more volatile renminbi is likely to increase the treasurer's focus on risk management, especially as central bankers in nearby economies look to respond with their own adjustments.

"The effect of RMB on Value-at-Risk (VaR) will go up as a result of this so corporates are more likely to hedge," says Blair. "But regulatory changes since 2012 making it easier to transfer their exposures and hedge RMB offshore have also been driving increased hedging." Carmen Ling, Head of RMB Solutions, Standard Chartered Bank agrees. "As RMB is becoming an international currency with more two-way volatility driven more and more by market forces, corporates and investors would need to rebalance their portfolio and we would expect to see more hedging activities," she says.

As is often the case though, where there are challenges there are also opportunities. "The depreciation may not be a bad thing for those who are holding US dollar but have a desire to invest in RMB-denominated securities/assets," Ling adds.

## Payment terms: regulation on the horizon?

In recent years, governments across the developed world have placed an increasing focus on corporate payment terms to their supplier base. Schemes such as the Prompt Payment Code in the UK, the EU Late Payment Directive and the SupplierPay initiative in the US are all aimed at creating a culture of reasonable – and responsible – payment terms amongst corporates. Whether corporates like it or not, payment terms are under the microscope. The question is: how can key working capital metrics be improved whilst also safeguarding the financial health of suppliers? This issue was debated at a recent executive briefing hosted by Taulia on board the HQS (Head Quarters Ship) Wellington on London's River Thames.

To a large corporation, the impact of a late payment, while frustrating, is normally fairly limited – or at least manageable. The same cannot always be said for SMEs and family-run businesses, however, many of whom supply larger corporations. A late payment for these companies can have a far more damaging impact as companies may be required to raise extra funds in order to fulfil working capital requirements and in today's post-crisis world, this is becoming increasingly difficult and expensive.

So what can be done to prevent squeezing suppliers? On board HQS Wellington, Philip King, Co-Chair Prompt Payment Code Advisory Board, Chief Executive, Chartered Institute of Credit Management compared the process of a small business sending an invoice to a large corporate to buying a lottery scratch card: "Sometimes you win and sometimes you lose." But according to King it doesn't have to be this way. In his opinion, most late payments are down to something trivial, not corporates behaving badly – such as inadequate paperwork or the invoice being sent to the wrong place.

Lex Greensill, Senior Advisor and Crown Representative of HMG and Chief Executive of Greensill Capital, agrees with King. "It is safe to say that very few companies have the objective of doing harm to their supply chain." But, he does believe that corporates – in the Basel III world – have a growing responsibility to ensure the financial health of their supply chain.

For Greensill, supply chain finance (SCF) is the way corporates can meet their new responsibility, and the UK government is leading the way in setting an example in this space. For instance, the government has recently implemented a SCF solution in its health department which ensures that drug vendors are paid by the government in a maximum of eight days. The purpose of the scheme is also to encourage corporates to also adopt such initiatives.

# Maximising your potential

“ *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?* ”



**Maciej Müldner**  
Finance Director,  
Skanska Property Poland

Whilst it may seem obvious, it is important to point out that in order to become a CFO, first and foremost, you have to want to. It should be part of your career plan because any aspiring CFO must understand the capabilities, knowledge and experience needed to fulfil that role. You can find a lot of ideas and descriptions of what the role entails on the internet (posts on LinkedIn, for instance). My personal view is that a CFO is a business partner; they are the person that ensures the president or owner of a company is comfortable with what the organisation does and the financial impact of all of its business activities. This involves business decisions that are properly considered and presented and ensuring, as much as possible, that decisions show the expected result.

There are, of course, certain things a treasurer can do to improve his or her chances of becoming a CFO. It is often the case that the treasury function, and those working in it, are rarely seen by the rest of the organisation so they need to make themselves more visible in the company. Employees can invite themselves to meetings even if these meetings are not 100% connected to their day-to-day role. This is one way of gaining the desirable understanding of the business beyond a current role, for a CFO needs to get much closer to the operational side of the business – understanding the consequences of their decisions and how operational processes work, for instance. For those who wish to gain such skills, first, they need to appreciate what experiences they are lacking. A few typical areas where treasurers need to gain knowledge are accounting rules and processes and controlling. Controlling can refer to financial controlling, an area which treasurers usually work quite closely with, and business controlling. This is where a treasurer could boost their marketability: how to do a budget, how to forecast, the best way of following up on a forecast and the key performance indicators (KPIs) that drive a business, for example. It is also a good idea to start expanding your scope of responsibilities.

In a way, a CFO lives in two worlds – the operational world and the financial world – so it is crucial to build up good communication skills in order to explain difficult and

complicated concepts in a way others can understand and relate to. Whilst this is a challenge on the one hand, on the other if you can build up this skill, it is invaluable in fulfilling the CFO's role of being an operational voice. Moreover, this involves having the capability of translating business decisions into numbers, both seeing and explaining the impact on the company's bottom line.

To summarise, as a CFO you need to harness a combination of skills. Typical financial qualifications are good to have, as well as a Master of Business Administration (MBA) or alternative forms of management study. Treasurers will develop the relevant skills when focusing on transactions within a given benchmark or certain value to achieve. Accountants, will reflect on what has happened by analysing the accounts. But, as a CFO, you need to combine both – as well as looking into the future, all the time translating reality into numbers and numbers into reality. There is no 'safe haven' for a CFO, so whilst many talk about it, the role isn't for everybody.



**Mike Richards**  
Founder and President,  
MR Recruitment

For the ambitious, it is always a good thing to look towards the future and, with regards to maximising your chances of one day becoming a CFO, I have the following advice. Of course, it is extremely useful for corporates to have a background in a wide range of business functions (rather than have spent their entire career within treasury), although I do find that many treasurers tend to have developed their treasury or finance expertise within just the treasury 'stream'. This isn't always intentional, however. It is often by accident rather than design: once you develop excellence within a particular area of finance why wouldn't you utilise that to your advantage? Financial reward is on offer and, in these challenging economic times, who could blame an expert for wanting to be rewarded as such.

This being said, of the CFOs that I know with a background in treasury, all have also worked in other areas within finance as part of their career path, eg they have become experts in the treasury area and have moved into other senior business roles or senior finance positions. Thus, they have made active

choices to move into financial controller or planning roles in order to experience finance as a whole, enabling them to better sell themselves when applying for CFO and/or FD positions.

In short, for a treasurer looking to move up the career ladder, take a moment to reflect on what you have and have not achieved through the challenging economic period we have seen over the past three to five years and ask yourself:

- Have you achieved what you set out to achieve?
- Where have you fallen short?
- What have you done to achieve your aims?

After all, these questions will be asked of you at your next job interview. If you are satisfied with your answers then you are on the right track to achieve your next move. If you are not happy with your answers, why would anyone else be? A track record of success within the treasury function is simply the precursor to achieving the next role. In order for corporates to enhance their chances, all business related qualifications are beneficial. Professional treasury examinations are extremely useful as a benchmark of expertise and an MBA gives a wider business view. Whether business experience overrides professional qualifications, however, depends on the audience.



**Mustafa Kilic**  
CFO and Member of the Board  
of Directors,  
Candy Group Turkey

It goes without saying that the environment for all finance professionals is changing and, with that, the role of a CFO has also evolved. Within the last ten years, the CFO has started to become more of an integrator and co-ordinator in addition to the more traditional operator and protector tasks. There is also more competition in the business environment. This is pushing CFOs to gain new skills and the ability to sustain and continue business performance is more important than ever.

Against this backdrop, and in order for a treasurer to maximise his or her chances of becoming a CFO, it is important to understand the capacity of your organisation's business operations. Each and every company will have individual operating systems and their own ways of working with them. A CFO first needs to understand the range of areas the business operating system interfaces with in order to run effectively. This, of course, is a prerequisite for writing and applying policy.

Moreover, with the state of the current regulatory environment, expectations to understand the impact of such regulations, are higher than ten years ago. Understanding these procedures, and the company's exposure to risk, is crucial in a CFO's role. I cannot even begin to compare the tools we are using today to measure risk with those from say ten years ago. But this isn't all a would-be CFO needs to be aware of. The world is now more connected than ever before and news spreads fast: crisis management and communication skills are important in order to fulfil the expanded role of a CFO in today's world. In this position, you need to learn how to deliver both good and bad news.

One of the positives is that, as treasurer, you are already in touch with some of the most critical contacts within the CFO's reach – financial institutions (FIs) and suppliers, for instance. Treasurers have the added advantage that they've worked with cash flows and have experience with this element of a company's business operating system. It is also second nature for a treasurer to look for financial risk; they understand how operational, financial and strategic risks are all linked and can trigger each other. In their existing roles, treasurers have already built up a good perspective of credit and market risks too.

In addition, treasurers are always in touch with the key working capital management components: cash, payables, receivables, inventory, funding and profitability. Thus, they develop the key skills which allow them to contribute to the liquidity, transparency and general effectiveness of the organisation's cash management. The skills that are becoming increasingly valued in CFOs I would summarise as follows; an in-depth understanding of an individual company's business operating environment; risk management skills; the ability to communicate well with people from governments; banks and also local populations. Such skills are all within the reach of treasurers who are ideally placed to add these abilities to their current skillset and maximise their chances of becoming a CFO. ■

### The next question:

What's new in the Latin American treasury space? Are there any cash management or payment innovations treasurer should be aware of, for instance?

Please send your comments and responses to [qa@treasurytoday.com](mailto:qa@treasurytoday.com)

# Europe's forgotten fairy tale

*If we are to believe the stock markets, all is well in Europe. But are markets in danger of underestimating looming perils such as populism, a Brexit, German dominance and weakening European power? ECR investigates.*

The Greek crisis has been gnawing at the foundations of European unity for quite some time now. Negotiations over new aid have been conducted in combination with domestic political developments, Europe-wide trends, external threats and personal clashes. The result is that parties on either side have dug themselves into a hole, suffered from tunnel vision, and frequently ignored emotions and arguments put forward by the opposition. In this polarised climate, the real purpose of the negotiations has largely disappeared from view.

## A move away from the centre

An important implication of the events in Greece is an increase in the popularity of Europe's left-wing as well as right-wing populist parties. In the weak Eurozone countries, the leftist populist movements are making headway (for example, Podemos in Spain). The right-wing populists, too, have the political wind in their sails (for example, Lega Nord in Italy).

Numerous voters think that the elites – wherever they are on the political spectrum – have failed and should be ejected from power. This helps politicians who are seen as 'outsiders' or who are good at creating the illusion that they do not belong to the political establishment. It lends credibility to their claim that this time, everything will be different.

And in the 'stronger' Economic and Monetary Union (EMU) countries, the parties that are acting against immigration, European dictates, and the euro are doing well: for instance, the PVV (the Netherlands), the Fins (formerly the True Fins), the DPP (Denmark) and so on. Often, such parties combine a conservative, right-wing bias (sometimes mixed with racism) and left-wing viewpoints on pensions and healthcare.

The aforementioned parties are able to flourish because 'the masses' feel disenfranchised; powerless to influence the governance of their own country, for which they blame globalisation and the European integration process, as well as self-serving elites. German philosopher Friedrich Nietzsche stated that: "The democratisation of Europe is at the same

time an involuntary arrangement for the breeding of tyrants." Regardless of whether it is justified, this fear is what lies behind the dissatisfaction of many European citizens who believe that a small group of people, backed by powerful business interests are firmly in charge; whereas, ordinary people are left to the mercy of overwhelming global political and economic forces.

In the words of George Will, a US conservative political commentator, "the question we settle in an election is not whether elites shall rule but which elite shall rule." Numerous voters think that the elites – wherever they are on the political spectrum – have failed and should be ejected from power. This helps politicians who are seen as 'outsiders' or who are good at creating the illusion that they do not belong to the political establishment. It lends credibility to their claim that this time, everything will be different.

## Brexit: further disintegration?

European integration could be undermined further due to the threat of a Brexit. Prime Minister Cameron has promised a referendum regarding Britain's EU membership – at the latest in 2017, when he hopes to have negotiated new conditions for a renewed British membership. It is feared that Westminster's demands will compromise a fundamental tenet of the European project: the free movement of goods, services, capital, and people. Cameron wants to curb the latter, in particular. He is also opposed to any attempts towards an 'ever closer union'. In addition, he wants to reduce the EU budget and repatriate powers from Brussels.

The sorry Greek saga has reinforced the British belief that the EU should be overhauled. Bridging loans for Greece are financed by the EU; not the Eurozone. Every attempt is made to ensure that non-EMU states do not run risks in this respect. Yet, the British do not like the direction things are headed.

Simultaneously, British EU-sceptics see Greece's woes as an opportunity. They hope that Cameron can land several 'scoops' for the UK during the negotiations on Eurozone and EU strengthening. His approach will be: "I really want to put the Eurozone on a firmer footing but can you guarantee that it will not steamroller London when taking future decisions and what will you give me in exchange for my support, which is essential?" A fascinating political game, played for high stakes is guaranteed.

## The Paris-Berlin axis

But right now, more important than hanging on to the British, is keeping the French-German relationship on track.

The European project was built on the Paris-Berlin axis from the start. France's political and military might and the German economic miracle made for an equilibrium of sorts. German reunification threw the relationship off balance to some degree though and it has continued to deteriorate as Germany has far-exceeded France's economic performance.

Moreover, the eastward expansion of the EU has put Berlin at the geographical heart of the union, replacing Paris as the central hub. The credit crisis (and its ramifications) has further reinforced Germany's position as Europe's dominant power.

It was hoped that European integration would render Germany more 'European'. Now, many fear that Europe is becoming more German. Berlin is not consciously striving for hegemony, but it is prepared to take the lead, although it does not want to be seen as a 'bully'. Many think it is already too late and that the euro crisis has poisoned Germany's attitude towards Europe and vice-versa.

### The story continues

Nationalism, populism, ideological rifts, and economic worries are distracting leaders from other pressing issues, like the chaos at its southern borders and the Russian threat. The EU has always found it difficult to take a hard line – from both a political and military standpoint. Its USP seems to be economic as well as ideological/moral. In the latter areas, it has incurred heavy damage – internal divides are widening and political unity has declined.

For the moment, Greece may have been saved from the abyss but the underlying weaknesses of the Eurozone and the EU remain in place. Still, we do not think Europe will disintegrate for the foreseeable future. After all, the EU project is of importance to the European leaders. It has boosted economic growth, greatly reduced the chance of war breaking

out between EU countries, former communist countries are functioning as democracies, and Europe has a significant presence around the world. This is not forgotten and the EU leaders will not easily abandon the project.

The most likely outcome is that the Eurozone and the EU will continue to muddle on. At the same time, there is a constant threat of disintegration and waning global influence. Not to mention the rise of populism and problems arising from Germany's ascendant dominance.

On the other hand, the Eurozone and the EU are no longer a byword for unity, prosperity, democracy, solidarity and mutual respect. In essence, the project should be revamped to stop the rot, but this is unlikely to happen. Visionary leaders are lacking and the sprawling structure of the EU is incredibly complex and often rigid. Reforms are therefore years in the making.

The most likely outcome is that the Eurozone and the EU will continue to muddle on. At the same time, there is a constant threat of disintegration and waning global influence, not to mention the rise of populism and problems arising from Germany's ascendant dominance. A political analysis of Europe's future underpins our economists' opinion that the euro will have a hard time holding its own against the dollar in the medium to long term. The European fairy tale is over, but the story continues. ■

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# The innovation imperative

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Almost every treasury department will have at least one. They are those tech-savvy, early adopters; paying for their morning cappuccino using an app on their smartwatch, purchasing flights with Bitcoin and making credit transfers from their personal accounts with a few swipes of their state-of-the-art mobile tablet device.

Imagine, then, the disappointment when, every morning, these same treasurers arrive at their desks for work only to find themselves using the very same clapped-out, antiquated technology that they were using five or even ten years ago.

Yes, the global payments market is evolving rapidly. New providers, platforms and tools with the ability to transform the payments experience are coming to the market on a near daily basis now. But while payments may be the 'bread and butter' of the treasurer, the vast majority of mobile and other innovations we have seen in recent years have been

for the benefit, not of corporate banking customers, but consumers in the retail space.

Does it have to be like this? Matthew Leavenworth, Director of Product Innovation and Disbursement at Bank of America Merrill Lynch (BoFA Merrill), is certain it does not. "The consumer innovations that are happening have no cognitive separation in a treasurer's mind from their work when they go into the office every day," says Leavenworth. "What we have to be aware of is that we cannot say that, despite these dynamic new entrants we are seeing on the consumer payments side, we are still going to move blocks of gold because that is what worked for the Rothschilds 300 years ago."

## Digitising disbursements

An example of how recent innovations in retail payments are now, gradually, beginning to permeate the corporate banking

sector can be found in the Digital Disbursements solution BofA Merrill launched in late 2014. It is a novel solution to a seemingly age-old problem. When circumstances arise in which companies need to make payments to their customers (for rebates, refunds and claims payments, for example) the most common way of doing so has long been to write and send a cheque. But delivering funds this way is slow, complex and, above all, expensive (in the UK, cheques can cost up to £1 each to process and in the US, processing a single cheque costs on average \$4).

What is really interesting about the solution BofA Merrill developed to address this issue is that the inspiration came from the growing success of the peer-to-peer (P2P) online technology

that is now allowing individuals to transfer funds to one another's bank accounts via the internet or a mobile phone. The solution works by directly routing the payment to the bank account of the individual payee's choosing to use either a mobile phone number or email address as the identifier. Leavenworth recalls the 'Eureka' moment. "We thought, 'why are there still companies sending these one-off cheques to one another?'" So we developed a tool to allow them to use P2P transfers."

P2P payments are already proving popular in the consumer space. A study conducted last year by Forrester Research expects P2P payments in the US to grow to \$17bn by 2019, from \$5.2bn in 2014. In Western Europe, meanwhile, the research group forecasts P2P payments to rise at almost 24%

## Innovation challenges

The pace of change in consumer payments of late has been truly remarkable. In just the past few years we have seen new payments providers emerge, new wallets and new form factors – most notably mobile and wearable technologies – and even new, digital currencies like Bitcoin gain increasing traction in markets across different regions.

Treasurers might be big beneficiaries of these developments, with richer and more accessible business data, faster and cheaper transactions and more efficient reconciliation processes. Naturally, though, changes on this scale will also present significant challenges to the treasury community.

Foremost, there is the matter of working out the best way to integrate all of these new payment methods into the corporates cash management systems and processes whilst ensuring they maintain control over the company's data, Phillip McHugh, CEO, Barclaycard Business Solutions explains.

"The biggest challenge for the treasurer these days is dealing with the increasing biodiversity in the payment space," he says. Treasurers now need to accept that consumers today want to have more options for payment and that this will inevitably impact the reconciliation process, in some form or another.

Finding the right solution to this issue will be challenging, but the issue can be overcome with the right support. "Integration is going to be key for the treasurer, and because of that it is important for them to be working with providers who can help bring all of those new payment form factors and channels together into a single account or process and avoid unnecessarily complex reconciliations," he says.

"In an arena where new payments models are continuing to change and evolve, one new payment method doesn't replace another. The most important matter is to offer customers choice by helping make their everyday lives easier. This is a key business principle regardless of the size or the sector your organisation operates within."

## Guarding against fraud

Security should always be at the forefront of the treasurer's mind when dealing with new payments innovations. This may not be such a huge issue with respect to the new consumer payment solutions pioneered by large, well-established technology companies (as a matter of fact, one of the reasons purported for Apple Pay's success is the attention given to the authorisation authentication layer). But it could well be an issue with some of the smaller, more dynamic solutions providers who have been entering the payments space in droves of late.

As Phil Huggins, Vice President of Security Science at Stroz Friedberg, an investigations, intelligence and risk management firm explains, some of these firms may not be as well-resourced on the security side. "Most start-ups are focused on building something that works, something people like, and delivering it quickly," he says. "Writing secure code is, by its very nature, very hard. And start-ups simply don't have the time and resources to focus on security as much in the beginning and so they end up taking on what, in development terms, is called technical debt or security debt, which will need to be paid down at some point."

Besides treating new entrants with a healthy degree of caution is there anything else treasurers can do to minimise the security risks associated with integrating new payments innovations? Huggins recommends ensuring that the new entrants have completed a threat modelling exercise. "It means they need to understand the solution they are building, in terms of the people, the processes, and the technology. Considering what it is that the bad guys are likely to want, why they would want them, and then go through a process of working out the various ways they might attempt to acquire them and how the solution prevents that. Treasurers also need to work with procurement and cyber professionals to complete a cyber supply chain risk assessment, which considers both the secure software development practices of a new entrant, as well as their operational security practices."

CAGR over the same time frame. Can Digital Disbursements enjoy the same rapid take-up as its counterpart in the consumer space is currently seeing?

With the benefits the solution offers, BofA Merrill are confident it will. In addition to aligning its payments solutions for corporate clients with evolving trends in mobile technology, the Digital Disbursements solution can bring about an estimated reduction of in end-to-end disbursement costs by as much as 75% when compared to a physical cheque.

Finally, Digital Disbursements also eliminate the need to obtain and store sensitive bank account information, the problem preventing companies from simply making such payments directly into their customers' bank accounts. A study performed by the Federal Reserve found that 85% of consumers and 81% of businesses prefer not to provide bank account information to the payee when making a payment. "We brought P2P technology over to the corporate side – it's been a big success and we were the first to do it," Leavenworth adds.

## Learning from Bitcoin

There are many other cases where we see innovations in consumer payments beginning to spill over into the corporate banking space. Blockchain, the distributed database behind the popular new digital payment method Bitcoin, is another example. In early 2015, it was announced that three of Australia's biggest lenders, ANZ, Westpac and the Commonwealth Bank of Australia (CBA) are working, or are at least having conversations, with US-based payment technology platform Ripple.

Billed as the world's 'first open-standard, Internet Protocol (IP)-based technology for banks to clear and settle transactions in real-time via a distributed network,' Ripple has the potential to allow banks to make faster payments – in more currencies and into more markets – with lower cost and risk than is possible today. Ripple claims that it can do this because, unlike traditional financial infrastructure, the platform is not tied to governments or third-party intermediaries such as clearing houses.

Instead, Ripple has adopted a similar model to the blockchain (eg a distributed public ledger that is backed and secured by mathematical algorithms) but with a key difference. Unlike the Bitcoin blockchain which relies on mining to create value (a Bitcoin), the Ripple network is powered by participating users agreeing on changes to its ledger every few seconds. As such, banks are able to clear transactions on its network 24/7, 365 days a year in real-time and (by avoiding third parties) without the same level of cost.

Although it is primarily banks that will plug in and use the Ripple network, the speed and low cost that it offers can potentially have a big impact on the service that corporates receive. "Making payments across borders takes time for the bank and incurs costs and – which are ultimately passed onto to the banks' clients," says Dilip Rao, Managing Director Asia Pacific at Ripple. "If a bank uses Ripple, the transaction will cost a lot less and also happens on a near real-time basis, so the cost and efficiency benefits can be passed onto the corporate client."

## Engaging on T&E

More evidence that new consumer payments technologies are increasingly disrupting corporate programmes is offered

by a recent White Paper commissioned by American Express in partnership with PhoCusWright. 'The Path to Innovation: Insights on the New Frequent Traveller', found that corporate travellers, particularly the tech savvy millennial generation, are increasingly aligning their business and leisure expectations.

"This has led to the gamification of corporate expense programmes, with companies seeing incentives, such as allowing employees to retain points earned for business travel, as a way to cultivate programme loyalty," says Piotr T Pogorzelski, Vice President, Global & Multinational Client Group Europe, American Express. "Furthermore, business travellers who are seeing apps and mobile payments replace traditional plastic cards in their personal lives, are beginning to expect the same high tech, hassle free ways to pay when it comes to business travel."

Some might question whether travel expenses are less of a treasury concern and more of a human resources issue. But that is misguided. A study carried out in 2014 by Concur reveals that businesses in the UK spend an estimated £8.2bn a year on T&E. Moreover, in some companies, T&E may constitute one of the largest categories of expenditure; for treasurers then, little to no visibility over T&E spend until a claim form is submitted is far from ideal.

The smartphone – a device which PhoCusWright estimates 92% of business travellers own – might just offer a solution to this problem, while also making the management of T&E more convenient for business travellers as well. Corporate professionals on the road can simply upload and attach hotel invoices or train tickets as and when they need to, making them less likely to lose the documentation or make inaccurate claims.

Managers, then, will have the ability to approve an expenses claim (or reject should it not comply with policy) instantaneously while the accounts payable clerk can more accurately tally the submitted and approved claims. Ultimately, this means that the treasurers and CFOs overseeing it all gain increased visibility of T&E payments and, therefore, have more confidence in the process.

## Treasury catching up

Over recent years, consumers have sped ahead on the innovation curve to embrace the new providers, form factors and other services now revolutionising the retail payments space.

These same innovations are now gradually beginning to permeate the commercial payments space, however. Treasurers may be characterised from time-to-time as a conservative and cautious bunch with respect to 'new-fangled technologies', but now using such innovations increasingly in their everyday lives as consumers. And the more they do, the more impatient they are becoming to use similar tools in their professional lives too.

Now that the demand is there, banks, treasury technology firms and other payments providers are working increasingly hard, and coming up with some highly creative solutions to meet it. There may still be some way to go yet, but if the above examples are anything to go by, it won't be too long before those tech-savvy, early adopters in the treasury department notice little difference between the technologies they use as consumers and those that they interact with during office hours. ■



**Anne Heidemann**

Director, Treasury Front Office, Group Finance & Services



**Kim Japp**

Director, Financial Shared Service Centre, Group Finance & Services

DONG Energy is one of the leading energy groups in Northern Europe. It is headquartered in Denmark. Around 6,500 employees are involved in areas such as oil and natural gas exploration and production, the generation of electricity and heat from offshore wind farms and power stations, and supplying energy to residential and business customers.



DONG Energy, having been created from a merger of six companies in 2006, each with its own procedures, systems and bank relationships, faced the problem of bringing its finance processes into alignment. Treasury Today explores how Nordea's Global Cash Pool and eGateway solutions helped to optimise DONG Energy's performance.

## Problem...

Merging multiple companies is always going to be a challenge – and with more than 200 legal entities in total – the scale of the task involved in managing payments to the company's subsidiaries and joint ventures was enormous. Moreover, the merger created a decentralised structure which brought problems in getting a complete view of the company's funding and liquidity to the table. "We knew it would take some years to align payment terms and contracts, to integrate systems and to merge departments," explains Kim Japp, Director of DONG Energy's Financial Shared Service Centre. "We started with totally decentralised accounting and finance functions in each business unit. It was only in 2011 that we formed our shared services centre (SSC) and centralised payments, by which point we were in a position to look ahead at how we could optimise our transactions and payments," Japp continues. Having been engaged in a close dialogue with Nordea since the merger in 2006, it was a natural choice to turn to this banking partner when the company embarked on an ambitious multi-year programme of activities with the vision of establishing an internal bank and payment factory, as well as a completely centralised treasury function.

## ...Solved

Having worked with DONG Energy in the cash management area for some years, Nordea had a firm understanding of the intricacies of the company's operations. As such, Nordea proposed its new Global Cash Pool solution to provide greater visibility across countries, currencies and accounts. Nordea worked closely with the company to define the rollout phases. The first steps were taken across Denmark, Norway and Sweden in January 2012 and the solution went live in November that year, with the company's numerous UK accounts added to the pool in October 2013. But the company's collaboration with Nordea didn't stop there. After DONG Energy set up an SSC with the ambition to introduce an internal bank and payment factory, the company began looking for a solution that would enable payments to and from all subsidiaries to be centrally approved directly within its SAP system. This time, Nordea proposed that the company migrate to its eGateway solution which would provide the treasury department with greater efficiency and enhanced liquidity management.

The project of simplifying payments with Nordea's eGateway began in December 2013 with a series of ambitious milestones and deadlines that needed to be met. Inevitably – with DONG Energy's complex business structure including many companies and joint ventures that require specific payment processes and handling – there were challenges to overcome. Nordea responded by assigning a project organisation with a dedicated manager to keep stakeholders informed and solve problems. As DONG Energy didn't just contact a service desk, "it helped a lot," explains Anne Heidemann, Director, Treasury Front Office, DONG Energy. "Of course, there were hiccups, but what was important was that everybody collaborated and focused on solving them quickly." The result: the new payments platform was live by the end of September 2014 (during the same year, the company's cash pooling solution was also extended to handle internal balance transfers with support the new internal bank model).

Both solutions (Nordea's Global Cash Pool and eGateway) are fully integrated into the company's SAP and treasury management system, as well as the shared services and treasury processes. "These have been two major projects and the implementation has been a complete success. Now DONG Energy has truly updated, modernised and enhanced its core finance processes, producing tangible results," says Japp. Both Japp and Heidemann also note that no comprehensive business change is easy, but the results are often worth the complex transition phase. "The collaboration between DONG Energy and Nordea has produced real benefits in cash management," explains Japp. "We have much more solid payment processes now, which is saving us money as well as reducing operational risk. It's hard to overstate the value this delivers to the business." ■

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# Trading places

*The last two decades have seen a seismic shift in global trade corridors. Where once trade was conducted primarily between developed western nations; today, emerging markets, and more specifically Asia, are now at the heart of those flows. So with trading relationships extending further afield and encompassing a broader range of companies than ever before, what has the impact been on international treasurers?*

Over the course of history, global trade flows have continually shifted. For instance, in the 1800s, Asia sat at the heart of global trade until the industrial revolution propelled North America and Europe ahead, eroding Asia's share to a fraction of what it was before. Western nations continued to dominate trade up until the 1990s when another shift began to occur, this time towards emerging markets (EMs).

EMs now account for nearly half of world exports – up from one fifth in 1990. And according to the IMF one-third of the \$15trn of global trade is now conducted between emerging and developing economies, known commonly as south-south trade.

At the heart of these new (or in many cases re-opening) global corridors is Asia. UNCTAD figures suggest that Asia now accounts for over 80% of all south-south exports and that nearly three-quarters of this figure can be attributed to Asian countries trading with each other. China is the engine of the region, accounting for 11.5% of global exports – surpassing the United States in 2013 as the world's largest trading nation.

## North becomes South

The changes in global trade flows cannot be attributed to one key factor; instead they are the result of a variety of shifts and events in the wider world over the past few decades. For starters, geopolitical developments such as the break-up of the Soviet Union and the opening up of emerging economies have played a significant role. Improvements and a reduction in the price of communication technology, thanks to the rise of the internet, has also played an important role in making the world smaller and more interconnected, while the creation of trade bodies such as the WTO in 1995 has looked to regulate global trade and allow it to flow freer and fairer.

Using these developments as a springboard, EMs have blossomed as their governments have liberalised trade, recognising the economic benefits afforded to them by adopting an export-led economy. For instance, countries such as China have been able to build up their capital account balances, drive international best practices domestically, improve the productivity and standards of local firms, bring more jobs and FDI and also increase their competitiveness on the global stage.

Regional and bi-lateral trade agreements, which have proliferated in recent years, have been used to further widen the new trade corridors. Agreements such as ASEAN in 1992 and NAFTA in 1994 and the creation of the single currency in the Eurozone in

1999 are some of the headline announcements. But bi-lateral agreements between emerging nations, whilst not always widely spoken about in the mainstream press, have been just as vital. As Nick Diamond, Head of Global Corporates, Transaction Banking Europe at Standard Chartered explains: "These agreements not only offer a number of benefits including a reduction in tariffs and tax charges, but underneath the agreements there is also a clear indication by these countries to allow investment and make it easier for corporates to do business there."

With it now easier to do business in many EMs around the world, corporates have taken the opportunity to transform their supply chains and trade policies, adopting a model known as the vertical supply chain. In a vertical chain the basic functions in the production cycle are outsourced to countries with low labour costs and the higher skilled functions are kept in traditionally more high-skilled countries – Apple's goods, for instance, are designed in California and assembled in China.

The other popular method, the horizontal supply chain, sees parts sourced from countries with similar wage levels where specialist skills are sought after. Aeroplane manufacturer Boeing is a prime example of this, as the company imports many of their parts from highly developed western economies such as the UK, as well as Japan, before assembling the plane in the US.

## Changing trade instruments

Although corporates have undoubtedly reaped many cost benefits from the vertical supply chain model, it has also increased their complexity and risk. Supply chains of today often involve dozens and sometimes thousands of suppliers located around the world. This risk is magnified when one considers how many of these suppliers are located in emerging Asian markets.

Of course, dealing with companies in EMs can be a risky business. Non-payment, fraud, corruption, geo-political disruption and natural disasters are just a handful of the potential threats a company can be exposed to. As a result of this, corporate treasurers around the world are beginning to place increasing emphasis on understanding their trade flows and counterparties. "Historically in Europe treasurers touched on trade – but many didn't see it as something core to their function," says Peter Jameson, Co-head of Product Management, Global Transaction Services for EMEA at Bank of American Merrill Lynch (BofAML). "In the last few years

## Manufacturing moves West

The growth of vertical supply chains has transformed China and has seen the country nicknamed 'the factory of the world', sitting at the heart of many global supply chains. China has been able to take the lead in this regard because its vast population has allowed for huge volumes of output and also for labour costs to be kept low. In fact, the rise of China as a global supplier is staggering: in the 1990s, China produced less than 3% of global manufacturing output by value, but joining the WTO in 2001 proved to be the catalyst for economic and trade policy reforms which has propelled China into being the world's largest exporter. The country produces nearly 25% of global goods.

But recent signs suggest China may be intentionally loosening its grip as the world's manufacturing hub as it shifts towards a more consumption-based economy, looks to expand its service sector, and its middle class grows. These developments are seeing workers in China demanding higher wages and thus the cost of business is increasing.

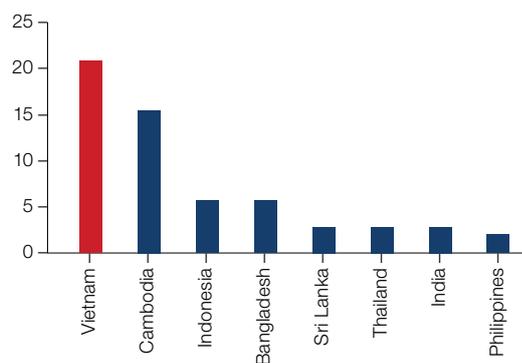
With the vertical supply chain model being built on low-cost labour and materials, China's attractiveness may therefore decline. "We are already seeing a shift in trade corridors because of this," says Standard Chartered's Diamond. "There are clear signs that manufacturing is moving west, away from China and into other countries primarily in the ASEAN region, such as Vietnam and the Philippines, and also India." In fact, in July this year Taiwanese manufacturer Foxconn announced that it would be looking to shift some of its manufacturing to India due to increasing costs in China.

This is not, however, an unexpected development. Asia operates under what Standard Chartered calls a 'flying geese strategy' where manufacturing moves away once a country reaches a certain economic level. This has already been seen in Korea and Taiwan, for instance, morph from low-cost manufacturing centres, to developers and consumers of sophisticated products and services. China, many experts now believe, is at this stage. It is expected that trade will therefore continue to move gradually east towards the Indian-subcontinent and eventually Africa as China continues to develop.

The sheer size of China does mean that it will still have a part to play in manufacturing moving forward, however. Its capacity is too large to be consumed entirely by other nations in the region. And despite its decreasing role in manufacturing, its presence in global trade looks set to increase. "China is repositioning itself to become a mega-trader and as a gateway to the new Silk Road linking up emerging markets and being at the centre of south-south trade. We are seeing the Chinese government investing heavily in this," says Diamond.

**Chart 1: Alternative locations for manufacturing outside of China**

Number of respondents



Source: Standard Chartered research

however, we have really begun to see our clients think of risk mitigation solutions through trade as a requirement."

Corporates are placing increasing focus on the trade instruments that they use both to finance trade and to mitigate risk. Although the new corridors haven't changed the products which are available that much – letters of credit (LCs), risk mitigation techniques, guarantees and receivables solutions are all still widely available – there has been a change in the popularity of certain products. As Baihas Baghdadi, Managing Director, Head of Trade and Working Capital International at Barclays explains: "Some decades ago, LCs and bank guarantees were the most widely used trade instruments, no matter the size of the counterparty. Today, however, they are secondary in the conversation." The most popular solution that corporates ask Barclays for now is the open account.

It may seem peculiar that the general trend in global trade, even sometimes in risky markets, is away from LCs – tools traditionally used to mitigate risk – and towards open account transactions where there is no protection. But there is a good reason for this. Kuresh Sarjan, Head of Asia Pacific Trade and Supply Chain Finance at BofAML, explains that "we have seen

lots of clients bolster their own credit functions in recent years, as a result of this they have turned counterparty risk into an art form." In doing so, corporates have been able to move away from pricey and document-heavy LCs and towards open account. "Should there be any question marks corporates might look to use risk mitigating products such as insurance, for the extra piece of mind." It is worth noting, though, that whilst LCs are arguably decreasing in popularity, they are still a crucial factor in trade and also can serve as collateral in transactions.

The bank payment obligation (BPO) however, may be a tool which will radically transform the trade landscape. The solution functions similarly to the traditional LC, but utilises fully automated electronic transmissions to increase efficiency and enhance risk mitigation. Since the first BPO transaction took place between BP Aromatics and Oman-based Octal Petrochemicals in 2011 progress has been slow, despite the International Chamber of Commerce issuing rules to govern the solution in 2013.

Yet, in recent months the BPO has once again moved into the headlines, thanks in part to the recent BPO+ transaction

which utilised full electronic documents to complete the transactions. With these new developments it is hoped that the solution will gain traction.

## The case for flexibility

Away from the instruments corporates can use, there has been an increasing focus in the years following the financial crisis around stable and sustainable supply chains as well as the need for flexibility. "Every change in the global environment brings along new opportunities but also new challenges," says Barclays' Baghdadi. For example, the recent political troubles in Thailand may have caused disruption to some supply chains, especially in the technology sectors. As a result of the increased risks, some firms in developed economies have begun to question whether the costs of outsourcing certain essential stages of the production process may outweigh the benefits.

"Corporates are therefore placing increasing emphasis on diversifying their supply chains and, in some cases, onshoring elements of the production process. This reduces the dependence on these suppliers and can save costs at times when oil prices are high due to the reduced need to transport the goods," says Baghdadi. This may also be occurring, according to Baghdadi, due to the changing nature of consumer behaviour and the desire to reduce the time to market in the fast moving consumer goods sector.

Onshoring is something that Bart Ras, Global Head Business Development, Global Trade and Receivables Finance at HSBC is also seeing occur in the market. But this is not to say that offshoring is a thing of the past. "Corporates are developing hybrid supply chains that are extremely flexible. Some companies, for example, may decide to have 80% of the production process offshore to reap the benefits that this offers. Twenty percent may then be left closer to the market." Ras is also seeing some corporates being strategic in their procurement as a way to reduce dependence on certain suppliers. "Some of our clients look to procure large volumes of stock from core suppliers, this gives them a buffer should the supplier suffer from difficulties, be it financial or otherwise. Dual-sourcing or even multi-sourcing where possible are other possible strategies."

The changing demographics and economic situations of many Asian economies may also see corporates once again change their supply chain philosophy. As these markets modernise and become more consumer orientated, it may be pertinent to keep some manufacturing in these markets despite the increasing costs. The reason: these regional supply chains will help reduce the impact of currency volatility and also match the speed of change in client and consumer requirements. For Ras, it is those companies who really think about their supply chain and turn it into an art form that are the most successful in today's world.

## Supporting the supply chain

However, for corporates and their supply chains, there may be another risk looming. The glut of regulation that has been placed on the financial services industry, not least Basel III, has reduced the ability for banks to lend to smaller players, leaving a significant, and growing, financing gap. In Asia alone, the Asian Development Bank estimates that the gap is as much as \$425bn. With key players in supply chains therefore struggling

to keep their heads above water, what can larger corporates do to ensure the health of their supply chain?

"We have seen an increased focus on the management of working capital since the financial crisis," says HSBC's Ras, "but what is becoming more important for more clients is the health of their supply chain, both up and down stream." Corporates are beginning to actively monitor their counterparties' liquidity positions and working capital to ensure they know if others are suffering from financial difficulties. This also provides insight into whether production can be accelerated or decelerated without causing difficulties.

One of the implications of Basel III, and shrinking bank lending, is that the responsibility of supporting supply chains financially is increasingly falling onto corporates. As a result, supply chain finance (SCF) is a product that many treasurers of large organisations are eager to explore. "In Asia, there is a fundamental shift towards SCF," says BofAML's Sarjan. "Often corporates are sitting on large cash reserves and are looking at ways to optimise this cash and in turn ensure the sustainability of their supply chain."

The increasing interest in SCF is also occurring in Europe. "We are having lots of dialogue around the solution with our clients," says BofAML's Jameson. "It can be a long process and many clients have to spend a lot of time considering what it means for them, their customers and their suppliers." Jameson is also keen to point out that in Europe there can be an important reputational angle to SCF and its impact on suppliers.

## An ever-changing world

Whilst there may be a level of uncertainty around SCF, what is certain is that the importance of trade looks set to increase and corporates must make the most of changing dynamics. Big four consultancy firm EY expects that the value of global trade will continue to proliferate, predicting the total of goods traded to reach around \$35trn in 2020, two and a half times the value of trade in 2010. EY also expects that the changing nature of global trade patterns, which increased following the global financial crisis, will continue.

As mentioned earlier, emerging Asia will play an ever-more critical role in global trade with manufacturing moving into the ASEAN region and the Indian subcontinent. Trade flows between China and India, for instance, are expected to account for one-fifth of global trade by 2020. We can also expect to see activity in Latin America and Africa increase as these regions continue to develop. "Africa has the potential to cause a seismic shift in global trade flows, but this will be down to a continued social, political and economic stability," says BofAML's Jameson. There are also lots of questions that remain around whether Africa can position itself as a low cost manufacturing region, in addition to the existing flows driven by infrastructure investment and flows of natural resources.

Of course, with the landscape continuing to evolve, support will be needed. "Every country is trying to promote trade," says BofAML's Sarjan. "So corporates need to be aware of the benefits and challenges posed by each market and ensure they are taking full advantage of these by adopting the correct solutions." With this in mind, corporates should take extra care when choosing banking partners for their trade transactions, to ensure that they can support the organisation across these key markets. ■

# BREAKING DOWN THE BARRIERS BETWEEN TREASURY AND RAW MATERIAL PROCUREMENT

Many corporates have considerable exposure to commodity and currency risk through their supply chain. But in today's highly volatile markets, companies can no longer effectively manage these two risks across separate treasury and procurement functions. Treasurers in industries ranging from manufacturing, retail, food and beverage, to airlines now need visibility to currency and commodity price risks across their business. Procurement divisions must have sophisticated, agile management of their physical commodity exposure and input prices as well as the currency risk associated with those commodity exposures.

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# Lloyds Bank strengthens European commitment

*To prosper globally, corporates must inevitably look beyond their traditional markets. With perceived instability in Europe however, treasurers want certainty. That means banking partners they can rely on to support their expansion. In this article, Lloyds Bank outlines how its strategic European focus aims to help corporates find growth across the UK and Europe, with an emphasis on commitment, strategic advice and tailored solutions.*

Given Lloyds Banking Group's strong position in the UK market and its sterling expertise, there is occasionally a perception among corporates that the bank is best suited to meeting the needs of British domestic clients only. Now – in 2015, the 250<sup>th</sup> anniversary of Lloyds Bank – it is time to change that misconception.

As Farouk Ramzan, Head of Commercial Banking Europe, Lloyds Bank says: “We have a strong balance sheet, and a long European history, together with an on-the-ground presence in key locations across the continent.” In fact, Lloyds Bank first entered the French market in 1911 and had set up nine branches in the country by 1938. The world is a very different place now but the Commercial Banking division aims to reinforce its client relationships by having an in-country presence in Frankfurt, Paris and Amsterdam.

“We have a strong balance sheet, and a long European history, together with an on-the-ground presence in key locations across the continent.”

The bank believes that now is an ideal time to be strengthening its European commitment because of the perceived volatility across the continent, driven by economic and political instability. “With the increased focus on counterparty risk, treasurers have to be able to know that the banks in which they place their trust and their money – whether it is investment or working capital – are safe and are committed long-term players. Commitment and stability underpin Lloyds Bank's cultural DNA and the bank is a stable entity in an otherwise turbulent operating environment across Europe.”

## Gateway to growth

“What is more, we are making a strategic commitment to European growth going forward.” The bank's focus, says Ramzan, is on developing even stronger relationships with existing European clients and helping new-to-bank clients to grow, across Europe and the Nordic region. “We support both European parents with UK subsidiaries and UK parents with European subsidiaries – with the aim of helping Britain prosper, globally,” he notes.

“With that in mind, we want to make sure that we provide a UK service element to all of our clients – which means delivering added-value through our product suite within the UK and complementing clients' multinational needs with our expertise in the international capital markets, derivatives, and project lending, for instance. We can do this by connecting our clients in need of capital by providing safe and reliable access to international funding markets. We can also work together with all major industry sectors and provide a comprehensive suite of capital markets, financial markets and global transaction banking product propositions,” explains Ramzan.

This two-way flow (in and out of the UK) is key to maximising growth opportunities, Ramzan believes. Lloyds Bank, for example, recently financed one of Europe's largest engineering companies in an infrastructure project that's set to create hundreds of jobs over the course of this year and 2016 in the North of England. Indeed, foreign direct investment (FDI) in the UK as a whole increased to £27,211m in the first quarter of 2015, up from £11,944m in the fourth quarter of 2014. Outward flows have been on the rise too. In 2014, for instance, UK corporates raised more than 70% of their bond and medium-term note funding from outside the UK.\*

\*Source: Office for National Statistics

Depending on the product in question, seamless delivery of this proposition involves Lloyds Bank working with a carefully selected network of partner banks, as well as utilising its existing European offices. “For a treasurer who operates in a number of those European geographies, it should feel like a streamlined holistic experience. We take this very seriously,” says Ramzan.

“Whilst all of the products that we offer are booked out of London, we also ensure that we gravitate towards where the corporate’s decision-making is done. So, if we are dealing with a decentralised company where FX and associated activities are completed locally, for example, we have local relationship managers on the ground in Europe to service those local needs. In short, we make sure that our product and service delivery model is flexible enough to accommodate different corporate structures and decision-making processes.”

## A valued relationship

The bank has embedded very clear values in its organisational culture to build valued relationships:

1. **Putting clients first** means thinking about clients first in everything we do, understanding and anticipating clients’ needs, delivering on our promises to clients and each other and taking ownership to get things right for clients.
2. **Keeping it simple** means making ourselves easy to do business with, communicating clearly and openly, identifying opportunities to simplify the things we do and working to get things right first time every time.
3. **Making a difference together** means working together to deliver for clients, using feedback to improve what we do, treating people fairly and acting responsibly at all times and contributing positively to the communities we serve.

## Unwavering support

In practical terms, these values manifest themselves in a variety of ways throughout the bank’s product and service offerings. Consistently providing good quality advice and sound execution is a good example, says Ramzan. “After all, it is one thing having a range of products suitable for the task in hand, but it is another thing being trusted to provide minimal execution risk alongside those products.” Lloyds Bank’s commitment to clients is that when a product or service is offered, it will be followed through from start to finish, with a focus on mitigating risk along the entire journey.

However, Ramzan does acknowledge that there are some risks that treasurers and their banks will never be able to fully protect themselves from: “political risk, for instance, is a part of the world we live in. Nevertheless, we aim to help our clients through the volatility by ensuring they have a good source of advice and strong execution around the products and services we provide. What we are trying to do is make sure that we truly offer a service that is built for the long-term success of our clients.”

As a complement to its product suite, Lloyds Bank is committed to providing up-to-date technical and regulatory information to clients – both around the wider industry impact of regulation and the impact on specific areas of business operations, such as treasury.

## Product suite

The bank offers corporate clients a very clearly defined product suite which includes the following areas:

- **Financing:** includes award-winning teams that provide a range of capital markets solutions, as well as providing financing solutions to fund international trade and working capital. Revolving credit facilities and asset financing are also offered.
- **Risk management:** Lloyds Bank’s products will help manage interest rate risk, foreign exchange (FX) risk, inflation risk, and commodities risk as well as providing guidance on International Finance Reporting Standards (IFRS). The bank offers a dedicated 24-hour FX dealing team and bespoke solutions to manage associated risk, including insights into competitor activity and sector trends.
- **Cash management:** a full range of comprehensive services are on offer and also available online.
- **Deposits:** whether the priority is security, yield or return, Lloyds Bank will ensure deposit strategies meet the liquidity requirements of the business.
- **International trade:** providing banking solutions to access currency accounts across Europe and beyond, as well as ensuring the right financing is in place.

Solutions are continually evolving and expanding. They can be tailored and account for client needs, as well as market developments. For an extensive list of all corporate products and services, please see [www.lloydsbank.com/commercial](http://www.lloydsbank.com/commercial)

“What we are trying to do is be very clear about the effects of regulation and how these are filtering through to our client base. Take the debate around cash versus liquidity, for instance, which has been going on for some time now. Treasurers increasingly need to be taking on the role of liquidity manager and that necessarily involves being an asset manager,” says Ramzan.

By and large, treasurers are taking on this broader remit, but the bank is also doing all it can to help them strategically in the liquidity versus cash debate. This requires an ability to tailor the product suite to match individual client needs, as well as a deep understanding of their business. Lloyds Bank has also set-up a dedicated strategic liquidity team to help their clients find and implement optimal liquidity solutions.

## The human touch

To facilitate this level of understanding, and to continue to grow the bank’s client base, Ramzan explains that hiring and retaining the best people remains a strategic priority for the bank. “We will continue to partner new and existing clients with the right relationship manager(s) and the right senior bankers, who recognise the sensitivities of clients’ industry sectors, and who have a solid history of working at the C-suite level with similar clients,” he says. “It’s not just a case of knowing what automotive companies are doing in Europe, for instance, it is knowing what these companies are doing globally, how the sector in Europe is idiosyncratically different, and what tailored services those companies are looking for as a result.”

The sector aligned relationship teams also help identify areas where the bank itself can add real value to corporate operations, and safely invest in its business, as part of Lloyds Bank’s commitment to being a long-term banking partner for corporates across Europe. This is a particularly important theme for Ramzan, given that the market has seen the demise of global banks over the last five to ten years, with many retrenching from European geographies, leaving their clients up in the air.

“What we are trying to do is be very clear about the effects of regulation and how these are filtering through to our client base. Take the debate around cash versus liquidity, for instance, which has been going on for some time now. Treasurers increasingly need to be taking on the role of liquidity manager and that necessarily involves being an asset manager.”

“Lloyds Bank is an international bank, not a global bank. We know what we do well and our strategy is to focus on what we do best. Ultimately, we do what is best for our clients in the long term, and that is what really separates us from our peers. We are a very solid British bank that has an attractive regional capability which we continue to invest in, to the benefit of European corporates,” Ramzan concludes.



Farouk Ramzan is Head of Commercial Banking, Europe at Lloyds Bank. He began his career in 1990 at Kleinwort Benson’s International Corporate Finance division.

Following two years in the International Structured Products Group marketing tax based financing structures (1993-1995), Ramzan joined Global Debt Origination at Dresdner Kleinwort originating bonds for corporates and financials in the UK and USA. Between 1999 and 2001 he continued this role in New York, returning to the UK in 2001 with Société Générale where he was Head of UK/US/Australasian DCM Corporate Origination (covering Loans, Bonds, Securitisation and Tax & Debt Advisory).

In 2007 Ramzan moved to Lloyds as Head of Capital Markets Origination (consisting of global Debt Capital Markets for corporate and financial institution clients as well as global Capital Structuring Advisory and Ratings). Most recently, in November 2014, Ramzan began his European Commercial Banking role that encompasses all the European coverage, product and delivery activity across the whole client base for the Commercial Bank at Lloyds Bank.

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**LLOYDS BANK**





## The art of being there

**James Koh**  
Group Treasurer

### VERTU

Having built a number of treasuries from scratch, including his current team at Vertu, James Koh has accumulated a wealth of knowledge, experience and friendships on his journey so far. He tells Treasury Today how his early mentors shaped his view of the world for the better.

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*Vertu is a British manufacturer and retailer of luxury, handmade mobile phones, with offices across the world. It was established by Nokia in 1998 and in October 2012 was sold to private equity group, EQT VI. Vertu phones are handmade in its factory in Hampshire, England, with the emphasis on craftsmanship. The current range, which starts at around £4,000, is sold through around 500 stores, including 70 Vertu-owned boutiques, in 66 countries. The business has 1,000 employees.*

From Malaysia to the UK via Australia, and from banking to luxury retailer via travel, finance and telecoms, by his own admission, James Koh has always managed to be in the right place at the right time. He says it is luck, but there is strong evidence that he has worked hard to get where he is today, having seen and taken every opportunity that came his way.

After school in Malaysia, Koh spent a brief period in banking before heading off to Macquarie University in Australia. Graduating with a Bachelor's Degree in Economics, majoring

in Accounting and Financial Management, he set his sights on qualifying as an accountant. In the mid-1980s he moved to the UK to find work, pitching up with the asset management company, Oppenheimer, as a fund management accountant. A position managing repo valuations at Kidder Peabody Securities awaited him in his next move, but with an eye on his first steps into treasury, Koh switched tack and found himself at holiday firm, Owners Abroad (later known as First Choice, now part of TUJ). Here he met his first real challenge, being asked to establish an internal audit department and a

group treasury function. "I took the challenge, set them up and started learning treasury from scratch; it was very hands-on," Koh recalls. He was guided in the treasurer role by one Geoffrey Stone, who became Koh's mentor, steering him through some of the intricacies of the job as both he and the company went from strength to strength.

## The A to Z of treasury

From his first exploratory steps at First Choice, Koh moved to Lombard, a financial services firm that was part of NatWest bank. "Here I met my second great mentor, David Loosley, who took me under his wing." Under his tutelage, Koh says he grew quickly. Loosley's "no-nonsense" approach ensured the team of 12 efficiently managed internal treasury for five banks, Koh also managing to attain Associate of the Chartered Institute of Bankers (ACIB) and Member of the Association of Corporate Treasurers (MCT) letters in the process. Further study was deemed a necessary part of the plan to advance his career, states Koh. "As a young man, I decided to do all my letters and now I have A to Z," he jokes.

The exacting nature of Loosley's regime saw Koh extend his knowledge into a broader field of finance than he might otherwise have experienced. Thus armed, when Lombard was acquired by RBS, he was given the task of integrating the internal treasury functions as Loosley moved on to GEC Marconi. Following a successful project at RBS, the call came to reunite with Loosley. At that stage, GEC Marconi was the largest FTSE 100 firm: "What an accolade," says Koh of his call to arms. What an opportunity to learn too: with GEC transforming into Marconi, Koh was appointed as Treasurer of Marconi Finance, running the company's global treasury team, with offices in the UK, EMEA and the US. "Running a global treasury team is quite different – and launching a Eurobond and EIB vendor financing was exciting too. It all gave me the kind of international exposure I was hungry for."

Marconi went into liquidation during Koh's tenure (no fault of treasury), giving him unexpected hands-on experience of winding-down books and operating under strict INSOL Principles. "It was a very rigorous process; it took me a couple of months before handing it over and moving on," he recalls. With an opportunistic eye he moved into the consultancy and interim field, feeling that he was ready to expand his repertoire.

The next phase of his career saw him taking senior treasury roles across a range of sectors, either setting up corporate treasury teams from scratch (both domestic and international), taking established units to the next stage and implementing finance and treasury transformation programmes. These included amongst others RBS, Direct Wines, Fortress Investments Inc, Travel City Direct, Cendent Corporation (Travelport), Courts and Burberry. Having accumulated a wealth of hands-on experience, exposure and friendships in the interim line, after eight years Koh decided to head back to a permanent Group Treasurer position. In December 2011 he joined Vertu, a UK-based manufacturer of ultra-high-end mobile phones, as Group Treasurer, his task once more to carve out and establish a group treasury function from scratch.

## From public to PE

Koh joined Vertu as it was divested from Nokia and transferred to Nordic private equity (PE) group, EQT. Vertu's customers are located all over the world, buying from top-end boutiques and stores. It required a truly international treasury,

offering a centralised take on treasury policy, strategy and traditional operational activities such as treasury risk management, liquidity management, cash pooling funding, FX and establishing key banking relationships.

As part of a PE house, treasury must take a slightly different approach. Having experienced many forms of ownership over the years, the key difference for Koh is that whilst the 'cash is king' mantra still holds true, it has more intensity about it than in other business ownership models. "It's about counting the pennies; there are plenty of them, but everything is under scrutiny – and so it should be," he comments. "I find that the regime is much more rigorous; these are expert investors and they expect a professional treasury – and they get one."

A major difference between Vertu and other corporates on Koh's CV is the amount which its customers pay in a single transaction. Although some use bank transfers, the majority are card transactions. The volumes are not especially large but the values can become "exceedingly high." Vertu's stock-in-trade is exclusive, hand-crafted mobile phones aimed at a market that typically does not have to ask the price before buying (the average, if you do have to ask, is around £7,000 but the highly customised versions can rise substantially higher). This creates an interesting profile in terms of online Cardholder Not Present transactions and fraud prevention; the typical automated fraud solution "is just not good enough," notes Koh.

In response, Vertu deploys an in-house security team, to look after the best interest of the customer, customer data protection and payments. In-store is reliant upon the skill and judgement of the team at the point of sale and they must adhere to policy guidelines. However, because the phones are often bought as bespoke items, the lead time between order and delivery affords Vertu the necessary window to carry out due diligence.

## An eye for technology

The delivery of a successful treasury team is in no small part due to deployment of the right technology, and Koh likes to keep abreast of developments in this space. "I am always on the lookout for sensible improvements," he says. "If you run multiple bank accounts on a global basis with multi-currency cash flows and you have to consolidate the start and forecast close position – including rolling cash flow forecasts – automation is extremely important, especially when your boss wants it yesterday." In treasuries the world over, spreadsheets persist "because treasurers can tailor them to meet their needs." But when it comes to cash flow forecasting, behaviouralisation for timings, leads and lags is an ongoing quest for Koh. By looking at local activities to determine the actual ebb and flow of cash, it is, he says, possible to manage cash flows based on expectations rather than contractual terms. However, he is yet to find a good cash flow reporting and forecasting tool which also incorporates the cash behaviouralisation assumptions on a necessary dynamic basis. "Maybe I will invent the first one!"

## Market challenges

There are certain countries where treasurers face additional demands on their skill and judgement. Some, currently subject to trade sanctions, happen to be within Vertu's current distribution. Facing entrenched bureaucracy, tight regulation and certain difficulty when repatriating cash must be tackled intelligently and sensitively. "Obviously we try to use local currency to pay wherever possible rather than having to convert," says Koh. "We directly repatriate via trade payments

and convert only the net long positions.” Vertu also takes action in terms of its pricing. While its margins are generally fairly stable, pricing can be used to mitigate global FX volatility in extreme cases. This is ‘best practice’ for the luxury goods market and, to a degree, customers are less sensitive to price volatility. “If you have forward FX contracts in those markets you would probably be badly burnt,” Koh explains. The team nonetheless carries out relentless stress testing to determine how much it needs to move to mitigate these volatilities.

Having worked many years in banking and treasury, Koh feels he has never been busier than now, not least because global liquidity management, finance change management, sanctions and regulations are an ongoing theme for him. They will always require a response and he knows he must be both aware of and in compliance with all that comes his way. “I deal with all the internal and external treasury matters – that is my bread and butter – but at Vertu we do trade in regulated markets and for that I find that the best information comes from our own local people on the ground.” Koh says that he also talks to other treasury professionals in similar markets, and expert providers, enabling him to assess the changing mood of the industry, and his local and global banking partners help out in an advisory capacity too.

## Befriending the banks

Banks are natural facilitators in practical treasury operations and Koh says he considers some of his key banking partners as friends, having known them for many years and taken the finest exponents on the journey with him. Having come from a financial services and banking background, he understands what many financial institutions have gone through recently. “Many have taken a lot of flak, rightly or wrongly. Now, from the treasury side of the fence, of course I insist on the best I can get from friends who are still within banks.” His policy is to be clear about his expectations and time-frames so no one should be under any illusion as to what must be delivered. If a mandate is awarded then both sides should go all out to make it happen within the deadline. “If you are fair with the banks, they will go the extra mile for you,” he believes.

## Softer side of treasury

Cultivating strong working relationships with the key stakeholders, the treasury team and external providers are a vital part of Koh’s armoury. Drawn from his breadth and depth of experience, the so-called ‘soft skills’ of people management, negotiation and influence are, he feels, an essential element of a best-in-class treasury function. “When you are looking to deliver in very tight deadlines and you have a team of providers helping you out, as well as an internal team that works alongside you, things are so much easier to accomplish.”

To draw the best deals out of banks and vendors, and to encourage the team to buy into plans and targets, negotiation skills have to be “spot on,” he believes. “If you go head-on into conflict you get nowhere.” The skill to influence is vital too, he says. Of course, he has his own views in terms of what the best solutions may be, and these may not accord with the views of another. But in seeking the best course of action, enabling and convincing stakeholders to see that there are better alternative ways of achieving the same goal is important.

Building the right team is the best way to succeed. Koh knows that many CFOs and CEOs expect the incumbent to hit the ground running and one of the most important elements, alongside aspects such as treasury strategy and policy, he

states, is in getting the right people on board. This is where his experience with previous teams and his mentoring and networking activities, and those well-honed soft skills, all come in handy; he knows who works well and who will fit in. In this space he says relationships tend to be long-lasting “and treasurers have a very good memory of who is good and who is not.”

## The right choice

Having considered his options en route, Koh knows now that he has taken the right course, not just with Vertu but with his career too. “I didn’t just want to be an accountant; there’s nothing wrong with that but it is not really my cup of tea, I wanted to expand on that.” Treasury, he feels, gets him involved in different functions and, when the need arises, “allows me to really put the pedal to the metal.” And building a global treasury function from scratch “really is my cup of tea,” he states. On top of all this, he feels that he has been truly feted in his chosen path, citing his win at the Treasury Today Adam Smith Awards in 2013 for ‘Best MME/SME Treasury Solution’ as a highlight.

As his career has progressed, Koh feels lucky to have been mentored by two experts in their field and he has made the most of their advice. The cumulative benefit of this experience is something he wishes to pass on to others. To this end he is currently mentoring the treasury team at Vertu. It is, he states, “a pleasure for me to be able to see my staff excelling in their ACT letters and being able to mentor, fast-track and shape their treasury skills and see them grow.” To other individuals looking for their first step on the rung, Koh says finding the right mentor is the luckiest break anyone can get. “Don’t think you know everything until you have worked with the very best,” he says. “It takes time and you will make mistakes but make sure you learn from them.”

As younger practitioners come up through the ranks and start taking on more responsibility, Koh is pragmatic about the steep learning curve, always very much aware of the need to look out for “the first big mistake,” hopefully catching it before it happens. “I encourage anyone starting out in treasury to double and triple check with the treasurer if they are unsure before they execute,” he advises. “If you make a mistake as an accountant you can do a correcting journal; as a treasurer, you cannot do that and need to get it right first time, every time.” One way in which he is able to rein in over-enthusiasm is by literally keeping an ear open for errors. “I keep telling my team members to make a lot of noise; if they are noisy I know what’s going on; if they are quiet then I worry.”

## A late career move?

With the volume and intensity of his particular operation turned to max, it might be expected that Koh has adopted some tranquil pastime to while away the hours. Nothing of the sort: he enters the high octane world of motorsport, power-sliding his BMW M3 around the chicanes and hairpins of the race track. He does also donate his time freely to a couple of charities as a way of “doing his bit,” but he has an equally fast-paced alternative career option lined up, taking to the streets as an “Interceptor Cop,” driving fast cars and chasing down the baddies. Whilst waiting for the call to kick-start his crime-fighting career, treasury still manages to offer him some very exciting moments, especially when he is building a team from scratch. He may not have super-villains to apprehend but when faced with a blank treasury canvas, where a lesser mortal might wilt under the pressure, Koh will already be making his mark. ■



## THE INDUSTRY VIEW

### Bea Rodriguez

Managing Director, Co-Head of International Cash Management and Chief Investment Officer for the Sterling and Euro Cash team

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*With negative rates, increasingly scarce liquidity in the money markets and regulatory upheaval in both Europe and the US, these are very challenging times for the corporate investor. In this article, Bea Rodriguez, Managing Director, Co-Head of International Cash Management and Chief Investment Officer for the Sterling and Euro Cash team at BlackRock describes how the liquidity management environment for corporates is changing, and outlines some of the alternative investment opportunities now being explored as a consequence.*

#### How would you describe the liquidity management environment for corporates at the present time?

'Challenging' is the word most of our clients are using to describe it. In any other historical period, a negative money market environment would probably have led to the vanishing or the 'gumming up' of that market completely. What negative rates tend to do is take out liquidity in an extreme way and collapse flow. What's different this time around is that we are undergoing enormous change in regulatory architecture with Basel III which is dislocating money from banks and setting money in motion. It is this new dynamic which also means that negative rates may not only be a feature of currencies with negative deposit rates and we are still discovering the new steady state for money markets in general.

#### How are treasurers responding to these new realities? Is there a need for treasurers to evolve their investment policies in order to adjust to these new realities?

We were in close dialogue with our corporate client base as the market headed into negative territory and, while it is certainly not very palatable from their perspective, there is an understanding amongst most clients that this is just where rates are at the moment.

What is interesting is that we are starting to see a little bit of disparity amongst our investor base in terms of the response. The responses range from those of some larger corporates, who are accepting the situation and still see capital preservation as their primary investment objective, to others that are really

trying to offset the negative impact and using this as an opportunity to segregate their cash a little bit more. Then we have those who are spending more to reduce the amount of cash they are holding. It's not a natural thing to accept dealing with a negative for your cash – whether that is your own cash or your company's – it just doesn't sit well. As a result, it has even prompted some of our investors to look at taking on more risk and given the volatility we currently have in the market this needs to be very carefully considered.

We do think that the new investment realities treasurers are now facing mean that a more flexible approach within policies, or the ability to review them more often, will be required as we go through the next couple of years. A lot of corporates currently take an annualised approach to reviewing their investment policies, but that might not be enough. They need to be having dialogue with their boards around this changing landscape and really work out what the right policy is for them. Preservation of principal should remain the priority, though, because one of our biggest concerns at the moment is that the environment is pushing investors to take on too much additional unnecessary risk.

### **What in your view is the best strategy for corporate investors at the moment with respect to yield?**

Our advice to treasurers is to be very wary of stretching for yield because we think that the risk is asymmetric. Even with the ongoing support of the European Central Bank (ECB) there are many scenarios out there that could throw the market; we have seen a number of such incidents over the past year. Moreover, the volatility attached to these events may be much higher now than it has been in the past. I think conditions will get more challenging from here, not less. Therefore, from a high level perspective, investors need to understand that from here the upside to investing is much harder to achieve than the downside.

The yield environment has spurred some interest in other types of investment products: separately managed accounts being one example. Interest in these products is not driven purely by the desire to offset negative yield though; for many, capital preservation is still the core of that strategy. Overall, corporates are realising they need to become far better and more targeted at segmenting their cash and finding ways to make it work that little bit harder. Unfortunately, the reality of the environment we are in today is that even if you are doing that, in euros you will probably still end up with a negative yield. It is a really difficult hurdle to get over.

### **Trading liquidity has been on a downward trajectory in recent years. What impact is this having on the short-term investment environment for corporates?**

The issue of liquidity is absolutely front and centre, in every sense. In recent years it has been draining away from the banks and, as asset managers, we are going to have to hunt it in new places. I think BlackRock is perfectly positioned to leverage our counterparty base and access that balance sheet which we absolutely need in order to invest in these short-term markets. On the credit side, the changing regulation regimes in each country means investors are going to have to really understand where they rank in terms of seniority: deposits and certificates of deposit (CDs) may in

some countries be higher than unsecured commercial paper (CP). Treasurers absolutely need to understand the intricacies around that hierarchy.

“Be very wary of stretching for yield because we think that the risk is asymmetric.”

In the current negative yield environment, the lack of liquidity is becoming especially pronounced. When the money fund peer group went negative earlier this year – we were one of the bigger providers to go negative at the beginning of April – it was interesting because not all securities were trading with the same liquidity. Government securities traded on both bid and offer. In the credit market, in CP and CDs, the bid-offer spread started to widen whilst MMFs teetered at the zero yield level. Credit was offered at negative, but not bid at negative. It was an interesting dynamic and it took the gross yield on the peer group going negative for it to change. The bid-offer spread in credit is still wider than on the sovereign side in money markets.

For a MMF, it means that you have got to be thinking about raising the quality of your portfolio in order to maintain liquidity without increasing your cost of trading. A negative rate environment by virtue of being inherently less liquid will tend to switch you from thinking in an active portfolio sense, to a more buy and hold stance and it is important for investors to understand this dynamic.

### **The regulatory environment is changing in the European MMF space. How do you see the reforms agreed earlier this year by the European Commission impacting the corporate investor? Will so-called low volatility (LVNAV) funds serve as a viable option for the corporate investor who is used to using stable NAV funds?**

On the face of it, we think the proposed LVNAV will be more palatable for our corporate clients, it being much closer to the constant NAV (CNAV) funds many of them use today. Conceptually, it could deliver some of the key CNAV features that investors cherish such as same day liquidity, intraday liquidity and a stable net asset value. We remain somewhat sceptical, however, with respect to the detail of the regulation. How that is mapped out over the coming months will be crucial. At the moment, the proposal has a sunset clause in it, which we do not see as being particularly helpful. The technical and the operational build around creating a product that has the ability to switch to VNAV on a day's notice is actually really complicated. It is expensive to create.

But if the sunset clause is not there, then where the trigger threshold is set will be the main determinant for the success of LVNAV. If that ends up at a reasonable place – and the industry is comfortable with Parliament's proposed 20bps threshold – then this could be a really workable solution, one which will deliver some of the key features that our corporate investors like. Realistically, from an investment side, the tightness of the trigger threshold will obviously de-risk the proposition, because from a fund manager's perspective there is no incentive to want to be hitting those thresholds, at any point, and the best way to avoid doing so is to de-risk the

fund. That is effectively what will happen if the regulators impose a trigger materially south of 20bps.

There is still a long way to go on this debate, though. The European Parliament passed the framework for MMF regulation in April and now the next step is for the Council of Ministers to provide opinion and text. The Council is by no means bound by the Parliament's text – the member states retain divergent views on some key issues. The Council's review is unlikely to be completed through 2015 while the Presidency sits with Luxembourg, a strong MMF centre that may not be deemed wholly independent by the broader EU community. The Council Presidency will pass to the Netherlands in January 2016 and we anticipate the MMF regulatory debate to gather pace around that time. Only upon the Council completing their review can the Trilogue process begin, through which the Commission, Parliament and Council will agree on the final text. Throughout the next steps in the process much of the technical detail behind the framework will be resolved and an implementation timeframe agreed. As such it could be that we are at least two years away from anything happening.

### How do you see investment market developing for the corporate treasurer in the coming months and years?

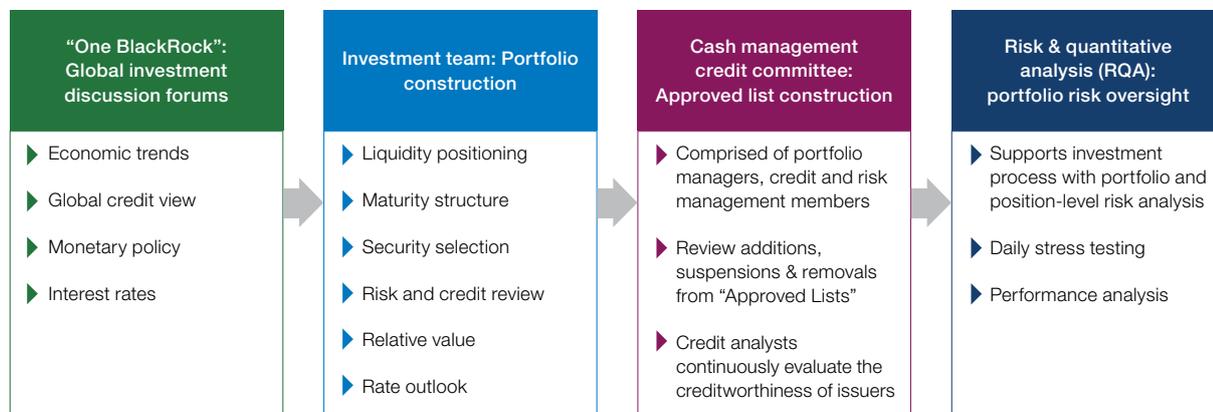
One trend that we are already seeing a lot of in the post-Basel III environment is an increase in structured paper being offered.

We are seeing more structured repo; more term repo; and we are seeing a lot more structured CP being offered. That's existed in the past, of course, but there is more of it being issued.

Banks are looking for new and innovative ways of financing trade receivables for their high quality corporates too, which is also a form of structured product financing. But the thing with all of these structures is that they inherently have no liquidity attached to them. That means they can be a part of the solution, but they may not be an entire solution.

Corporates have been talking more about the different products they can access and, certainly with the larger corporates, looking closely at things like repo. We think that can work for some of our client base, but again, it all comes down to the ability to access liquidity. Corporates need to have a large amount of counterparties set-up, and need to take a flexible approach to the collateral that is accepted. They also need to be more flexible with respect to duration, operating in that favourable space for the banks that tends to be over the 90-day mark. Ultimately, the market is moving towards more of a 'buy and hold' stance. That means the credit piece is becoming an even more crucial part of the corporate investors' strategy. Corporates will need to allocate more resources towards credit and those who do not have them should think about outsourcing to an investment manager with extensive resources and a highly disciplined process involving credit, risk and portfolio management (see Chart 1). ■

Chart 1: Liquidity investment process



Source: BlackRock

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# Mapping the new liquidity landscape

*Across the globe, the cash and liquidity landscape is changing. Once the dust settles from the extensive regulatory and market changes currently being witnessed, what will the new short-term investment world look like for the corporate treasurer?*

Auna Dunlevy has been pondering the investment climate a lot of late. In just the past several years, the Head of Front Office at Royal Mail has witnessed euro rates dive into negative territory, banks becoming more selective around deposits, and regulatory upheaval within asset management that looks increasingly likely to eliminate one of her department's preferred short-term investment vehicles, the euro CNAV money market fund (MMF).

Such has been the epochal scale of change in the European cash management landscape that treasurers like Dunlevy have had little choice but to almost go completely back to the drawing board (and many, indeed, to the corporate board) with respect to investment strategies. "Where possible we've

tried to remove the 'security blanket' of overnight cash," she explained to delegates at the Association of Treasurers Annual Conference 2015 in Manchester earlier this year. For what Dunlevy and her colleagues define as 'primary liquidity' the traditional investment prerogatives – security, then liquidity, then yield – remain the order of the day. Notwithstanding, treasury has worked hard to negotiate lower fees or higher rates on overnight deposits, leveraging where necessary relationships that banks have with the company's pension department. But for secondary liquidity, yield is sought over liquidity in some cases.

"In order to maximise the duration of funds falling into this category, we make the decision as early in our cash flow cycle

as possible,” she says. “We need to evaluate what the banks offer, check that it fits with our policy and make sure we understand the products. I’m not talking about anything fancy here – it is usually notice accounts or extendables but the fact is that every product is slightly different and they do change from bank to bank.”

Similar strategy discussions will have been taking place in corporate treasury departments across the globe, and especially within those that operate within the Eurozone. It is not just that the investment environment has become a much more challenging one in recent years, it is also that corporates, on aggregate, have much more to invest now than ever before. Companies have become increasingly accustomed to ultra-low borrowing costs (the other side of the low rate coin) and as they tapped the bond markets for record amounts the cash on balance sheets has swelled. Take as evidence the annual S&P Global Corporate Capex Survey, which tracks the top 2,000 global companies that spend the most on capital expenditure. The survey revealed, when it was published in August 2015, that companies are now holding some \$4.4trn of cash and equivalents on the balance sheet.

## But those prophesying the imminent demise of bank deposits as a corporate investment vehicle might be jumping the gun a little.

“Liquidity management is certainly a bigger activity for the typical corporate treasurer,” says Nick Burge, Managing Director, Head of Strategic Liquidity at Lloyds Bank. “Some of them are making the migration from managing a bit of cash on the side to an operation equivalent to a medium-sized asset business. So that will mean looking across a much broader range of products, different risk matrices, different maturity profiles; it’s all becoming about trying to get some return while still meeting that liquidity requirement.”

### Heading East

It is not just corporates in western markets that are facing investment challenges though. With the notable exception of Japan, treasurers in Asia Pacific have largely been spared the same ultra-low rates investment predicament facing their peers in the US and Europe. Nevertheless, central banks across the region now appear to be in a race to cut rates quickly in order to starve off the economic malaise now beginning to take hold in the region.

Since the beginning of 2015 a number of Asia Pacific’s major economies – China, India, South Korea, Australia, and Thailand – have reduced short-term policy rates to varying degrees. “In the emerging markets, we do see in our footprint a slight decline away from those double-digit interest rates there have been in the past to, depending on the market, between 7 – 10%,” Vanessa Manning, Head of Product Management, Transaction Banking, Europe, Standard Chartered told Treasury Today.

With corporates in the Asia Pacific sitting on more idle cash – an average of \$4.2bn each according to S&P – this is news that treasurers in the region probably do not want to hear. Although the risk to preservation of principal for the time being

(especially against the current deflationary backdrop) is arguably minimal, a new corporate investment dynamic is beginning to emerge all the same. “That is why, across the regulated markets especially, we are seeing a growing range of interest optimisation solutions for short term operating cash balances where you have a range of EM currencies building up and difficulty in repatriation – your bank will provide a notional aggregation of those, providing both a local arms length return with additional incentive on top of the worth of those currencies and offer you interest based on those,” says Manning.

This is all a part of the treasury efficiency story for multinationals operating in emerging markets and it is, in some respects, a necessary step for corporates that wish to improve their returns while continuing to comply with their own governance and compliance policies. By working with a single bank across a region like Africa or ASEAN and using such interest optimising solutions, corporates can secure a safe enhanced return on operating cash, without needing to move into potentially riskier and less liquid structured products.

The changing rate environment in Asia is also giving a lift to a number of nascent MMF markets across the region. “Malaysia, and Indonesia especially, have rapidly growing MMF sectors,” Manning adds. “We are seeing more and more funds setting up in Indonesia and taking advantage of both the surplus of investment going into that market and the requirement for funds as an alternative investment product.”

### Demise of deposits?

The imperative to consider other types of investment product is not just being driven by the yield environment, however; several other factors are also at play here. First is the deterioration in the credit quality of many banking institutions witnessed post-crisis. Many investment-grade corporates are surveying the banking landscape and noting that a significant number of their banking counterparties are now deemed less creditworthy than they themselves are by the ratings agencies. And outlooks are tending more towards the negative than the stable.

“I’m moving away from investing in traditional bank deposits because with the reduced liquidity and the risk that a credit rating agency may change a view on a rating of a bank,” Asim Iqbal, Head of Treasury at British motoring association, the AA, said at the ACT Annual Conference 2015. “That would be putting me at risk of breaching my own treasury policy.”

Even in instances where the treasurer decides that the safest place for their cash is with one or more of their banks, they may find certain types of deposits are no longer welcomed. The beginning of 2015 marked the introduction of the Liquidity Coverage Ratio (LCR) under Basel III, designed to ensure that banks have sufficient assets on hand to withstand any liquidity crunch the market might throw at them. Prudent though that requirement may be, given everything that unfolded back in 2008, there is little doubt that it will impact the value of cash. Operational deposits are continuing to be sought after, but taking non-operational deposits, which have been assigned a higher run-off rate due to their perception as being less stable, is becoming far less attractive for banks under the new rules.

But those prophesying the imminent demise of bank deposits as a corporate investment vehicle might be jumping the gun a little. In fact, if a shift is indeed under way it appears, in the US at least, to be going in the opposite direction. To understand why,

one would be advised to take a look at the 2015 Association of Financial Professionals (AFP) Liquidity Survey, which looked at what American corporates are doing with all that unused firepower accumulating on their balance sheets. The report notes that, in 2008, treasurers were keeping approximately half of their short-term liquidity in the capital markets, by way of MMFs, treasury bills and other such instruments. Around one-fifth, meanwhile was being stored in traditional bank deposits. Now we are seeing the reverse. Today, MMFs are storing a mere 15% of short-term cash, while 56% of is being placed into bank deposits.

That may well be a reflection of the fact that treasurers are now finally beginning to feel more confident about the health of US banks (in contrast to the picture in Europe) and that, in the current yield environment it is becoming extremely difficult to get any return on capital markets instruments. It may also be a manifestation of the growing concerns that treasurers have around the changing regulatory environment around the capital markets and, the reforms that the Securities and Exchange Commission (SEC) have introduced in the MMF space in particular. Either way, it would seem that a majority of corporates, having explored a variety of investment solutions, simply cannot find any better alternatives.

Recent talk around tri-party repos is a case in point. Superficially, at least, they look like a great alternative to bank deposits in the current environment. At a time when banks are not as safe as they once seemed, tri-party repos offer security. In markets where interest rates are flat or have minus signs next to them, tri-party repos are claimed to offer the rare prospect of some return. Indeed, tri-party repos would seem so advantageous for corporate investors in this current investment environment, greater direct participation from treasurers in this market would seem like a natural development.

Yet while some corporate treasurers have indeed begun experimenting with the tri-party repo, enthusiasm for the product within the profession has not quite been universal. "I have looked at repos but I have decided at the moment the time and cost in setting up a repo is quite significant," says The AA's Iqbal. "And from conversations I've had with other treasurers, I understand that the returns being offered by a repo might not be any more than that of a MMF deposit. So the question of tri-party repos is still out there for me."

## Bracing for VNAV

Although some treasurers like Iqbal might currently see no yield incentive to choose a tri-party repo over a MMF investment, there may soon, like in the US, be a regulatory one (at least for those who staunchly favour prime CNAV euro MMFs as a home for their short-term liquidity).

Earlier this year, the European Commission (EC) announced new regulations for the industry, which, once formally approved over the course of the next year will reshape the investment environment for corporates in Europe quite radically. Rather than impose a mandatory VNAV for prime institutional CNAV MMFs without delay, as the US has opted to do, the EC has agreed (still subject to approval from the Council of Ministers) to allow for a so-called Low Volatility (LVNAV) money fund product to operate for a five year interim period.

Treasurers with a view to the long term have, however, have grasped the fact that – LVNAV or otherwise – prime CNAV MMFs now have a death sentence hanging over them and are

beginning to consider how their investment strategies might have to adapt in the coming years as a result. Unlike in the US, the persistently poor health of the European banking sector would appear to rule out a return, en-masse, to traditional deposits. Some treasurers, like the Royal Mail's Delaney, believe there is little sense in delaying the inevitable.

"Perhaps the thing we spent longest thinking about is CNAV MMFs," she says. Unlike some of its corporate peers, Royal Mail's board policy already covered VNAV funds. But treasury, being very comfortable with the CNAV funds they had used since the early 2000s, had always shied away from VNAV products. As the policy direction at the European-level became apparent, however, the department decided it was time to revisit the products.

Many treasurers will feel obliged, in this new world, to experiment with new investment products and services, different durations and new cash segmentation strategies. But the prudent thing for treasurers to do would be to take their time.

The way they approached this task should serve as a useful best practice guide for other treasurers, many of whom are likely to have similar decisions to make in the coming years. "We looked at the volatility of VNAV and also the underlying volatility of CNAV funds," she explains. "We considered the duration of which we could invest our funds. Then we considered some historical examples and, of course, checked out the accounting and spoke to some other corporates before we made the decision to invest."

Many treasurers who, like Delaney, have gone through this process, have been pleasantly surprised by the muted volatility and general stability of the funds (Aviva Investors, which converted its daily sterling liquidity fund to VNAV seven years ago told Treasury Today in May 2015 that since its inception the valuation has never moved away from one). But a careful approach is nevertheless advisable, as it would be for any new instruments, and at Royal Mail investment limits are, for the time, at a lower level than for a corresponding CNAV fund.

## Tomorrow's world

Once the dust finally settles from regulatory and market adjustments of recent years the corporate treasurer is likely to see an investment world that has changed considerably, in some jurisdictions, perhaps beyond all recognition.

Caution, though, should be the name of the game for corporate treasurers right now. Many treasurers will feel obliged, in this new world, to experiment with new investment products and services, different durations and new cash segmentation strategies, as the insights offered by Delaney and Iqbal testify. But the prudent thing for treasurers to do would be to take their time. Only once each new product and strategy has been carefully considered and they have worked out what is the suitable to them, will the time be right to gradually implement the changes which need to be made. ■



## THE BANK INTERVIEW

### Erik Zingmark

Deputy Head of Transaction Products



*He might not have a crystal ball, but Erik Zingmark, Deputy Head of Transaction Products, Nordea is extremely well placed to discuss both current and future trends impacting the treasury profession. In this interview, Zingmark outlines the new strategic imperatives for treasurers, reveals key insights from Nordea's Treasury 2017 report and addresses the opportunities treasuries have in becoming strategic drivers in digitisation.*

#### **We're now several years on from the global financial crisis. In what ways are treasurers still being impacted?**

As we all know, the global financial crisis of 2008 resulted in an increased focus on cash management, balance sheet monitoring and liquidity. The role of corporate treasury therefore grew to be even more significant in this respect, with senior executives taking a very keen interest in cash positions, buffers and exposures, and expecting frequent updates. Today, cash is certainly still king.

Since the crisis, a wave of new financial regulation has also been introduced, impacting the treasury function both directly and indirectly. Aside from gaining responsibility for specific regulatory-driven projects, treasury has also become even more influential in the compliance sphere. The treasurer now has increased responsibility for all risks – ranging from market risk to sovereign risk, with counterparty risk at the heart of everything. Indeed, the desire to spread risk among reliable counterparties is certainly something we are still seeing today.

At the height of the financial crisis, it became obvious to corporates that not all banking partners had the same creditworthiness. The strategy of having as few banks as possible turned out to be too risky – and this led directly to a change in strategy, whereby the treasury now plays a key role in choosing the right banking partners, in finding alternative sources of funding and in improving the use of excess cash. What many corporates found, once this new strategy was in place, was they could actually create a more efficient cash management and banking set-up by engaging with strong regional banks, instead of implementing a set-up with one global bank. Finally, I would say that treasury departments are coming under increasing pressure to put more efficient systems in place in order to cope with growing complexity and transaction intensity in the post-crisis environment.

#### **How can treasurers look to embrace the crisis-driven change that is still happening?**

Change presents an opportunity and the steady elevation and expansion of the treasury team's role within the organisation

paves the way for treasury to become an even more important partner with, and strategic advisor to, business units. This means supporting globalisation, promoting efficiency, improving integration with trading partners and the supply chain, as well as greater sophistication in risk/return optimisation.

As I alluded to earlier, treasury also has the opportunity to become the source that senior executives and key stakeholders throughout the organisation turn to for instant reports on liquidity and risk positions and to assess the financial impact of major events whether economic, political or environmental. This should allow the treasurer to gain an even greater trust and respect from the C-suite, whilst raising the profile and value of the treasury function internally.

### **What new solutions or techniques are being devised to help treasurers achieve their cash and liquidity aims?**

It is an old truth that the key to efficient liquidity management is greater control of intra-company cash balances through centralised cash flow management. What we see now is that new technology is making it possible for treasurers to continue to optimise the use of group liquidity by taking a wider responsibility for the subsidiaries' working capital processes. Furthermore, new ways of distributing technology – such as cloud delivery – are making it easier for a treasury function to start using, or upgrade to, tools that are more sophisticated.

Another established way of improving efficiency is through the centralisation of payables management. What SEPA has done is to enable treasurers to take this to the next level, by centralising receivables management as well. The rationale for this is clear: by building a collections factory and applying the receivables on-behalf-of model, the organisation can benefit from economies of scale, better credit and risk management, rationalisation of bank accounts, faster use of incoming payments, and reconciliation cost savings.

In terms of pooling, which is of course a traditional cash and liquidity tool, I would say the attractiveness of notional pooling is likely to decline since Basel III imposes stricter requirements on offsetting balances, but instant access to group liquidity can be made possible through physical real-time cash concentration across borders. This technique, provided by only a handful of banks today, is probably the most efficient means to minimise cash traps and idle cash, as well as to enable better visibility and control over liquidity.

### **What else can cash management banks do to help treasurers in this respect?**

Today's treasurers require more data and more analysis around cash and liquidity than ever before. They need this to monitor and feed business demand in a timely manner. With that in mind, banks must be in a position to deliver what their customers require. This means providing presentational tools, such as dashboards, to help treasurers consume and interpret this data – and also in a mobile environment.

Whilst this is an obvious area for investment by banks going forward, some banks have struggled thus far to aggregate and coordinate data supply since many of them are using aged core systems that cannot cope. And although certain banks are managing with old technology at the moment, there will come a time that these legacy systems will have to be changed in order to enable banks and customers to embrace the

benefits of new technology and move forward to the next stage of development. It may be a painful experience for many banks to make such a big change, but it will absolutely be necessary.

### **Is centralisation still the best way to solve cash and liquidity visibility challenges? How is innovation enabling more treasury departments to achieve a greater degree of centralisation?**

In most cases, full optimisation in the use of group liquidity requires the centralisation of payables and receivables. But even though centralisation is a key enabler for efficient liquidity management, it has often been difficult for treasury functions to obtain, largely due to a lack of standardisation among banks and the need to invest in expensive technology.

Again, the introduction of SEPA has changed the rules here, making it possible to master euro payments and collections to and from counterparties in many countries through accounts (and in some instances a single account) held in one country. Whilst this may have seemed like a daunting step when SEPA was relatively new, the success stories from the first movers are now rapidly spreading across the corporate community. This is creating an incentive for more companies to establish payment and collection factories and to implement payables and receivables on-behalf-of structures.

Cloud technology and Software-as-a-Service (SaaS) models are also playing a role in the drive towards centralisation. For example, they are making it less expensive for treasuries and shared service centres (SSCs) to employ technology solutions that are more sophisticated – and up-to-date. In turn, cherry-picking the relevant modules from the right technology vendors and outsourcing the hosting of data, as well as the support to the business units, will enable smaller treasuries to reach the next level of centralisation.

### **Looking ahead, what do you see as the key themes for treasurers to concentrate on over the next 12-24 months?**

In Q4 2014, we conducted the Nordea Treasury 2017 report with the precise aim of taking the pulse of the industry. We surveyed 82 large corporate treasuries and interviewed more than 60 CFOs and treasurers, building a clear picture of where the treasury stands today, and how treasurers see their role evolving in the future.

The key findings reinforce much of what we've spoken about already, such as banking relationships being absolutely key, and the fact many treasurers are finding that a smaller number of core banks gives greater oversight of liquidity and exposure, without the counterparty risk of a single global bank model. Elsewhere, the survey found visibility and control over cash and liquidity remain significant priorities, with access to funding and optimising existing funding arrangements also high on the agenda. In addition, centralisation is widely recognised as 'the future': giving treasurers a better overview of their cash and liquidity positions, whilst also helping to deliver the efficiencies needed as treasuries take on an expanding workload and become strategic advisors to the business.

Perhaps the biggest change the survey results highlighted was the decline in trading activity undertaken by the treasury department over the last decade. Only a third of treasuries still have a trading mandate and, for them, the objective is usually to sustain market knowledge rather than to generate a profit.

Whilst trading may be declining, hedging is on the up. The survey results revealed large corporates are now hedging more risks than they were two to three years ago, and most expect they will be hedging even more by 2017. In particular, corporates are hedging to protect themselves against fluctuations in FX and interest rates, typically using futures. In summary, the Treasury 2017 report underlines that treasury has moved into a strategic role, but that is not to say the transactional element of the treasury's role is going away – this remains just as important as ever.

### **Looking at the transactional space for a moment then, how is innovation in the world of payments set to impact corporate treasurers and their payment providers?**

In its current form, 'the payment' is a standalone product for the transfer of funds to settle a transaction. And over the last decade, it has gradually turned into a low-priced commodity of little strategic interest. Due to the impact of new technology and regulatory changes, however, we can foresee a huge transformation in the role of a payment. In the future, the humble payment will become a value-adding solution that is integrated into broader commercial transactions. A key factor that will affect all stakeholders is the advent of the Payment Service Directive 2 (PSD2) as it will allow new non-bank players to enter the space. Of course, this could be seen as a threat by the banks, but the smart operators will use it as an opportunity; they can set themselves up (perhaps via subsidiary) as a non-bank and offer the same services to customers. So, this change should not be seen by banks as a threat but as a way of liberating them from some of the regulatory constraints they were subject to before.

And since banks already have the infrastructure, the compliance teams, and the knowledge of the industry, they are in a perfect place to better serve payments customers. Conversely, some of the new entrants will find that, as they expand, they encounter all the same regulations that banks now do – and they will struggle without the right resources and expertise. So, for smart banks, this could be the start of a new life. The PSD2 will focus the attention of the banks and they will have to build an appropriate response or, ultimately, face a bleak future.

### **Another trend we are hearing a great deal about is digitisation. Why do treasurers need to be thinking about this?**

Digitisation is very much a hot topic. We foresee many innovative digital offerings entering the market with the potential to support the treasury function more efficiently than traditional bank services. For example, just as FX services have been made available in an auction format through portals that enable corporates to pick and choose who they want to deal with for a given transaction, in the future it may be possible for many other banking services to be consumed in this way, making the marketplace far more competitive.

Naturally, the banks will not sit idly by and watch while new entrants eat their proverbial lunch though, so we can expect greater innovation coming from the banks too. As discussed, the traditional payment offering will be redefined – it will also be further integrated with more comprehensive product propositions covering the customer's process end-to-end. Treasurers should also expect to see banks making use of new technology to create multi-channel functionality based on real-time exchange of transactions and balances.

For the treasurer, the key messages around digitisation are to stay up-to-date and to be ready to exploit the new offerings. In a world of fast-shifting technology and rapid adoption of new digital solutions, it is important to be part of the flow. Simply waiting and seeing how it turns out is not likely to be a winning strategy, since you need to be in sync with your counterparties to stay efficient.

### **Finally, how is Nordea embracing digital opportunities?**

In order to become very easy to deal with, whilst remaining relevant and reliable, Nordea is one of few banks in the world so far to embark on a simplification journey whereby the complete core banking and payment platforms are being replaced. This will enable Nordea to become highly efficient and agile, and at the same time to further embrace the digital opportunities ahead.

Nordea is also utilising new technologies to create innovative services and to establish omnichannel solutions which are more efficient in reaching and supporting our customers. We are increasing our spending on innovation and people working in a lab environment. We were one of the first banks to provide banking content for the Apple Watch and have many other interesting solutions cooking. The golden rule, and our ultimate goal, is to be available whenever, from wherever, and through whichever channel our customer chooses.

Beyond our own horizons, we believe digitisation is a key enabler for transforming the whole banking industry. Going forward, we will see traditional bank propriety solutions being replaced by more comprehensive offerings, whereby any given financial service will be closely integrated into broader commercial product propositions. XML will be the bedrock of much progress in this space, as long as it remains standardised, and Common Global Implementation will play a big role in keeping it as a true standard. And then we have blockchain technology which could transform banking fundamentally.

To be part of this digital evolution, banks will have to utilise the best of new technology and be willing to partner with other players when building and delivering new services. Another major component of this ongoing development is engagement with the customers; to ensure what the banks are working towards really taps in to their long-term ambitions. Digitisation is a primary strategic initiative and growing need on the customer side and banks must respond by facilitating discussions with their customers around the innovative use of digitisation. The payment execution is a central part of the commercial process but digitisation stretches far beyond that. Collaboration, for instance, could focus on potential cost reductions, efficiency enhancement, risk, reallocation of treasury staff from back office to more high-value front execution or even positioning treasury as a strategic business partner in the internal digital ambition.

We are increasingly assuming this role as a knowledge centre and strategic advisor where we facilitate the sharing of best practices, digital strategies and smarter ways of working between and together with our customers. This helps prepare treasurers for the next opportunities that digitisation will bring and arms them with relevant knowledge and viewpoints to carry into the C-suite. It is a new step in the customer-bank relationship and I would certainly encourage treasurers to proactively engage with their banking partners around digitisation and help shape the future of financial services and, indeed, drive the innovation agenda within their own organisations. ■



# A tangled web

*Defined by the UK Serious Fraud Office as intentional deception to obtain an advantage, avoid an obligation or cause loss to another person or company, fraud is an ongoing issue for the business community. Treasury Today considers the threat from the treasurer's perspective and asks what role the profession has in defending corporate cash and reputation.*

In a globalised and competitive world where complexity of systems and processes meet a workforce subjected to increasing personal financial pressures, and where blasé attitudes to security assist unchecked greed, the conditions are right for fraudsters to try their luck. Fraud is of course nothing new, but despite awareness of its prevalence, and the adoption of sophisticated anti-fraud technologies by some business, it remains a major commercial issue.

Despite this, the ACT/Kyriba annual report shows that fraud prevention remains surprisingly low on the priority list with only 11% viewing it as one of their three top concerns for 2015. Martin Taylor, Vice President of Northern European Sales at Kyriba says it is certainly “a concern” that fraud does not feature highly on most treasurers’ radars, particularly given the number of high-profile cases that have come to light on both sides of the Atlantic in the past couple of years. “At the moment, there does not seem to be too much ownership of the problem.” It is, he believes, not solely an ‘IT problem’ or a ‘risk problem’; it is a matter in which all must be involved.

After all, the reputation of a business that is in some way embroiled in major fraudulent activity is starting to have an interesting and potentially serious side effect, notably in the Asia Pacific region. Ethical business practices are directly related to attracting and retaining talent in the region, with almost 80% of respondents polled in Ernst & Young’s (EY) recent APAC Fraud Survey 2015 saying they would be unwilling to work for companies involved in bribery and corruption. As EY concludes, “fraud prevention is no longer just a legal and compliance issue but impacts recruitment, talent retention and business continuity.”

## Red flag act

So how do you spot a potential fraud, or stop fraud before it even starts? Well, most perpetrators of corporate fraud do not aim for the big numbers straight away simply because the chances of being caught syphoning millions in one hit are very high. The intelligent fraudster makes multiple micro-transactions, often sent on a circuitous route, ensuring far greater difficulty in

tracing their movement. The UK Serious Fraud Office notes a number of indicators or 'red flags' that may suggest an individual is engaged in fraud. Its watch-list is not exhaustive but combinations of the following may indicate trouble:

- Significant changes in behaviour.
- An individual is known to have large personal debts or financial losses.
- Transactions taking place at odd times, odd frequencies, or involving unusual amounts or to odd recipients.
- Discrepancies in accounting records and unexplained items on reconciliations.
- Missing documents or only photocopied documents available.
- One employee has control of a process from start to finish with no segregation of duties.

It almost goes without saying that any approach must be handled with extreme sensitivity.

## Human weakness

Within any organisation humans are most likely the weakest link, says Kyriba's Taylor. "If an employee is given unilateral control over financial movements without safeguards then the possibility for fraud exists." As part of a pre-employment checklist, he suggests a degree of due diligence, checking relevant credentials for example. Although most recruitment specialists should do this anyway, a discreet background search may prove worthwhile. As employment progresses it becomes a line management and HR duty to keep up with personnel matters; this may reveal at an early stage problems that could, if left, resolve in fraud.

As treasurers are at the helm of the company's finances, they are often the last in the chain when approving payments or executing trades, Taylor notes. "If the company is still depending on individual banking portals and spreadsheets then the potential to defraud is much higher than for a treasurer with highly secure workflows."

For Steve Baseby, the UK ACT's Associate Policy & Technical Director, the fact that treasurers tend to deal with the wholesale end of the money spectrum sets them apart from more obvious areas of potential fraud (simply because of the process, not the people) such as accounting, accounts payable or purchasing. Treasurers do have access to payments systems where they move quite large sums of money, but even here the classic bank internet system for the corporate treasurer has a three-tier transaction process, he explains. When one of these systems is implemented the first thing internal audit will do is certify its integrity so that once in operation, having got to the stage where the business is creating a payment instruction, it is certain that, depending on value, at least 'four eyes' approval is given. "And ideally none of these people will have anything to do with the original commercial transaction."

## IT meets IQ

In addition to multi-factor authentication, companies can put in place more general safeguards such as Virtual Private Networks and IP Filtering. Many of these tools are commonly and conveniently deployed as part of a TMS or ERP.

Furthermore, IT can also integrate treasury system user rights with internal systems using Lightweight Directory Access Protocol (LDAP) Authentication, effectively creating a secure single sign on for multiple services. "Even just implementing these controls increases security dramatically, without having to resort to further IT investments," says Taylor. "As long as people follow the process and don't make exceptions 'just because it seems to be the CEO emailing me', then the defences will remain enforced."

In any approach to fraud detection and prevention, whilst most environments can be considered for risk-free operation, there will always be a cost associated with the number of people or systems engaged in checking every transaction. "If you increase the oversight you lower the risk, but businesses have to take decisions about how much cost they can justify to lower those risks," says Baseby. "There is a persistent level of fraud because business in general chooses not to overload the internal controls because they know that costs can get out of hand." There is, he notes, a "bearable level of control" and within that limit, internal auditors will use various statistical sampling methods to check the level of confidence that there is not fraud within a system, but fraud is still possible.

Why is this acceptable? As an example, a normal commercial relationship that involves a continuous flow of trade will, in the eyes of the auditors, have a standard deviation probability measure of the way the business runs its procedures. This methodology may give 98% certainty that things are happening as they should. Within this boundary Baseby says it is generally accepted that the cost of pushing that last 2%, and thus fully eradicating fraud, would be "ludicrous." Even if the costs were acceptable, the reality of business would most likely see the company grind to a halt under such a regime anyway; hence there has to be a practical limit of control beyond which it becomes unfeasible. Herein lies the need for clear, well-documented and promoted policy as a means of providing the foundations and guidance for all.

## A matter of policy

Most corporates will have a two-stage policy process, Baseby notes. A summary policy will be agreed at Board level, covering the general principles and strategies (including IT) around matters such as managing payments, dealing processes, counterparty exposures (including bank exposures) and will set risk appetite, boundaries and limits for practical application above which additional checks will be required.

The second stage of policy takes the form of the more detailed procedures manual, which describes actual processes. This should be the constantly evolving part. As this document is amended, so the conversation must continue with internal auditors to keep every process up to date. This, Baseby explains, avoids the common error of thinking that "just because a system worked once it will always work." Although policy must not be too restrictive and prescriptive, the adoption of procedure must be across the board, with no exceptions because, as Taylor mentions above, as soon as its influence is disregarded the risk of fraud rises significantly.

Policy around fraud should address control measures which will seek to either prevent or detect at various levels. Organisational controls may include assurance that senior management has oversight, that staff background checks have been carried out and that there is segregation of duties

where necessary. Physical controls such as workplace security roll into system controls that cover areas such as access and authorisation rights and identification. Controls around process will consider a wide spread of areas such as management of mandates for bank and dealing activity, the control of financial product acceptability, payment approval processes, strong reporting and the insistence on at least an annual independent audit. Accenture's 'Treasury operations and controls' advisory document urges treasurers to make sure policy is relevant, clear, well understood, aligned to the corporate objectives and, most importantly, has full buy-in of all stakeholders.

Ultimately it is the responsibility of all employees to safeguard and be vigilant to the threat of fraud – but are strong policy guidelines enough? The EY Fraud survey referred to above suggests that policies are failing to improve attitudes to fraud. Some 52% of EY's respondents believe anti-bribery and corruption policies are 'irrelevant and ineffective'. In addition, 41% said a code of conduct has little impact on how people actually behave. Although 55% of APAC companies have whistleblowing hotlines in place, the number of respondents prepared to use them has dropped since the last survey (81% in 2013 but 53% in 2015). "The drop in whistleblower hotline usage appears to be due to respondents being increasingly concerned about insufficient legal protection or the lack of confidentiality leading to a risk of retaliation," says Reuben Khoo, EY Partner and ASEAN Leader for Fraud Investigation & Dispute Services. "It is clear that APAC policies, codes of conduct and whistleblowing hotlines are not enough. Companies need to demonstrate and communicate about ethical behaviour if they want to affect true change."

## A forensic approach

When something is amiss and internal audit and investigation cannot find an answer, an external forensic accounting expert may be required. Forensic accounting is all about piecing together information contained in financial records and other documents, to create, or recreate, as accurate a picture as possible of an event or transaction that has happened, explains Richard Abbey, Head of Global Forensic Accounting firm, Stroz Friedberg.

The unwinding of that event or transaction is like "reverse engineering" each step to be able to tell when a payment was made, where it went, how it was described in the system and what it was that triggered it, such as an invoice or payment instruction, and who authorised it, which cost centre did it go to and so on until the truth is revealed. But other than the knowledge that something is not right, Abbey notes that there are few immediate warning signs with which a forensic investigation can commence; it can require a long and patient trawl by skilled practitioners through the relevant data.

However, genuinely beneficial technology is at hand in the form of 'transaction monitoring' which can help uncover anomalies. Stroz Friedberg has developed its own analytical engine that uses complex algorithms to unearth irregular transaction patterns. The output, also known as red flags, will be further investigated by the team, tracing them back through the chain, both internally and externally.

Abbey is convinced that it is becoming less effective for businesses to rely fully on internal networks and control mechanisms such as segregation of duties to protect assets. He argues that organisations will need to run regular

monitoring and analytics on all their transactions to be sure they have not been compromised. The issue is not now just one of fraud prevention and detection, but also one of regulatory compliance, as rulings around AML, bribery and corruption and fraud hit the statute books.

Curiously, although he comments that many organisations still think fraud is something that only happens to other companies and thus they prefer not to spend time and resources in trying to prevent it, he believes that the current raft of regulations is having more impact in this respect. Abbey comments that businesses have spent a lot of money in the past few years taking advice on internal control frameworks to ensure regulatory compliance. For him, the next challenge is going to be in proving that these controls are working and being adhered to. "The most obvious way to do that is to carry out regular transaction monitoring, and if you're not doing that then query whether you really have implemented adequate controls." Whilst he concedes that real-time monitoring of every transaction is maybe too much of a regulatory ask, he feels it is "inevitable" that the regulators will eventually expect some kind of "regular retrospective design to control and capture infringements."

## Detection and prevention

Claiming a first for transaction monitoring in the procure-to-pay environment is David Griffiths, CEO of UK-based FISCAL Technologies, vendor of the APForensics suite. He says his firm's cloud-based or installed system sits alongside a corporate accounting system, monitoring invoice payments and consuming master data relating to suppliers and employees to build a picture of payments activities of all values as they unfold in real-time. Working in the fraud and compliance context, it uses proprietary algorithms to perform real-time controls monitoring by continuously recalculating and outputting any anomalies or 'red flags' for further investigation. These warnings may, for example, be based on the size of the payment, the date of payment, the frequency or a combination of such issues. If a red flag is created it may warrant further investigation by internal audit or an external forensics unit.

Due to the sheer volume of data being processed, internal audit capacity for this kind of investigation is typically restricted to ad hoc investigations. "They may do this once a year; what we do is carry out those tests all the time," says Griffiths. "This enables management within each business unit to own the output of all procure-to-pay monitoring and to take responsibility for it." The role of treasury in this context is to provide detailed insight into the mechanics of cash and payments processes within their company which can help other functions to better understand their own processes and any suspicious movements.

## Taking ownership

Ultimately, a company can only control the opportunities it gives to fraudsters; it has no control over the external pressures its staff face nor how they may rationalise an act of fraud. With or without technology, one thing is certain and that is the responsibility for preventing or capturing fraudulent activity must now be collaborative rather than individual and that the entire process must start from a company-wide ethical stance and be led by a set of policies that everyone buys into. Where there is the risk of fraud, the chances are that fraud will eventually occur, unless the organisation has identified the risk first and put effective anti-fraud controls in place. ■

# Working capital connections

*“As the newly appointed Head of the HSBC Payments and Cash Management business in Europe, I'm excited about the opportunities we have to help our clients to grow their business. With a presence in 33 European markets we are ideally placed to help clients across the globe expand into Europe and to help our European clients expand into fast growing markets in other regions.*

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**Eddie Norton, Head of Payments and Cash Management, Europe, HSBC**

In the working capital space, one of the current pressing themes is the state of connection between the physical and the financial supply chain. They have been interlinked in the past, particularly for international trade, through documentary trade solutions such as Letters of Credit (LCs). However, as trade has shifted ever more towards open account practices, a divide has appeared and can be problematic for a number of reasons.

To facilitate the finance element on open account trade, the market has seen increased take-up of solutions such as Supply Chain Finance (SCF). Particularly prevalent post global financial crisis, this proposition remains largely independent of the physical supply chain, notes Stuart Rousell, Global Head of Working Capital Advisory, HSBC. With the implementation of Basel III, the trend of widening pricing gap between highly rated and less well rated is set to continue. This is such that the great task today is to re-integrate the connectors between both sides whilst retaining their functional independence. Whilst the pressure point for that integration is the availability, or otherwise, of sufficient and sensibly-priced finance, the real stimulus for bringing both back together is buyer concern around the financial resilience of suppliers along their supply chain. “Solutions that enable the co-existence of both physical and financial supply chains provide robustness and better future-proofing,” argues Rousell. “Where we bring both together, solutions provide logistical reliance on the need for finance, but the visibility is available to financing banks and is equally available to benefit suppliers to help take out the real cost of the supply chain.”

## Exclusive systems

The data flows that exist in the procurement process often exist independently of finance solutions, often via third-party web portals or directly through Enterprise Resource Planning (ERP) systems. Indeed, says Rousell, “a number of e-Procurement platforms exist with payment, billing and even dispute management functionality. But these tend to be over-engineered for roll-out into smaller client sites, as are the majority of ERP systems; although tier one suppliers might have the resources to connect directly, the smaller tier 2 and tier 3 suppliers can often be left high and dry.” This, he notes, “usually creates a default to paper, adding unwanted costs.”

The real opportunity then lies in understanding the flow of procurement data and sharing it with banks more effectively at a transactional level, says Rousell. “There is no desire by banks to get in the way of a process that works between buyers and suppliers. What we want to do is supplement that process with perhaps a financing element; we can do that by capturing data from buyers and using that to identify suppliers,” he explains.

If the use of proprietary software means that at both ends of the chain there will be re-keying of data into different platforms, then the clarion call is for standardisation. This does not require a wholesale replacement of systems: many of the solutions that could be used already exist. These may be EDI (electronic data interchange) standards-based offerings capable of fulfilling an order straight through from purchase order to fulfilment.

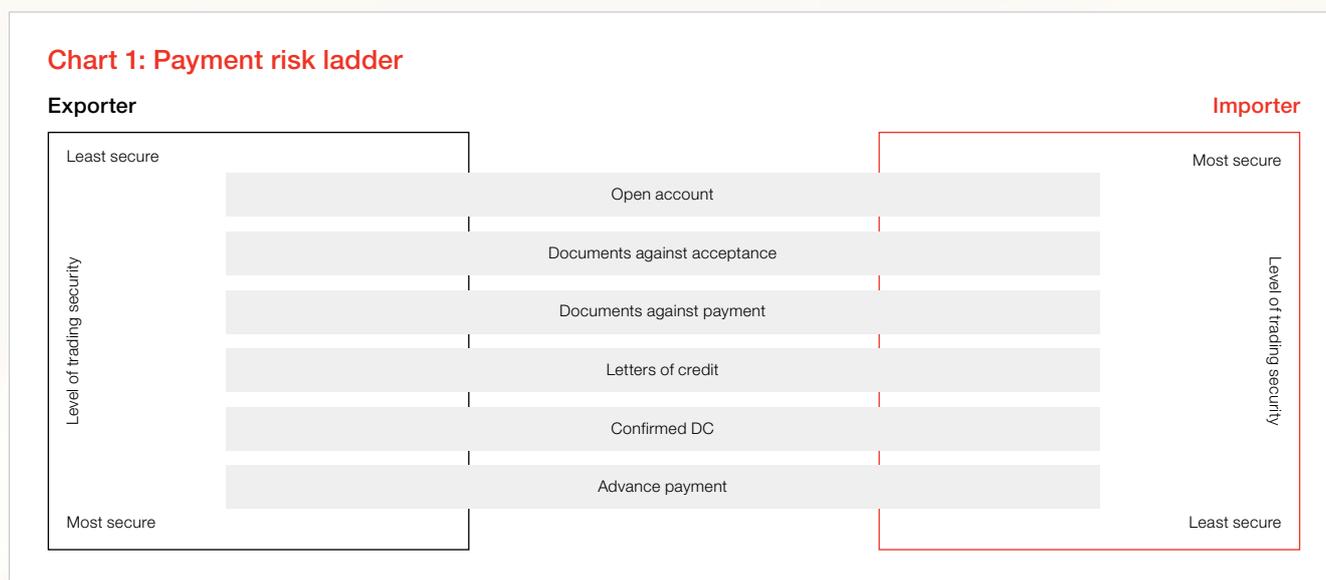
EDI standards (such as EDIFACT and the US-centred ANSI) have been available for more than 30 years. However, one of the key issues for products using EDI-based software is still supplier on-boarding. “Many of the solutions in this space have been designed for the buyer not supplier,” notes Rousell. He feels there is also a lack of understanding amongst smaller businesses around what can be achieved with the existing toolkit. However, he does feel that there is at last “greater collaboration coming down the supply chain,” this being driven by an across-the-board need for efficient working capital management and a better view on where costs can be taken out. His ideal is clear: “We need to be heading towards common data being shared as an in-built process where, as soon as there is invoice acceptance, the next stage is automatic presentment of that invoice to the bank for financing; that is not an automated process today.” The most active users of EDI standards are the “logistically challenged” automotive and retail sectors.

Even so, elements of the physical supply chain often act independently, with electronic delivery notes being followed by manual acceptance of delivery, frequently creating reconciliation issues for stock and payments. “But within the EDI environment, there is an opportunity to electronically pass that acceptance notice to a bank for financing.” Additionally, in the stock-control environment, across multiple sectors, universal GS1 Bar Code standards are being used to identify individual goods or parts so data can be captured at various points of the physical supply chain lifecycle. This can be shared between different stakeholders within that chain, including those in the financial supply chain.

## Co-operation with leadership

“If the parts of the solution already exist, then what is required to make it work is increased co-operation around working capital between business functions,” explains Rousell. Driving change internally thus rests with the fundamental question of working capital ownership. It could equally be claimed by operations, procurement, financial control or treasury, but each has a different agenda. This, he observes, means “too many silos leading to too many conflicting processes.” One way to break down these silos is to establish a head of working capital. Reporting to the CFO, the role should focus on driving efficiencies and costs through analysis of key elements such as Days Sales Outstanding (DSO), Days Payable Outstanding (DPO) and Days Inventory Outstanding (DIO) and aligning objectives.

**Chart 1: Payment risk ladder**



Source: HSBC

In a wider context, (using the automotive sector as an example), the collaborative model will require a change of practice by some suppliers to enable acceptance of electronic delivery notes. “If we can get to a stage where there is further integration of banking into that process, we can get to a point of providing finance,” explains Rousell. “This would be self-liquidating at an individual transactional level, not merely on aggregated values.”

## The value of virtual

Further to the above, a simple form of financed payment is a corporate card. When it comes to purchasing solutions a number of opportunities have opened up in recent years. Perhaps one of the most surprising developments in the business to business (B2B) space, and one not necessarily associated with the supply chain, is the rise of the humble card to a position of significant status within a treasurer’s tool box. Traditional Travel and Expense cards have evolved into broader B2B card programmes, for supplier payments. The ever-improving security and more sophisticated usage controls has seen payments values rise accordingly and can provide treasurers with the confidence to make card payments upwards of £1m. And perhaps the most significant development to arrive in the card arena – and facilitate the security of these larger payments – is the creation of virtual cards.

The ‘one-time use’ virtual card leverages the existing card network for acceptance and settlement in the B2B space, whilst effectively locking down the card number to a specific purpose or set of purposes, controlling factors such as purchase type, value, date and supplier. The inherent flexibility of virtual card numbers is complemented by an array of interfaces which can be used to generate them, for example, a traditional payment file can be used to create a batch of virtual card payments. The most recent evolution of the virtual card has even seen the cards being processed directly into the acquiring network so that the beneficiary need never touch the card data; the details are sent directly to its own bank where it will be processed and paid directly into the relevant account (usually within a day or two).

There are a number of reasons why the virtual card concept might appeal to a business. “Firstly, it is a very data-rich product,” explains Brian Tomkins, European Head of Corporate Cards, HSBC. “Once a payment has been settled with the supplier, having been processed through the card network as usual, the client can access real-time transaction information, making use of multiple client-selected data fields. This ensures clients can track and reconcile each payment made and offers stronger client oversight and control over spend patterns.

In addition to this, as these are commercial credit cards, it also gives up to 56 days of interest free credit from the issuing bank. This heralds a distinct cash flow benefit: the supplier receives earlier payment and the buyer receives interest-free cash flow.”

## In practice

“There are a number of B2B payment scenarios where virtual cards add value,” observes Tomkins. One-off payments for new suppliers that have not yet been brought into a purchasing programme would suit this format, with rich payment and invoicing data still being provided by the bank. Even more traditional high volume, low value payments can be optimised using the virtual card concept. If paying a courier or a travel management firm for example, where there are many transactions per month, it may be beneficial to lodge a virtual card with that supplier so all transactions can be billed to just one account. Rather than processing multiple invoices, the dedicated virtual card account means just one payment per month, for many transactions, with the benefit of enhanced data available for reconciliation of each transaction. Tomkins also notes that “increasingly, cards are being used as a simple means to enhance cash flow. In any sector where a business is typically expected to pay its bills before it is paid (such as the construction industry) the effect on cash flow can be challenging. A card programme alleviates the pressure, allowing the business to effectively create a free ‘extended float period’ enabling up to an extra 56 days to collect on its receivables.”

Of course, the supplier has to agree to be paid in this way and will be charged a fee to accept a virtual card payment, similar to any other commercial credit card. The challenge lies in ensuring the fee does not outweigh the advantage of enjoying earlier settlement of receivables. For long-term core suppliers and for those where the payment value is substantial, the traditional supply chain finance programme might still be deemed preferable. However, a major benefit of using cards over the traditional model is that it removes the often complex three-way legal contract between buyer, bank and supplier, making the on-boarding process quicker and simpler as well as opening doors to the circa 38 million suppliers that accept cards today.

## The perfect mix

The simplicity of virtual cards, combined with commercial benefits, means that this is a focus area for card issuers. “There is big focus from HSBC on the B2B space because it is still a largely untapped area compared to the more heavily penetrated T&E sector,” notes Tomkins. “This is really being driven by our clients and their level of interest on optimising payments within their supply chain” he adds. Rather than cards competing with our financed payment products, such as supplier finance programmes, virtual card programmes have complementary effect. “One of the biggest challenges in financed supplier payment products is that there is no ‘one-size-fits-all’; when we look at a client’s accounts payable file there are clearly different financing payment products that work better for some suppliers and their payment profile than others.” From international trade finance to local invoice finance solutions, the inclusion of a card programme helps to create the best possible, holistic, solution. “There is a harmonious balance to be struck between the different payment methods available. At the high end there is traditional trade finance, whilst supply chain finance is well suited to the middle ground. The fluidity of a card programme means it can effectively capture the high volume, smaller value transactions all the while providing the same benefits without some of the wider complexities,” says Tomkins. The virtual card concept will only serve to reinforce this and contribute to a wider acceptance and trust in the value and security of a card solution.

## The impact of regulation

The evolving regulatory landscape – particularly Basel III and its European interpretation, Capital Requirements Directive IV (CRD IV) – plays a significant part in the development of treasury solutions. Whilst Basel III may initially have been viewed by corporate treasurers as a challenge only for the banks, it is becoming increasingly apparent that what affects banks will indirectly be ultimately reflected in the corporate world. Today, whilst the concepts of account rationalisation, cash mobilisation, centralisation and yield optimisation remain core to most treasury operations, the arrival of Basel III – and the flurry of other major regulatory initiatives – has shifted their focus by a degree or two as treasurers need to consider the regulatory impact on their banking partners and on themselves.

Historically, banks have managed their balance sheets with a more asset centric approach impacting the scope and extent of lending decisions, says Jennifer Doherty, Global Head of Commercialisation, Liquidity & Investment Products, HSBC and a speaker at Eurofinance Copenhagen 2015. However, as Basel III’s Liquidity Coverage Ratio (LCR), Leverage Ratios (LR) and Net Stable Funding Ratio (NSFR) comes into play, banks will need to look more holistically at the impact of their client relationship on both the asset and the liabilities side of their balance sheets. Compliance with the new liquidity and leverage ratios means that banks have already begun to assess the impact of nominal value of their assets as well as the deposits profile of the liabilities. For certain deposits that cannot be redeployed for lending, sufficient high quality liquid assets (HQLA) need to be held to maintain LCR. This in turn could impact the leverage ratio and capital cost.

One point to note is the increasing importance of the ‘Operational Deposits’. These are frictional deposits that help in facilitating clients’ payables and receivables activities. As Operational Deposits are linked to daily activities, they are deemed to be more stable from a longer-term funding perspective and they reduce the LCR requirement. As the Operational Deposit requires substantially less HQLA to be held against it, the deposit derived from operational business becomes more valuable to the banks. This will lead to a rise in the importance of the operational banking relationship. Unlike historic pricing trends based on higher interest rate and yield for larger balances, Operational Deposits must be ‘priced without giving an economic incentive’ as per the Basel III directive. From a stable funding and capital cost perspective, operational relationships are therefore growing in importance for banks. Economic value for moving cash to a non-operating bank or an over-layer structure may not be as rewarding for clients as in the previous regulatory environment.

“We need to work with our clients to find different ways to make it work for both them and the bank. Clients who not only understand Basel III but also engage with their banks will have the edge,” says Doherty. “It is more important than ever for clients to segment their cash and understand what will be considered as operational. Clients should work with their banks to understand the most suitable deposit and investment offerings for their segmented cash.”

### Innovative design

The quest for a mutually beneficial position has seen the financial sector become more innovative with Basel III-compliant products such as the 30+ days Evergreen notice accounts offering. “Innovation in this space will also see current operational burdens being removed as clients can automatically and seamlessly move their cash into other suitable off balance-sheet instruments (such as money market funds or short-term cash investments) without the need for last minute placements that may not produce optimal returns,” notes Doherty. This requires an intelligent approach to liquidity investment. “Our subject matter experts are on the ground talking to clients, discussing the likely impacts of Basel III and other regulations,” says Doherty. “Although Basel III is still at a relatively early stage of its implementation (LCR will be finalised later this year and the net stable funding ratio (NSFR) follows in January 2018) HSBC is already fielding questions ranging from ‘how will the new regulations impact treasury management on a day-to-day basis?’, to specific questions such as how CRD IV will impact notional pooling.”

Commenting on the latter, Doherty says banks may take different views on how CRD IV will impact their pooling proposition depending on their regulatory and financial reporting (GAAP, IFRS etc) structure. Over time, she feels that there will be a shift in focus towards cash concentration solutions as banks become increasingly sophisticated with their offerings in this space. By offering the ability to calculate and post interest, for example, they enable the use of this model but without the additional administrative burden of an inter-company loan. However, Doherty does not see notional pooling disappearing altogether. She believes, “there is still an appetite for it,” but due to the leverage ratio implications, banks have already started engaging in deeper dialogue with clients for managing gross pool positions. “Clients will start closely monitoring their positions within their notional pools to ensure they are being used as intended, as a short-term working capital tool rather than as a source of long-term funding.”

### The need to know

As the regulatory landscape becomes more complex, so too does the level of market concern. Corporates must keep in touch with these changes and understand how they may be impacted. They also need to understand the fundamentals of the regulation and how it impacts their operations and the relationship with their banks. “Regulation can be perceived as a challenge but with it also comes opportunities,” notes Doherty. “It ensures banks and clients re-evaluate their respective positions and ensure their solutions are fit for purpose.” She believes that treasurers are now well placed because most corporates have multiple bank relationships, they have access to a diverse range of advisory services and subject matter experts. “They should be using all that knowledge to enable them to draw their own conclusions and obtain the best outcome possible for their businesses in this new environment.”

In increasingly uncertain times, a strong treasury team will find new ways to make working capital work as hard as it can to contribute to cash flows whilst educating colleagues about good working capital management. But in the push for working capital optimisation, it is clear that treasurers need to work with banks who have a wide product offering with international connectivity and the ability to facilitate working capital and supply chain solutions flexibly, as part of the overall relationship. ■



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