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July/August 2017

A new dawn for European MMFs

After a prolonged period, the rules that will govern the future of Europe's money fund industry have been published. What are the key changes and what will they mean for treasurers looking to invest short-term cash?

The Corporate View

Miguel Trinidad

Corporate Treasurer

Mexichem

Green bond developments

As more and more businesses look to become more sustainable and environmentally friendly we explore how green bonds can finance this transition and what treasurers need to do to issue green bonds.

Adam Smith Awards 2017

A day of celebration

Regulation

KYC challenges

Back to Basics

Derivative developments

Fintech Focus

Funding where it is needed

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It's ten years since the crisis. A lot has changed

It's been a decade since the financial crisis transformed the lives of all of us that work in financial markets. Looking back now, few could have imagined the sizeable impact the crisis had and still has on the world today.

Treasury, in particular, has changed markedly since those infamous years. It is a much-clichéd phrase but the profession has, without a doubt, become more strategic. This has seen treasury teams around the world step out of the back office and become much more proactive within the organisation facilitating it to do more business.

Last month, the Treasury Today Adam Smith Awards celebrated their ten-year anniversary. In a lavish Gala Presentation Lunch held at Plaisterers' Hall in the City of London, treasury professionals from around the world joined together to celebrate each other's successes.

The event reflects a tremendous transformation seen over the years. Treasurers everywhere are now developing a completely different set of skills to those required a decade ago. In this edition's Corporate View feature, Miguel Trinidad, Corporate Treasurer at Mexichem, talks about how he has evolved his skillset, allowing him to be the value-adding treasurer that he is today.

For Mexichem and a host of other businesses there is a meaningful move towards becoming more sustainable and environmentally friendly. Green bonds are one way to finance such a shift and in this edition's financing article we chart the growth of the market and find out why it should be a product that all treasury teams should pay close attention too.

Elsewhere, we take a comprehensive look at the new regulation that will govern European money market funds and find out what this will mean for corporate short-term investment policies. We also explore the latest developments in the KYC domain and see if this burdensome task is becoming any easier.

Congratulations to all our winning corporates

Finally, all of us here at the Treasury Today Group would again like to extend our sincere congratulations to all the winners in our 2017 Adam Smith Awards. More information about the winning solutions are available in our Adam Smith Awards Yearbook and on our website.

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Launched in 2007, BNP Paribas' Cash Management University is due to celebrate its tenth anniversary towards the end of 2017. We spoke with Carole Djen-Ullmo, Global Head of Marketing and Communications at BNP Paribas Cash Management about this highly successful and important event in the treasury calendar.

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The challenges of KYC

For treasurers around the world, the challenges associated with know your customer (KYC) compliance have escalated rapidly in recent years. With corporates increasingly struggling to meet KYC requirements, what specific challenges do they face – and what developments and initiatives could help them to overcome these issues?

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Successful businesses in the future will be those that consider the impact they are having on the environment and take active steps to reverse this.

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Miguel Trinidad
Corporate Treasurer
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In plotting his career path, Miguel Trinidad, Corporate Treasurer at Mexichem, has carefully picked roles that have enabled him to build a skillset to reach the very top of the profession. Now he is building a best in class treasury department that seeks to add value to the organisation.

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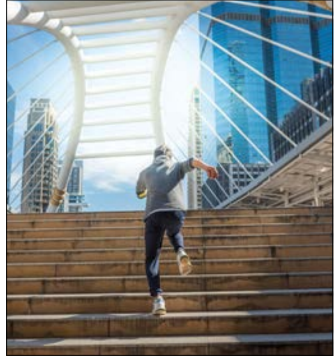
Exercising options: getting back to basics with derivatives

Derivatives have been traded for many years as both a risk mitigation tool in their simplest form, and as an instrument of profit generation in their more exotic incarnation. For corporate treasurers, they can help mitigate risk of future price movements in the underlying commodity, currency or interest rate, allowing for more accurate budgeting and forecasting. To find out more Treasury Today goes back to basics on this multifaceted topic.



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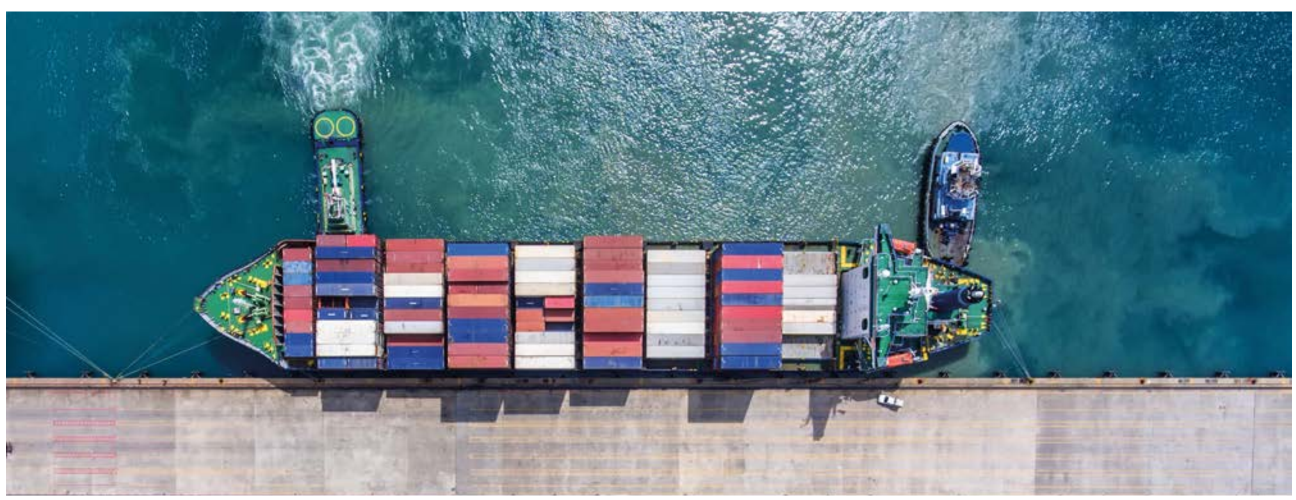
Funding where it is needed

CrossLend believes that the financing space needs a shake-up and has developed a solution that aims to do exactly that.



Shaping up and shipping out: Maersk expands trade finance offering

Maersk's trade finance offering is part of the company's ambition to simplify and digitise how its customers do business and thus simplify global trade.

"The processes behind global trade are still very cumbersome, time-consuming and expensive," says Vipul Sardana, Global Head – Maersk Trade Finance. "In fact, many of the core processes are completed as they were over a century ago; this doesn't have to be the case anymore."

Maersk is very active in leveraging technology to digitise its processes. For example, 98% of its customers' bookings are made through its electronic channel – just as a seat is booked with a commercial airline.

Although this work is beneficial for both Maersk and its customers, for the company to achieve its ambition of enabling global commerce, it must do more.

Overcoming financing challenges

Most notably, Maersk's customers cannot always access sufficient and readily-accessible finance. Indeed, the WTO recently reported that access to capital is one of the biggest inhibitors to global trade.

More than that says Sardana, Maersk's customers say that when they use a bank's trade finance product there is always a trade-off between security and simplicity. "A Letter of Credit mitigates risk but it is inefficient, complex and often costly," he explains. "The Open Account, however, provides simplicity but does very little to mitigate the risk.

"It is a shame that this decision has to be made as both security and simplification are critical to the future of global trade," Sardana adds. "But banks are very cautious to make trade finance transactions and their entire product suite is designed to mitigate the underlying risks."

Maersk's offering provides both security and simplicity, says Sardana. "We have a digital platform that our customers use to apply for financing," he explains. "After they apply we can utilise a wealth of data to quickly, but diligently, check their creditworthiness."

Once a credit line is granted and Maersk takes control of the shipment it pays 80% of the purchase order (PO) value to its customer. Upon completion of the shipment and once the consignee pays 100% of the PO value, the shipping documents are exchanged and the process is complete.

All round benefit

Maersk's customers benefit using this solution by accessing financing quicker, allowing them to do more business sooner. "Banks normally release funds when the Bill of Lading is provided, which is generated two to three days after the ship sets sail," Sardana explains. "Given that cargo is typically handed over to the shipment company well before the ship sets sail, companies may have to wait two to three weeks to get the Bill of Lading and therefore delay financing."

Maersk's customers also do not have to post any additional collateral. "The only thing we dictate is that the goods are shipped with Maersk," says Sardana. "We mitigate the risk because we have ownership of the cargo and know exactly what it is and where it is going."

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FX code of conduct gets green light

A new set of guidelines that will guide behaviour and best practice in the global FX markets have been released by the Foreign Exchange Working Group (FXWG) under the supervision of the Bank for International Settlements (BIS).

The new guidelines come after a swath of scandals in the FX market – most notably in 2013 when it was revealed that currency dealers had been rigging the foreign exchange benchmark rates.

According to the FXWG, the guidelines are a set of "global principles of good practice in the foreign exchange market" and the code has been "developed to provide a common set of guidelines to promote the integrity and effective functioning of the wholesale foreign exchange market".

A closer look at the code

The 78-page code is organised around six key pillars with respective leading principles as follows:

1. **Ethics**. Market participants are expected to behave in an ethical and professional manner to promote the fairness and integrity of the FX market.
2. **Governance**. Market participants are expected to have robust and clear policies, procedures, and organisational structures in place to promote responsible engagement in the FX market.
3. **Information sharing**. Market participants are expected to be clear and accurate in their communications and to protect confidential information to promote effective communication that supports a robust, fair, open, liquid and appropriately transparent FX market.
4. **Execution**. Market participants are expected to exercise care when negotiating and executing transactions in order to promote a robust, fair, open, liquid and appropriately transparent FX market.
5. **Risk management and compliance**. Market participants are expected to promote and maintain a robust control and compliance environment to effectively identify, measure, monitor, manage and report on the risks associated with their engagement in the FX market.
6. **Confirmation and settlement processes**. Market participants are expected to put in place robust, efficient, transparent and risk-mitigating post-trade processes to promote the predictable, smooth and timely settlement of transactions in the FX market.

Neill Penney, Managing Director, Trading at Thomson Reuters commenting on the code in a recent webinar said: "The code is not regulation, but it defines conduct expected by regulators and regulators intend widespread adoption. This is the industry's last chance to write its own rule book."

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European MMFs: the way forward

Following years of negotiation, European money market fund reform is close to being finalised. The new rules differ significantly from the changes already introduced by regulators in the US – so will European funds avoid the considerable outflows seen in US last year?

An end is in sight for European money market fund (MMF) reform, with the regulation set to enter into force in the coming weeks. While funds will not be required to comply with the new rules until late 2018 or early 2019, fund providers are preparing to adopt the new structures. So what do treasurers need to know about the types of fund that will be available in the future?

History of MMF reform

The impetus for the new regulation dates back to the financial crisis. The failure of Lehman Brothers in September 2008 resulted in the Reserve Primary Fund 'breaking the buck', meaning that the fund's net asset value fell below US$1 per share. This prompted a run on US money market funds – and, in the longer term, a regulatory drive to make money market funds on both sides of the Atlantic more robust.

In the US, this resulted in a programme of reform led by the Securities and Exchange Commission (SEC). The new rules, which came into effect on 14th October 2016, require funds to adopt a variable net asset value (VNAV) model, meaning that the value of the investment fluctuates with market conditions rather than being fixed at US$1 per share.

Other changes include the ability to funds to impose liquidity fees and/or redemption gates during times of stress, thereby discouraging or preventing investors from making redemptions at such times:

- **Liquidity fees** of up to 2% can be imposed at the discretion of the board if the percentage of a fund's assets that can be liquidated within one week falls below 30%. If the fund's weekly liquidity falls below 10%, the board is required to impose a 1% redemption fee, unless the board votes otherwise in the fund's best interests. Liquidity fees are automatically lifted if weekly liquidity reaches or exceeds 30%.
- **Redemption gates** are also being introduced which can temporarily prevent redemptions for up to ten business days in a 90-day period if weekly liquid assets fall below 30% of the fund's total assets.

At the same time, US prime funds are required to disclose certain information on their websites, including their daily and weekly liquid assets as well as details of any fees and gates that have been imposed.

Following the announcement of the new rules, significant outflows took place in the US, with US$1trn reportedly flowing out of prime money market funds and into government funds. This was backed up by the 2017 J.P. Morgan Asset Management 2017 Investment PeerView℠ survey, which found that only 37% of US-based investors were invested in a prime money market fund, compared to 63% in 2015.

However, as investors have become familiar with the new rules there are signs that cash has begun to return to prime funds. Half of the US-based investors surveyed by J.P. Morgan Asset Management said that their comfort level with floating NAV funds and fees/gates would be the most important factor affecting their decision to move assets back into prime funds.

MMF reform in Europe

While the same events may have set in motion money market fund reform in both the US and Europe, there are some important differences between the approaches taken by regulators.

The story so far

The European Commission issued a proposal for new money market fund regulation as long ago as September 2013. Lengthy negotiations followed, and the final rules were agreed by the European Commission, European Parliament and European Council on 14th November 2016.

The text of the regulation is expected to be published in the Official Journal of the European Union in the coming weeks. The regulation will enter into force 20 days later and will apply 12 months after the date of entry into force. The European Commission will then review the regulation within five years after the regulation enters into force and will, among other things, evaluate the impact of the regulation on investors.

In the meantime, the European Securities and Markets Authorities (ESMA) has published a consultation paper on the new regulation, covering areas such as draft technical advice, draft implementing technical standards and guidelines. Stakeholders have been asked to provide feedback on the proposals by 7th August.

What's changing?

"Whilst all MMFs will, under the new regulation, face some change, the most significant element for corporate treasurers will be the changes occurring to existing Constant Net Asset

> At this stage, LVNAV is expected to be a likely choice for many clients and is being viewed by investors as the option most akin to short-term CNAV money market funds.
>
> Jim Fuell, Managing Director, Head of Global Liquidity Sales, International, J.P. Morgan Asset Management

Value (CNAV) money market funds," observes James Finch, Head of Liquidity Management, EMEA at UBS. "This category of money market fund has in recent years seen significant usage by corporate treasurers as a cash management tool. Under the new regulation, it will be replaced by two new categories, defined as Public Debt CNAV and Low Volatility NAV (LVNAV) MMFs."

Under the new rules, three types of short-term money market fund will be available in Europe:

- VNAV MMFs, which calculate NAV using mark-to-market or mark-to-model prices. At least 15% of a fund's assets will need to consist of weekly maturing assets, and 7.5% will need to consist of daily maturing assets.
- Public debt CNAV MMFs, which maintain a constant NAV and must invest at least 99.5% of their assets in public debt.
- Low Volatility Net Asset Value (LVNAV) MMFs.

In addition, there will be one category for standard MMFs, the Standard VNAV MMF.

Understanding LVNAV

As Jim Fuell, Managing Director, Head of Global Liquidity Sales, International at J.P. Morgan Asset Management, notes, "At this stage, LVNAV is expected to be a likely choice for many clients and is being viewed by investors as the option most akin to short-term CNAV money market funds."

LVNAV funds will be able to use amortised cost accounting for assets which have a residual maturity of up to 75 days, with mark-to-market or mark-to-model valuations required for longer dated instruments. Funds can issue shares at a price equal to the fund's CNAV per unit or share as long as the constant NAV does not deviate from the actual NAV by more than 20 basis points.

At the same time, funds will be required to maintain minimum weekly liquidity of 30%. If liquidity falls below 30% and daily net redemptions exceed 10% of the fund's total assets, measures may be put in place including liquidity fees, redemption gates and suspension of redemptions. If weekly liquidity falls below 10%, mandatory fees and gates will apply. As with the other categories of MMF, sponsor support is prohibited under the new rules.

Response from fund providers

Fund providers have welcomed the changes. "It has taken a long time to get to this point, but the reforms are generally prudent and sensible," says Jonathan Curry, Global Chief Investment Officer, Liquidity at HSBC Global Asset Management. "From the outset, we've had some very clear views on what we thought the reform should focus on, and a decent number of those have made it into the final reform in Europe, such as the prohibition on sponsor support and the use of liquidity fees and redemption gates."

Fuell is similarly positive about the new regulation. "While the finalisation of the rules is still in progress, there's been a degree of greater certainty," he says, noting that the greater certainty sheds light on two important elements of the new regulations. "For one thing, the proposed new regulations offer new optionality which will allow money market funds to continue offering investors the advantages they already enjoy," he observes.

"In addition, the new regulations bring together elements of oversight which have previously been afforded not just by the previous regulations, but also by industry codes of practice, rating agency requirements and prudent practices within individual asset management firms. The new regulations we think therefore provide clarity, consistency and more certainty for investors."

A key question is whether the new rules could result in an exodus of cash similar to that seen in the US. As Finch points out, "Whenever change is introduced to a product that not only has a loyal following but some would argue didn't require significant amendment, the initial view is often that the outcome will be sub-optimal." However, he points out that since many of the reforms are already in use within existing CNAV MMFs through UCITS and ESMA guidelines, external rating agency restrictions and adherence to the Institutional Money Market Fund Associations (IMMFA) code of practice, "I don't see why the new regulation will make MMFs less attractive."

The difference in approach between US and European regulators may be key when it comes to the impact on investor behaviour. "Europe hasn't followed the approach that the United States took, which was to require prime CNAV funds to convert to VNAV," says Curry. "That's likely to lead to quite different outcomes to what we've seen in the US, where

Impact on investment policies

The 2017 J.P. Morgan Asset Management 2017 Investment PeerView[SM] survey found that 58% of respondents in Europe were considering making changes to their investment policies in the next six to 12 months in light of regulatory changes.

The survey also asked respondents about their preference in terms of the different money market fund structures which will be available in Europe under the new regulation. Twenty nine percent of respondents favoured LVNAV funds compared to 24% who cited VNAV funds. However, 44% stated that they needed more time and/or information before making a decision.

a significant majority of investors in prime CNAV funds have switched to government CNAV funds and treasury CNAV funds."

Fuell concurs: "We are not expecting to see the same significant movement of money market fund flows that we saw in the US following their regulatory reform."

Adopting the new rules

For fund providers, a key question will be whether to create new funds or convert existing CNAV funds to the new models. In the first instance, it is likely that many will opt for the latter. "We will look to convert our existing funds," says Natalie Cross, Client Portfolio Manager at Invesco. "Looking forwards, once the regulations go live, as clients get more comfortable with the different fund types we will then look to see if there is room in the market to consider different products."

It is worth noting that in practice, many fund providers already follow many of the guidelines that will be formalised under the new regulation. "We will need to do some back testing and scenario testing to find out what sort of situation would lead you to invoke the 20 basis point collar," says Paul Mueller, Senior Portfolio Manager at Invesco Fixed Income. "But to be honest, we're already operating under a similar regime collar on our S&P rated fund(s) to be consistent with a AAA rating. If the fund went outside the NAV by more than 25 basis points (an amount quite similar to the proposed regulations), it would more than likely be downgraded by S&P, so in essence we're already operating under that."

Other areas of the regulation are likewise in line with the practices already used by some providers. As Mueller explains, "The new rules put in different guidelines on liquidity, but we already operate under those liquidity requirements. There are slight differences in that you can only hold a certain amount of government securities in your liquidity bucket, but I don't think that will impact us. There is also more formalisation with fees and gates, which is slightly different – but again, we already have discretion within our prospectus to impose a gate, and many prospectuses have the same. So there isn't much that is new, but some things are being highlighted more formally."

Next steps

For treasurers, there is still some time before the new funds will become available. "It will be the beginning of 2019 before existing funds need to comply with the new regulation, and there will be a 12-month implementation process for any new funds, taking the date for these funds to comply to June 2018," says Curry. "That said, we are encouraging investors not to leave this to the last minute – we recognise that treasury teams are very busy, but we are encouraging clients to start formulating their views as soon as possible and start the necessary approval processes. In this way, treasurers can ensure they are in a position to respond as and when new funds are created."

As such, fund managers are taking steps to keep their investors up to date about the new regulations. Fuell says that J.P. Morgan Asset Management is taking a proactive approach in communicating with investors. "We're taking the discussion to them," he explains. "We have a dedicated reform resource centre on our website where we have posted various articles and insight pieces. Meanwhile, our sales team is actively talking to clients about the regulatory reform."

> We will need to do some back testing and scenario testing to find out what sort of situation would lead you to invoke the 20 basis point collar.
>
> Paul Mueller, Senior Portfolio Manager, Invesco Fixed Income

Curry notes that HSBC Global Asset Management has been very active for the last seven years in terms of keeping investors informed about the debate in Europe. "Since we've had more certainty about what the final reforms are going to be, we've had a process of engagement with our investors in a number of different formats, including one-to-one meetings, conferences and client events," he adds.

While much attention has been focused on the new LVNAV funds, it is worth noting that treasurers may choose to explore the opportunities presented by other categories of money market fund under the new rules. "What I do anticipate is corporate treasurers taking a closer look at VNAV MMFs, looking to use these in combination with the new LVNAV MMFs to create a blended portfolio," says UBS' Finch. "Whilst this approach has often been discussed, it's not really been widely implemented among treasures. One of the reason being that providers with a large corporate client base have focused more heavily on the CNAV category with limited VNAV fund options."

Given the new reforms, Finch says he wouldn't be surprised to see those providers launching new VNAV MMFs. "At UBS AM, we have managed both CNAV and VNAV MMFs in multiple currencies for many years and we see this as a particular advantage in light of the new regulations," he adds.

The big picture

Finally, it is important to note that the new rules are being introduced at a time when other factors are also affecting the short-term investment landscape, such as low/negative interest rates and the impact of Basel III on banks deposits. As such, any decisions about investment strategies will need to be made with the big picture in mind.

"Treasurers have seen the evolution of banking regulation and the impact of what banks are able to offer compared to several years ago," says Fuell. "They will be factoring this into the decisions they will have to make in a couple of years' time."

With that in mind, providers remain optimistic that money market funds will continue to meet treasurers' needs once the new structures come into effect. "While the changes may seem quite dramatic on paper, what the regulations have brought about is a coping mechanism for funds to be able to continue operating in times of market stress," concludes Invesco's Cross. "Those going down the LVNAV route should continue to operate in a similar manner as they currently do as they used to, which means there will hopefully not be too much disruption to the industry."

Money market fund reform: the bigger picture

With the new European money market fund (MMF) regulations due to come into effect over the next 18 months, J.P. Morgan Asset Management is taking a proactive approach to communicating the changes to corporate investors. Jim Fuell, Head of Global Liquidity Sales, International and Kerrie Mitchener-Nissen, Head of Product Development, International for Global Liquidity, outline what is happening and what this means for investors.

Jim Fuell
Head of Global Liquidity Sales, International

Kerrie Mitchener-Nissen
Head of Product Development, International for Global Liquidity

MMFs have long been used by corporate treasurers to manage short-term cash, making it vital to understand the regulatory changes currently in the pipeline, and the steps that treasurers should be taking as a result.

State of play

MMF reform in Europe has now entered its implementation stage. On Friday 30th June 2017, the regulation was published into the Official Journal, with the regulation coming into force on 21st July 2017. All existing MMFs will then have 18 months to comply with the new rules – in other words, a deadline of January 2019. New funds must be in compliance by 21st July 2018.

The new regulation features many components that are not necessarily new, but which have been in place through other existing regulation, including broad fund regulation, industry codes of practice and rating agency requirements. The regulations bring more clarity and consistency to the MMF landscape by drawing together these elements into one consolidated regulation.

What's changing?

At a high level, there are currently two broad categories of MMFs: short-term MMFs and standard MMFs. Under existing regulations, the standard MMF can only be run as a variable net asset value (VNAV) fund, while the short-term MMF can be run as either a constant net asset value (CNAV) or VNAV fund.

The new regulations introduce a couple of changes to the short-term MMF category. Until now, these have included government style funds and credit style funds (referred to as "prime" funds in the US). The new regulation provides optionality for investors, allowing for three new successor structures:

- A CNAV fund option, which will be permitted for "public debt" or government style funds.
- A VNAV fund option, which could be a government fund or a credit fund.
- A low-volatility NAV (LVNAV) fund, which delivers a stable NAV and is also available for credit-style offerings.

As a manager, we see the developments that have come out of the regulatory process as an opportunity. The changes will give us more flexibility to deliver different options to clients, based on their specific needs.

Considerations for investors

For treasurers, it is important to understand the various structures and the underlying characteristics of those products. The topic of fees and gates is certainly sparking interest among treasurers, particularly in light of the regulatory changes that were introduced in the US, where we saw a fairly significant dislocation, with assets moving from prime or credit-style funds over to government style funds.

But in Europe, the reaction from clients to fees and gates has been very different. Given that investors in European funds tend to be familiar with fees and gates, they are simply keen to understand how the concepts will be embedded into the regulation. As a result, we are not expecting to see the same sort of dislocation in the European MMF landscape. Indeed, we are now beginning to see some of that money shift back into prime MMFs in the US.

Another important consideration for investors is whether their funds will be considered as cash and cash equivalent. It is up to each treasurer's audit firm to determine this point, but from our perspective, very little has changed in terms of how the fund relates to the

rules. In fact, the investment restrictions embedded in these regulations are a little tighter than before, so there is no reason to believe that a fund would not continue to be considered as cash and cash equivalent going forward. By the same token, our expectation is that funds will still be accessible on a T+0 basis, and that they will continue to benefit from external credit ratings.

Of course, treasurers shouldn't look at the reforms in isolation. The investment landscape is changing, and investors have to look at all of these developments together when understanding the regulatory changes affecting MMFs. A number of other factors are influencing the short-term investment landscape, such as central bank monetary policy, which has moved rates to zero or even negative in certain currencies, as well as Basel III and its impact on banks' appetite for liability balances.

Adapting investment policy

Our clients are actively talking to us about the changes they will need to make to their investment policies and are seeking our guidance and advice on how to structure those new investment policies. Indeed, our **Investment PeerView 2017** survey found that more than half of European liquidity investors (58%) are considering changing their investment policies to meet the evolving regulatory environment. The survey, which gathered the views of treasurers, chief investment officers and senior cash decision-makers, also found that among those considering new structures, 43% ranked the risk of gating or a liquidity fee as the most important factor in their decision-making process.

When changes are required to the investment policy, these can take some time to work through. With an 18-month implementation period, clients will have plenty of time to consider their options and review their investment policies. That said, it's important that clients think ahead about how they can prepare for the implementation of the new regulation in 18 months' time. Corporate treasurers do not routinely change their investment policies every six months or every year. Ideally, a policy should have enough flexibility to navigate changing times without making wholesale changes. In the current market, however, it is essential to review the investment policy – not only because of European MMF reform, but because of wider market developments.

Ten years ago, many treasurers simply parked their money in a bank deposit account. More recently, Basel III has made this less feasible. A bank might have an appetite for operating balances, but non-operating balances are firmly off the agenda. It may also have a cap on the level of operating balances that it can take.

As a result, treasurers' capacity to manage their short-term cash using bank deposits is now more constrained, motivating them to explore alternative solutions. At the same time, they are looking for ways to navigate away from negative yield in light of negative interest rates in Europe and elsewhere.

Faced with this perfect storm of factors, prudent treasurers are seeking to implement an investment policy that focuses on their highest-priority requirements — typically including capital preservation and the need for liquidity on demand. However, treasurers also need to incorporate a level of flexibility into their revised investment policy.

Keeping treasurers informed and engaged

In light of these changes, we are focused on ensuring that our clients are fully aware of the nature of the regulations. For clients, this means gaining a clear understanding of what the similarities and differences will be between the funds they are currently investing in and the funds that they will use going forward.

As a result, we are talking to treasurers about the changing landscape, the challenges that this brings and the likelihood that MMFs will continue to play a core role in helping our investors manage their short-term investments. While returns aren't necessarily on top of the agenda for corporate treasurers, we are also talking about the challenges that these changes will bring on our ability to generate the returns they are targeting. At the same time, we are discussing the increasing importance of cash segmentation and are explaining how treasurers can generate incremental return by gaining more transparency over their investment horizons.

To support these communications, we have developed the **European MMF Reform Resource Centre**, which clients can access via our Global Liquidity web page. This includes a number of resources for clients and prospective customers. We also hold annual global liquidity investment forums around the world where existing and prospective clients can gain a clearer understanding of the changing environment by hearing from our market strategists, portfolio managers, credit and risk professionals and product development professionals.

With change comes opportunity

With the new regulation moving into implementation, we remain positive both about MMFs in general, and about the broader environment for MMFs. We expect that MMFs will remain a core component of the solutions that corporate investors use to manage their cash, in part due to the other changes affecting short-term investors, such as Basel III. Above all, we see regulatory reform as a positive catalyst for the evolution of this vibrant market, particularly when it comes to increasing awareness of the benefits of cash segmentation among corporate investors.

To find out more, visit **www.jpmgloballiquidity.com**

A DECADE DEFINED

BY EXCEPTIONAL ACHIEVEMENT

CELEBRATING TEN YEARS OF THE ADAM SMITH AWARDS

On Thursday 22nd June 2017, the very best and brightest from the treasury universe descended on the City of London to celebrate each other's success at the tenth anniversary of the Treasury Today Adam Smith Awards. Hosted at the magnificent Plaisterers' Hall situated by the ancient City Wall of London, the event's location echoed the importance of the day.

Since launching back in 2008, the Adam Smith Awards programme has become universally recognised as the industry benchmark for achievement. Beginning in London in 2008, the programme was widened with the launch of the Adam Smith Awards Asia in 2013, which have gone from strength to strength, with over 200 submissions of their own in 2016. The Treasury Today Group are proud that wherever you are in the world, if you are demonstrating true excellence in our industry, an Adam Smith Award is the certified mark of this achievement.

Showcasing the very best of the work done by Treasurers, CFOs and Finance Directors, the Adam Smith Awards place treasury firmly in the spotlight. This year the programme received an overwhelming number of submissions, with 211 nominations spanning 30 countries. With Herc Rentals, Etihad Aviation Group, Microsoft, PepsiCo and Emirates Airlines amongst those honoured, it was a who's who of leading corporates.

Taking the spotlight

The Gala Presentation Lunch began with a networking drinks reception, followed by an introductory speech from Treasury Today's founder, Angela Berry. The opening speech reflected not just on this year's award winners, but on the changes in the industry since the awards were launched and the increasingly high regard in which the treasury profession is held. She explained

that, "2017 is the tenth anniversary of the Adam Smith Awards and this is a great time to reflect on where we are in our industry today. In June 2008 at the very first Adam Smith Awards Gala Presentation Lunch, none of us could have imagined the seismic shifts in the global geopolitical and economic environment that have occurred. Since the Global Financial Crisis and over the past decade the role of treasury as a true strategic partner to the business has been established as you are challenged to deliver better and more innovative solutions. We are proud that an Adam Smith Award is the benchmark of that achievement."

Following the lunch, it was time for the awards ceremony, with crystal awards presented by Richard Parkinson, Managing Director, and Meg Coates, Associate Publisher EMEA and Americas. It was Herc Rentals who took home the coveted Top Treasury Team Award. It was also a great year for Etihad Aviation Group who were Overall Winner of the Best in Class Treasury Solution in the Middle East and won Highly Commended awards in the Best Funding Solution category, the Best Risk Management Solution category and the Best Trade/Supply Chain Finance Solution category. Microsoft also had a hugely successful year, taking home the Overall Winner award in the One to Watch category, the Best Trade/Supply Chain Finance Solution, the Best Cash Flow Forecasting Solution and Judges' Choice award and Highly Commended awards in the Best in Class Treasury Solution in Africa and Best Cash Flow Solution categories.

What does winning an award mean?

We asked some of this year's winners what an Adam Smith Award means to them. Who else can better describe what the awards represent and who they honour?

World Vision International

Overall Winner, Best Foreign Exchange Solution

World Vision International who this year were recognised as our Overall Winner, Best Foreign Exchange Solution, Ashwin Ramji, Global Assistant Treasurer replied, "Global treasury made the decision to implement a foreign exchange hedging programme over ten years ago, but recognised that static hedging is inconsistent with active cash management. It was imperative to synchronise the two, but change management takes time. Over the past few years, global treasury pursued this goal relentlessly by eliminating internal silos and emphasising a consistent message throughout the partnership that cash and risk are on the same continuum. Its effort has paid off handsomely, including its ability to generate gains by its active FX risk management programme. Today, World Vision International's global treasury is a world-class treasury function recognised for excellence by its corporate peers, as evidenced by receiving the Adam Smith Award for Best Foreign Exchange Solution."

F. Hoffmann-La Roche

Overall Winner, Best SWIFT Solution

F. Hoffmann-La Roche who were our Overall Winner, Best SWIFT Solution, represented by Marco Braehler, Head of Treasury Back Office responded as follows: "We are very proud and honoured that our hard work and treasury expertise has been identified to be a winner for the tenth Adam Smith Awards ceremony. It reflects not only the success of a single project, but our long-term efforts towards a centralised and best in class treasury, organisational and technology wise." Braehler added that he hoped their experiences could help the treasury community in recognising "the right centralised strategy, in-house treasury technology expertise and a long-term partnership with SWIFT were the success factors for this project. It was all about connecting the right people to overcome the major hurdles along the implementation path."

Herc Rentals

Overall Winner, Treasury Today's Top Treasury Team

Herc Rentals were 2017's Overall Winner for the highly coveted Treasury Today's Top Treasury Team Award. Mustally Hussain, their Vice President and Treasurer, shared his thoughts on winning this outstanding award, "Winning an Adam Smith Award is an excellent validation of our effort to build a great team and deliver value to the broader enterprise as a strategic business partner. In summary, Herc designed a centralised treasury department with automated processes and advanced analytics to deliver benefits to the enterprise. These benefits ranged from re-engineering cash and banking operations to prudent risk and stakeholder management."

Christy Barwick – Intellectual Ventures

Highly Commended, Treasury Today Woman of the Year 2017

Treasury Today Group's worldwide Women in Treasury initiative plots the treasury profession's path to diversity. Christy Barwick of Intellectual Ventures was recognised as recipient of our Highly Commended award in the Woman of the Year category. Whilst there are a number of exceptional female treasurers who are achieving great things, the profession remains largely male dominated and we want to honour those women who are excelling in their professions whilst also driving diversity in the treasury community. Christy Barwick shared some of her thoughts on why diversity in this space is important, "I think when you look at it from a finance perspective and how we can increase the return on investment, which is by increasing diversification or diversity within the group, that can add a lot of value and increase the ROI of an organisation".

When asked what advice she would offer to women seeking to build a career in treasury, Barwick responded, "I would highly recommend that women seek out mentors within the finance and treasury community, primarily for three reasons. Firstly, it will help expand your professional network. Secondly, it will offer you a different perspective on certain challenges that you might be facing, and finally, it will help set you up for success in terms of finding opportunities rather than roadblocks."

Fear of missing out?

This is just a small sample of some of the success stories heard as part of the 2017 Adam Smith Awards. In the final analysis, in spite of – or perhaps because of – continuing issues around regulation, financial uncertainty and all manner of risk, treasurers have clearly risen to the challenge. As each year's Adam Smith Awards event comes around and the panel of judges are presented with the unenviable task of selecting winners, it is obvious that this is one profession that is constantly on the hunt for the next improvement and we can only imagine how it will evolve over the next ten years.

If you think that you or your team deserve recognition for your diligence and dedication then fear not! Nominations for our Adam Smith Awards Asia are now open and will close on 8th September 2017. The Adam Smith Awards Asia honour excellence in corporate treasury implemented in the Asia Pacific area and our Gala Presentation lunch will be held on 13th November in Singapore. Nominations for the next Adam Smith Awards recognising those in EMEA and the US will open in January 2018.

Cash Management University

Launched in 2007, BNP Paribas' Cash Management University is due to celebrate its tenth anniversary towards the end of 2017. We spoke with Carole Djen-Ullmo, Global Head of Marketing and Communications at BNP Paribas Cash Management about this highly successful and important event in the treasury calendar.

Carole Djen-Ullmo
Global Head of Marketing and Communications

What is the central concept of the Cash Management University?

The Cash Management University (CMU) is a unique event designed for treasurers and senior finance professionals. It has been attracting hundreds of delegates from all over the world, who come together for two days to focus on the subject of cash and liquidity management as a performance lever for businesses. Over the years this annual event has established itself as a prominent fixture in the world of cash management. The CMU provides an opportunity for treasurers from all over the world to exchange ideas and experiences with their peers and key industry players and to get to know the latest in the business using pan-European and international case studies.

Tell us a little more about the content of a typical Cash Management University. Also, give us a flavour of the companies represented.

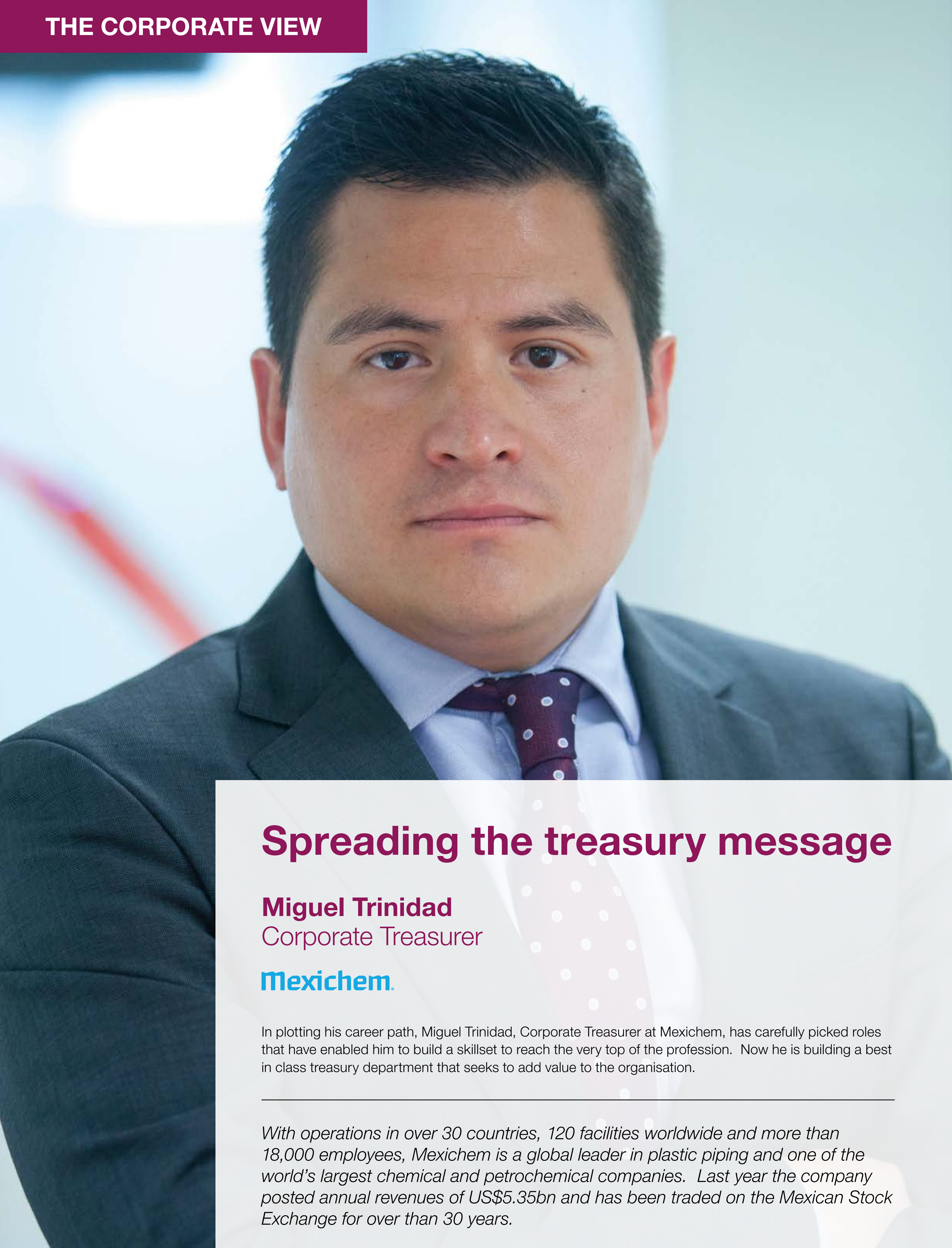
Over the years we have been using the feedback of our delegates to constantly adapt the content and the structure of the Cash Management University. For example, in 2016 the event marked a substantial change in format. We adapted the 9th CMU in order to preserve those features that make the event unique, but also moved away from a 'seminar-like' setup. We have been encouraging delegates to co-create the agenda with us so that their engagement becomes a core value of the event. In this spirit, last year's Cash Management University comprised of smaller workshop sessions on various industry 'hot-topics' like fintechs, reverse factoring and treasury robotics. We really do our best to provide unique added value to all our delegates.

As for the participating companies, BNP Paribas Cash Management, alongside other group business lines, has been bringing together major players in the cash management business. For example, the ninth Cash Management University received 260 treasury professionals, 100 group treasurers and leading treasury experts from 20 countries representing organisations like IATA, Orange, Merck, BASF, Accipiter, KPMG and SWIFT. Several of these delegates were more than just participants and took an active part in the plenary sessions or workshops of the event. This afforded them the opportunity to network with their peers as well as representatives from BNP Paribas.

2017 will mark a decade for the Cash Management University. What's in store for delegates to the tenth anniversary edition?

The motto of the tenth Cash Management University is 'EXCELerate – from knowledge to decision making'. It will be a revamped and modernised event, the first to be organised at Chateauform Paris, centrally located at Avenue George V in Paris. Instead of two full days, the event this year will be held over two half days (on 30th November and 1st December 2017), giving ample networking opportunity to delegates. The programme will consist of topics at the top of treasurers' agendas (cyber-security, fintechs, the future of treasury). I am happy to announce that along with Pierre Fersztand, Global Head of BNP Paribas Cash Management, we will have the pleasure of hosting the CEO of BNP Paribas, Jean-Laurent Bonnafé, who will open the second day of the event. The Group Chief Economist, William De Vijlder and Philippe Henrotte from HEC will talk about the global economic outlook and there will be a host of workshops and roundtables around the most important topics of the day. Additionally, there will be a special session dedicated to the second edition of our thought leadership report, Journeys to Treasury, which we are co-producing with the European Association of Corporate Treasurers (EACT), PwC, and SAP.

In 2016, delegates were invited to select a word to summarise the ninth Cash Management University and 'great' was the winner. We are committed to improving the experience this year.



Spreading the treasury message

Miguel Trinidad
Corporate Treasurer

Mexichem

In plotting his career path, Miguel Trinidad, Corporate Treasurer at Mexichem, has carefully picked roles that have enabled him to build a skillset to reach the very top of the profession. Now he is building a best in class treasury department that seeks to add value to the organisation.

With operations in over 30 countries, 120 facilities worldwide and more than 18,000 employees, Mexichem is a global leader in plastic piping and one of the world's largest chemical and petrochemical companies. Last year the company posted annual revenues of US$5.35bn and has been traded on the Mexican Stock Exchange for over than 30 years.

Miguel Trinidad, Corporate Treasurer at Mexichem, believes that treasury is about much more than the management of cash. According to Trinidad, treasury is an increasingly important function that needs to be intimately involved in all corners of the business to help manage risks and facilitate growth. This, Trinidad says, is the core objective of the strategic treasurer.

Yet elevating treasury to this level is not straightforward. To be a strategic treasury professional, Trinidad believes that you need to watch the bigger picture while keeping an eye on the details; take a global outlook while building local understanding and be technically skilled while holding management level soft skills. He also believes that the strategic treasurer should be knowledgeable while retaining a desire to keep on learning.

It is these attributes that Trinidad has looked to acquire throughout a career that has spanned multiple roles, companies and countries. Since arriving at the helm of one of Mexico's largest corporations, Trinidad has applied these skills to build a treasury that can truly call itself a value-adding function.

Charting a course

To arrive at his current position, Trinidad has followed a well-defined career path. Indeed, Trinidad's CV looks like a careers coach curated it, with each step enabling him to build on the experience gained in the previous role and take on more responsibility. Nevertheless he notes that while some degree of planning was involved, often the right role just came calling at the right time.

His first job was with a bank after graduating from the Monterrey Institute of Technology (Tecnológico de Monterrey) with a degree in economics and a specific focus on corporate finance. This was only a short stint though as he soon joined the treasury department at CEMEX to work on various projects including, client financing schemes, credit risk management, and asset financing and lease portfolio management.

In 2005, Trinidad moved to Latvia and then London to work on a post-merger integration (PMI) project after CEMEX acquired RMC Group. Trinidad's performance in the PMI made him visible to the company's top management who offered him an expat position in London to help build the European treasury centre – specifically managing the company's financial liabilities and financing in Europe (in more than ten countries). Trinidad's big break came in 2007 when CEMEX promoted him to Treasury Director for Northern Europe and the UK. In this role, he led a team of 12 across the full gamut of treasury activity.

After a successful seven years at CEMEX, Trinidad decided that he wanted to test himself in a different environment and jumped at the chance to take on the Group Treasurer role at NATRA, a mid-cap headquartered in Madrid. Trinidad was later promoted to CFO of NATRA in 2012, reporting directly to the CEO.

A phone call from a head hunter from Mexico in late 2014 piqued his interest in returning to his home country. "At the time, I was open to the idea, but I was enjoying my time in Europe so it was not something I was desperate to do," explains Trinidad. But the overall project (role, challenge, company, industry) he was offered – Corporate Treasurer at Mexichem – was too good to turn down.

"The chance to lead the treasury for a truly global multinational in expansion mode was an opportunity I had prepared for during my career," he says. "What also excited me was that I would be given the mandate to take the treasury department to the next level and re-build its overall operating model to create a truly strategic global function."

A department for all

Trinidad would call upon his previous experiences at CEMEX and NATRA to re-shape the department and ensure that it was able to match the needs of the business – and add value. This was not an easy task, notes Trinidad, as Mexichem is a complex organisation which operates numerous business lines in over 30 countries. A one-size-fits-all approach would therefore not work.

"At CEMEX, the treasury was highly centralised at the time" recalls Trinidad. "There are lots of benefits to this structure, especially the coordinated global approach, consistency and control that it provides. Yet very quickly I realised that this model would not suit Mexichem, due to the make-up of the business and the operational autonomy granted to the local business units."

On the other hand, at NATRA Trinidad had experienced working in a highly decentralised treasury and had found that empowering the local business units offered certain advantages – most notably ensuring that experts in local markets are empowered to make judgement calls that would benefit the business. But Trinidad realised that, as Mexichem was working to be a fully-fledged multinational, compliance matters and central control on selected strategic treasury and risk matters was fundamental.

Trinidad therefore decided to call on the best of both approaches and establish a hybrid treasury structure. This model sees Trinidad lead the central treasury, which maintains the global treasury policy, directs key banking relationships, drives enterprise-wide projects, manages the debt and hedging programme and acts as an advisor to the business. Empowered regional and in-country treasury teams then support the central treasury and business at local level.

Think treasury

With a treasury structure in place, Trinidad's next job was making sure that the voice of treasury was heard across the business. Trinidad had experienced the complexity of doing this at his previous roles where treasury had been a well-established function. He knew he would have his work cut out at Mexichem.

Adopting a methodical approach, Trinidad and his team start with the basics, explaining and showing the purpose and value of the treasury function to the business units. Once this elementary education is complete, the next stage is to demonstrate how the treasury can add value.

"A local business head who oversees the P&L usually has little interest in the treasury talking about new automated cash sweeping structure or host-to-host bank connectivity," says Trinidad. "But they get interested if we can save them money and help them mitigate risks. A key task has therefore been to analyse the local business unit's operations and approach the business heads with suggestions for how they can improve their performance through various treasury related projects."

Trinidad notes that many of these projects focus on improving the working capital management of the business units. "We

> Treasurers need to ensure that the technology they select not only fits the needs of the company today but can also be developed and evolved to meet the needs of the future.

have implemented a number of working capital financing projects around the world and they have been well received," he says. Another area of focus has been on payments. "We push the business units to minimise the frequency of payments runs," Trinidad explains. "There is often resistance at first, but once the cash forecast accuracy, cost and efficiency savings are demonstrated they all agree in the tangible value of these principles."

In taking the effort to spread the treasury message and show how the department can add value, Trinidad has thrust the treasury department into the consciousness of the business units. "They start engaging the treasury team and asking for our support with a variety of projects they are working on," he says. "They know that we can help them and ultimately drive further value for them. It is a position we have worked hard to achieve and we will continue to work hard in order to maintain this."

Holistic risk management

As well as supporting the business units, Trinidad spends a lot of time managing risk. He is leading a company-wide project to build up the Enterprise Risk Management culture within his company. The key objective of this is to gain a holistic and deeper understanding of all the risks (not only financial) to which the company is exposed to.

"We produce in over 30 countries and sell in over 60, so we are exposed to a wide array of risks," he explains. "As a result, we have been working to ensure that we detect, assess and understand all risks, and thus ensure we prevent, mitigate, transfer or optimally manage all existing risks."

To do this, Trinidad and his team go beyond simply identifying the risk, and dig deeper to find the root cause of it. "We don't just want to know which direction a currency is moving in, but why it is moving in that direction," says Trinidad. "By doing this we are becoming better informed and able to make better predictions about future movements – and thus we are using products or solutions that better match the risk."

Banking on technology

Away from managing risk and regulation, some part of Trinidad's time is spent surveying the ever-changing treasury technology landscape. "There is a lot happening now," he says. "The company has put a lot of effort in keeping up with the technological advances so there is now a big enterprise-wide effort to update all our systems and roll out a single instance of our ERP globally."

From a treasury perspective, Trinidad is about to launch the implementation of a single treasury management system (TMS). "This is vital to help us achieve our objectives," he says. "We have accounts with many banks around the world and from day one at the company I knew we needed to gain more visibility over our cash. A single platform will go a long way to solving this issue for me and my team."

Trinidad notes that the pace of technological change is quite daunting. "By the time I have finished evaluating a new solution, it seems that more advanced technology is available," he says. "It is important not to get too caught up in all the changes. That said, treasurers need to ensure that the technology they select not only fits the needs of the company today but can also be developed and evolved to meet the needs of the future."

People power

Investing in technology is just one aspect of creating a robust treasury for the future. Trinidad places the same emphasis – if not more – on investing in people. "Having a talented team is vital," he says. "I spend a lot of time ensuring that my staff are given challenging projects and training to help them become well-rounded treasury and finance professionals. It is about giving people the opportunity and tools to harness their skills and strengthen their expertise, to maximise the value that they offer the organisation and to ensure they can constantly improve."

With a wealth of academic qualifications behind him, Trinidad encourages his staff to seek further education outside the business. "I have spent a good amount of time and money on my continuous education," says Trinidad. "The combination of industry certificates, executive education and the MBA courses at top universities and institutions in Mexico, USA and the UK has been greatly enriching. In addition to providing me with a valuable technical skillset, continuous advanced education allows me to develop a deeper comprehension of economic, financial and business challenges and how they are managed in different regions, countries and industries around the globe. They also help equip me with the soft skills to cope with myriad complex, though rewarding, business situations."

Although he learns about these soft skills in the classroom, Trinidad claims that the true development of these skills is the real-life day-to-day situations, including the workplace. "These develop further the more interactions you have with other areas and business units," he says. "You learn what works and what doesn't and develop empathy, which is a vital trait for treasurers to have."

Heading (back) to the C-suite

Just like his curated career path, Trinidad's investment in education has been geared towards his ultimate ambition: becoming a finance leader in a truly multinational environment. Given his prior experience as CFO at NATRA and now leading the treasury team at Mexichem, Trinidad feels that he is becoming well equipped to do this.

"Most of my career has been focused on creating, transforming, and restructuring the financial situation of a company through the proper development, alignment and empowerment of finance teams," he says. "This is what I love doing and where I thrive and thus being a finance leader seems a logical goal to strive towards."

Crossing borders: transacting in Asia's new reality

Geopolitical issues have dominated the headlines in recent months, but Asia Pacific has proved resilient to these shocks. Corporations doing cross-border business in the region now need to focus on their short-term tactics and long-term strategies to fit Asia Pacific's new reality. In this article, Mark Evans, Managing Director, Transaction Banking at ANZ explains how corporates can navigate shifting demand patterns and how China's policy goals and economic profile are shaping the region.

Mark Evans
Managing Director,
Transaction Banking

The geopolitical shocks of last year – namely Brexit and the election of Donald Trump – dominated global headlines, with businesses understandably concerned about how the new reality of resurgent economic nationalism might affect cross-border trade and capital flows. Despite the heightened volatility and uncertainty, we do not think these events should be a cause for overreaction. Rather, companies should focus on obtaining a more nuanced understanding of Asia Pacific's own new reality, characterised by evolving demand patterns and the changing role of China.

The corporate community tends to agree. They tell us that long-term shifts in demand are more significant than short-term volatility, despite the practical challenges the latter may present in the short term. We also find that businesses seeking to make the most of opportunities in this new reality are realigning their thinking to match China's policy goals and changing economic profile.

Shifting demand patterns

Much attention has been paid to the potential impact on this part of the world of Donald Trump's trade policies, but we believe that Asia is well placed to withstand the resurgent politics of anti-globalisation. Others agree: the Asian Development Bank recently forecast that Asia-Pacific economies (excluding Japan) would account for 60% of worldwide economic growth this year between them, even with a moderate slowdown expected in China. The prosperity of businesses relies on the extent they can tap into this economic dynamism.

Australia, for instance, is already seeing the impact of shifting demand patterns from Asian economies in this new reality. While resources exports have been subject to some volatility in recent years – and there is little doubt the China-led supercycle is over – other sources of demand from increasingly wealthy Asian populations is catching up, supported in recent months by a softer AUD.

> Businesses hoping to tap into these shifting sources of demand need a more nuanced understanding of China's long-term development and the rationale behind its policies and decision-making.

Growth in services exports, in particular tourism, education and financial services, is rapidly compensating for weaker shipments of resources. Recent data shows the value of tourism-related services alone has almost caught up with iron ore. The constraints here are almost exclusively on the supply side, in the form of the number of flights it is possible to run from key markets, China especially. The positive knock-on effects from expanding supply by adding more flights, such as more hotels, tourism jobs and service infrastructure, are considerable and nowhere near reaching their potential.

And, of course, foreign brands still enjoy some crucial advantages within China, especially when it comes to tapping China's growing middle class' demand for quality, trustworthy products. Consumer trust in suppliers is in short supply in China, particularly in the food supply chain, leading to the ever-increasing popularity of daigou sales, where orders are placed online in China for sales agents to pick up produce in physical stores overseas with receipts often required as proof of purchase in the specified location. Reinforcing the message of trust with discerning Chinese consumers is therefore becoming increasingly important.

Understanding a changing China

This means, of course, that businesses hoping to tap into these shifting sources of demand need a more nuanced understanding of China's long-term development and the rationale behind its policies and decision-making. To say the least, this is not necessarily easy for those outside the country or those doing business across its borders, but it is increasingly important to consider in both long-term strategic planning and short-term tactics.

Taking account of China's "multiple personalities" is a useful way of understanding the tension between broad policy aims and the sometimes-opaque evolution of rules and regulations for companies transacting with the country.

> China embodies the contradictions between a laissez-faire economy and a centrally planned one.

Look at the country's Five-Year Plans (FYP). They contain detailed blueprints of economic development with measurable targets that cascade from the national to the provincial to the local level—for instance in the 13th FYP to roll out 30,000km of new high-speed rail covering 80% of major cities by 2020. They also reveal the commitment to develop strategic new industries, with the goal of making them account for 15% of GDP. So, while on one level they confirm that China's demand for resources is far from over, on another they highlight those strategic sectors that are likely to take over from the old, investment-based economy, and which might well become as important to businesses in the future.

At the same time the FYPs also reveals the tensions between long-term strategy and short-term policy. Take the government's hope for more international business to be conducted in renminbi – reiterated in its commitment in the 13th FYP to continue with the internationalisation of the currency. This necessitates exposing China's financial system more fully to global market forces, something that is sometimes hard to square with the government's overriding commitment to promoting stability.

Awkward positions

Shifts between the two priorities can put foreign companies doing business in China in an awkward position. After taking several steps to liberalise the flow of capital across its borders in recent years, and to allow the market to play a greater role in the fixing of the value of the renminbi, volatility in the value of the currency (down 6.6% against the USD through 2016) and the level of its foreign exchange reserves (which fell by nearly US$320bn in the same period) made Beijing think more carefully about this process.

China's multiple personalities

One useful paradigm for interpreting China was explored by Jason Yat-sen Li, CEO of Yatsen Associates and long-time China expert at a recent ANZ client event. He stated that China should be thought of as a country with multiple, sometimes contradictory personalities, rather than as a monolithic entity.

For instance though, the rule of the Chinese Communist Party is strictly linked to the country's geographic boundaries, China's personality as a self-sufficient civilisation stretches across national borders into diaspora populations. Another of China's personality conflicts, Li explained, arises from whether it is a communist or capitalist country: arguably it is the most successful ever of the former and is now one of the most important of the latter, all the while balancing the tensions inherent between political control and market freedom.

This tension is seen in its position as a hotbed of internet innovation while it simultaneously employs the most restrictive internet controls of any country. In commercial terms there is extraordinary freedom, as the successes of Baidu, Alibaba and Tencent have demonstrated.

The country is at least three years ahead of Australia in terms of mobile payments, Li estimated, with full integration of online-to-offline mobile payments for at least the past two years. Meanwhile the most popular messaging app, WeChat (with over 880m monthly users and counting) has full banking integration to facilitate payments and transfers.

China can hardly therefore be described as a copycat economy. In fact it is incumbent on businesses elsewhere to try to harness some of its innovative spirit. To take just one example, the breadth of the online payments ecosystem in China has given rise to many more novel ways to monetise online audiences than just advertising. These include, for instance, the proliferation of live streaming services like Kuaishou, YY and around 100 others, for which collectively revenues are now around US$3bn (compared to annual box office receipts in China in 2016 of around US$7bn).

Finally, China embodies the contradictions between a laissez-faire economy and a centrally planned one. The kind of anything-goes innovation that characterises Alibaba's meteoric rise (and crossing of sectoral boundaries) belies the staid progress of reforming China's state-owned enterprises, not to mention the existence of rolling five-year economic plans.

RMB's share as an international payments currency

Customer initiated and institutional payments.
Messages exchanged on SWIFT. Based on value.

December 2015

Rank	Currency	Share
1	USD	43.89%
2	EUR	29.39%
3	GBP	8.43%
4	JPY	2.78%
5	CNY	2.31%
6	CAD	1.70%
7	CHF	1.56%
8	AUD	1.50%
9	HKD	1.17%
10	SEK	0.93%
11	SGD	0.85%
12	THB	0.81%
13	NOK	0.66%
14	PLN	0.51%
15	ZAR	0.39%
16	MXN	0.37%
17	DKK	0.37%
18	NZD	0.32%
19	TRY	0.24%
20	HUF	0.21%

April 2017

Rank	Currency	Share
1	USD	42.14%
2	EUR	31.10%
3	GBP	7.31%
4	JPY	3.53%
5	CAD	1.92%
6	CHF	1.60%
7	CNY	1.60%
8	AUD	1.54%
9	HKD	1.19%
10	SEK	1.00%
11	THB	0.95%
12	SGD	0.95%
13	NOK	0.65%
14	PLN	0.53%
15	MYR	0.44%
16	ZAR	0.40%
17	DKK	0.39%
18	NZD	0.33%
19	MXN	0.32%
20	TRY	0.25%

Source: SWIFTWatch

Last November, the authorities took steps to impose certain exchange controls (via its "window guidance"), some of which hit foreign companies' abilities to remit dividend payments. It looks like these controls have recently been relaxed – but pinning down what is and is not allowed is far from straightforward.

Perhaps unsurprisingly, such measures mean international usage of the RMB has diminished in recent months. But such short-term fluctuations do not change the long-term calculus, or negate the goals set out in the 13th FYP. On the capital account, the plan makes clear that the bid to make the RMB an international investment currency will continue. On the current account, pressure to transact more in renminbi across borders will grow, as Chinese exporters and importers seek to reduce the risks of dealing with a third currency – typically USD – in their international contracts.

Ultimately the greater use of the RMB across borders will work to the advantage of businesses transacting with the country, too, since they will be able to deal more often with direct currency cross rates (and pricing) without worrying about the RMB's value to third-party currencies. In the end, of course, full internationalisation will require allowing the renminbi's value to float, something that seems unlikely in the short term but necessary in the long term – and so important to plan for.

Long-term strategy, short-term tactics

One core theme running through all of this is the tension between the need to react tactically to short-term volatility and to devise strategy to capitalise on long-term shifts. In that respect, the tensions in Chinese policymaking appear explicable, while the opportunities from changing demand fundamentals, and structural economic shifts, remain clear.

Too much attention has been paid to political events in recent months, removing the focus from fundamental shifts in Asia Pacific economic relationships that continue to progress, and which businesses can capitalise on. All companies that seek to do cross-border business in the Asia Pacific's new reality will need to adjust both their short-term tactics and their long-term strategy accordingly.

Financing the future of the planet

The green bond market is flourishing, but there is plenty of room for further growth. In this article, we look at the development of the market and explore why corporates should consider issuing green bonds.

In his outgoing address, former US President Barack Obama said: "We've led the world to an agreement [the Paris Accords] that has the promise to save this planet. But without bolder action, our children won't have time to debate the existence of climate change. They'll be busy dealing with its effects. More environmental disasters, more economic disruptions, waves of climate refugees seeking sanctuary."

Climate change is arguably one of the great issues of our time. And to prevent further environmental damage, significant investment is needed in environmentally friendly projects. Governments around the world have reacted to this need and have committed substantial amounts to green projects. However, this is significantly less than the US$10.5trn of green investment that the International Energy Authority estimate is required in the coming two decades to halt climate change.

Shades of green

Channelling the tens of trillions of dollars that exist in the capital market towards climate change solutions is an effective way to achieve this. And core to this is the green bond, a financing product that can be loosely defined as any bond where the proceeds are specifically earmarked for green or environmental purposes.

In an effort to tighten the definition of a green bond, the International Capital Markets Association (ICMA) has created a set of Green Bond Principles (GBPs) – a voluntary framework that looks to add some structure to the green bond market. According to Nicholas Pfaff, Secretary of the GBPs at ICMA, companies that issue green bonds can publicise to investors that they are green by posting them on ICMA's website and adhering to four key principles:

- The use of proceeds must be put towards projects that provide environmental benefit.
- There must be a clear process to determine how the project fits within the eligible Green Projects categories.
- Proceeds must be segmented and tracked so investors can ensure their money has been used towards green projects.
- A framework must be put in place to show how the company will evaluate and report the impact of the project on the environment.

However, there are some nuances that need to be addressed because not every bond that is green is labelled a green bond. Indeed, statistics from the Climate Bonds Initiative highlight that only 17% of their broader definition of 'climate aligned bonds' are labelled green bonds. Sean Kidney, CEO of the Climate Bonds Initiative, explains that a bond issued by a solar wind farm company should be considered green even if it does not register with the GBPs, for instance.

"Ideally companies would abide by the GBPs," he says. "Investors have expressed that this helps when they are reporting back to their clients and we believe that labelling is key to the overall growth of the market. However, it is important not to get caught up too much in the semantics as this can often detract from what we are all trying to achieve here."

On the flip side, there is a lot of debate about whether labelled green bonds from traditionally non-green issuers should be considered truly green. In recent months, this debate has been reignited by the green bond issuance by Spanish oil giant Repsol and the first ever sovereign green bond issued by Poland. The Financial Times reported that some investors passed on investing in these bonds because one was from an oil company and the other from a country that was also raising finance for new coal plants as well as green projects.

ICMA's Pfaff believes that investors criticising such issues on that basis are missing the point slightly. "The green bond market is meant to promote the transition of business models towards being greener and sustainable," he says. "You can therefore have non-green businesses issue bonds focused on green projects and these bonds will still be classified as green under the GBPs."

Exceptional growth

Definitional issues aside, the green bond market has grown markedly since the first issuances by the European Investment Bank and World Bank in 2007. However, in those early years, progress was slow and dominated by multilateral agency issuers. It wasn't really until the GBPs were first published in 2014 that the market began to take off and corporates began to enter the market, with issuance rising to just over US$11bn that year, up from US$3.1bn in 2013.

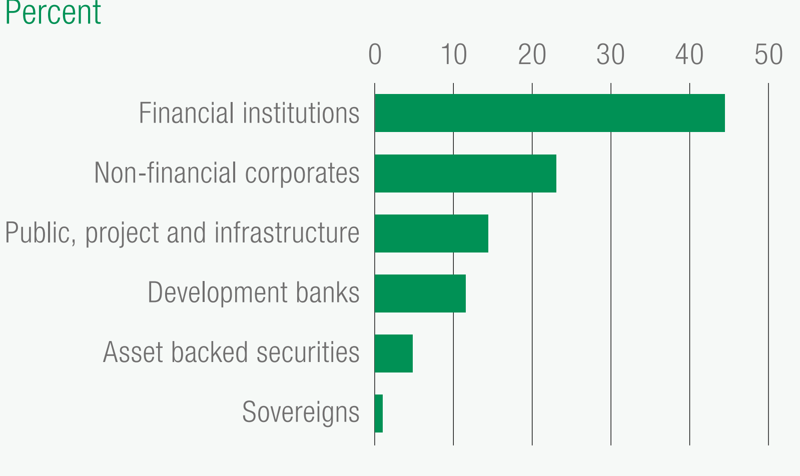
Recent growth has been more dramatic. Indeed, 2016 saw US$93bn of green bonds issued, including domestic Chinese green bonds, a record year and a greater than 100% increase compared to 2015. "All eyes have been on the green bond

A green bond

is a bond where the proceeds are earmarked for green projects

2016 issuance by type of issuer

Percent



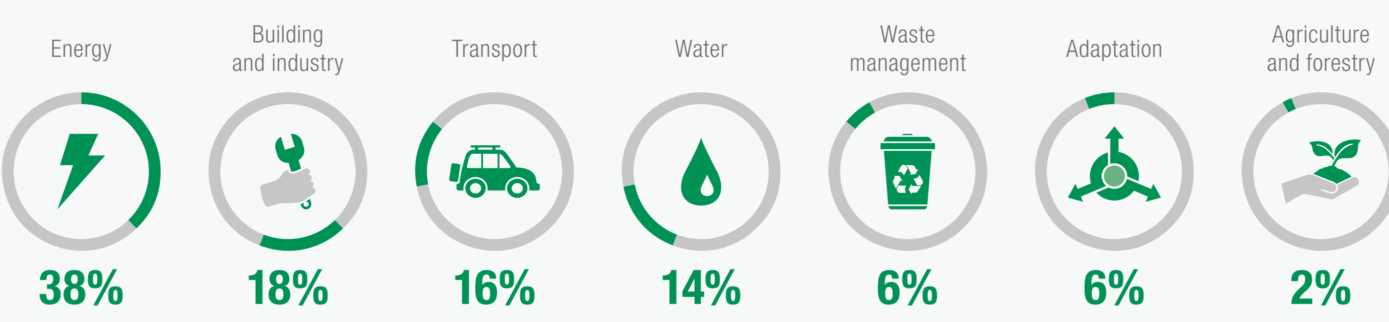
Apple's US$1.5bn green bond is the **largest** by a **US corporate**

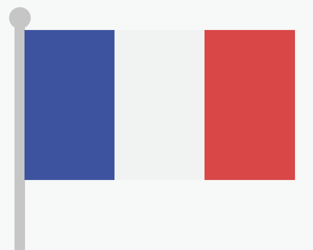
US$93bn

Total green bond issuance in 2016

Green debt raised by **Chinese entities** rose from less than US$1bn in **2015 (8th place)** to over US$23bn in **2016 (1st place)**

There was a broad range of use of proceeds in 2016





France's €7bn (US$7.5bn) **sovereign green bond** in **January 2017** is the **largest ever**

Green bonds have been **issued** by **entities** in **24 countries**

> If we are to shift our economies at the speed and scale needed to stop the planet becoming uninhabitable in the second half of this century then we need to give it everything we have. This is about survival.
>
> Sean Kidney, CEO, Climate Bonds Initiative

market in the past 12 to 18 months," explains Beijia Ma, Equity Strategist at Bank of America Merrill Lynch (BofAML). "The market has really begun to take off and this is being driven by China, which is now the world's biggest green bond market."

Ma is keen to note that while all eyes are on China, other emerging market countries are also developing green bond markets. "Europe is the most developed market," she says. "But we can't overlook the progress being made by the ASEAN countries, India and Brazil where the governments are taking active steps to develop and promote the market."

Geraint Thomas, Executive Director at MUFG, is also buoyed by the evolution of the green bond structures being used by corporates. "In the last few quarters we have seen the first hybrid structure issued by TenneT. Toyota in the US also completed an asset-backed security deal a few years back," he says. "These are important developments and I believe in the coming years we will see securitisation grow, with all the other bond structures that we are used to turning green as well."

Growth in the market is also being driven by investors hungry for green paper. "We have seen significant growth in the amount of money that investors are dedicating to green and ESG investments," says Thomas. "This has been the other significant driver behind the market and demand is still outstripping supply."

What is in it for corporates?

Attracting new investors is precisely the reason why many corporates have issued green bonds. As the Climate Bonds Initiative's Kidney explains: "The number one reason that corporates issue green bonds is to diversify their investor base. They have realised that there is a huge pool of people (and money) that like to invest in green products, many of whom they might not have dealt with before." Kidney adds that corporate treasurers have told him that if they are able to get 15-30% of new investors to register for the bond then that is a huge success and will lead to price depreciation in the future.

Kidney is also keen to add that issuing green bonds creates an investor 'stickiness' for corporations. "Investors are calling for corporates to do more green bonds and they are genuinely enthusiastic about buying green paper," he says. "This is a dream scenario for corporate treasurers issuing bonds."

Off the back of this huge demand and diversified investor base, corporates are also beginning to realise price advantages by issuing green bonds, says Kidney. "Like any market, as it gets larger, prices begin to depress," he explains. "Issuers are now realising a five to 15 basis point benefit in the dollar and euro green bond markets over traditional bond markets. This is great news and it will boost issuance next year."

Elsewhere, BofAML's Ma notes that there is a marketing benefit to be had from issuing green bonds. "Issuing a green bond can raise a corporate's overall sustainability profile," she says. "Apple, for instance, used its green bond last year to highlight all the work it is doing making sure its factories use renewable energy." Meanwhile, ratings agencies like Moody's and S&P are actively exploring how CSR commitments might factor into a company's overall credit rating.

Straight to market

If these benefits are not enough, treasurers will be pleased to hear that the process of issuing a green bond is not too dissimilar to that of issuing a traditional bond, although there is some extra work required when making the first issuance.

"The bond structure and the terms and conditions will be very similar to a non-green version of the bond," says MUFG's Thomas. "The lead-up to issuance, however, is slightly different, beginning with the internal process for identifying the use of proceeds and ensuring this fits into the investors understanding of what is green." Thomas notes that the issuing team will then need to work to make sure the bond aligns with the GBPs if it is to be labelled. "They may wish to get a second or third opinion on this to further verify the bond. This can, of course, add incremental cost to the first issue," he adds.

To encourage corporates to issue green bonds, some countries are looking to remove this incremental cost. For instance, the Monetary Authority of Singapore announced earlier this year that it is launching a Green Bond Grant scheme which will cover the costs of external reviews for green bond issuance.

Adam Stam, Director, Secured Funding at Toyota Financial Services, worked on the company's debut green bond issuance. He notes that while the credit risk associated with green bonds is no different from a traditional bond, there is an extra degree of reputational risk that needs to be managed. In Toyota's case, it was necessary to ensure that the company could rapidly deploy the funds into investment in green vehicles. "It is important that any company looking to issue a green bond is aware of the reputational risk," says Stam. "They shouldn't just jump on the bandwagon, because in doing so they run the risk of damaging their reputation by not being able to deliver on their promises of investing in projects which are considered green."

China's flourishing market

To find the world's largest green bond market you need to look towards the world's biggest polluter, China. Almost overnight, the country went from being a minor player in the market to accounting for 40% of the total value of green bonds issued globally last year. So what has been behind this rapid rise?

China is facing some serious environmental issues. The People's Bank of China has estimated that the country needs US$320bn a year to meet government targets for addressing widespread air, soil and water pollution. Encouraging the financing of a green economy is therefore just one part of a wider plan from the Chinese government to halt or reverse the environmental issues that the country currently faces.

But as Herry Cho, Director, Head of Sustainable Finance Asia at ING, explains, 'greening' the Chinese financial system is crucial if the government is to achieve its objectives. Indeed, China's 13th Five-Year Economic Plan states the importance of a "green, open and shared" development and incorporates a strategy for establishing a green financial system into the National Ecological Civilisation Construction Plan.

On the world stage China has also become a leader in the field. "As the G20 Chair, China has really put sustainability right at the forefront of the agenda and is encouraging the rest of the world to follow in its footsteps," says Cho.

Nuanced 'green'

It must be noted that while China is taking great strides in the green bond space, it is slightly unique in terms of what it qualifies as green. "Despite largely being based around the GBPs, China does have slightly more broader standards around what qualifies as green," says Cho. "This is perhaps most evident around the fact that China permits green bond proceeds to be put towards so-called clean coal projects."

Another nuance is that in other countries all proceeds from a green bond go towards green projects. In China, however, corporate borrowers may use up to half of the proceeds of the bonds for working capital and paying down loans.

To offer some statistics, the latest numbers from the Climate Bonds Initiative show that 61% of the US$2.47bn in green bonds issued by China in the first quarter of this year failed to meet the international definition of such instruments.

With the country slowly liberalising its bond market and looking to attract outside investment, more transparency and a greater adherence to international standards may be needed before international green investors feel fully comfortable investing in Chinese green bonds.

That being said, the future looks bright for China's green bond market and Bloomberg Business estimates that by the turn of the decade China's green bond market could be worth US$230bn.

Green shoots

The green bond market, at the time of writing, is on course for another impressive year. However, despite the recent growth these bonds still only make up about 1% of the total value of the world's capital markets. There is clearly a lot of room for the market to grow, and some would argue that this growth is vital to the future of the planet. What then is needed to help the green bond grow stronger?

For BofAML's Ma, more government support is key. "The long-term trajectory of the market is good, but in the short term government support will be vital," she says. "Governments offering favourable rates or subsidies to green bond issuers, like we have seen in Singapore, is just one way that this can be done. This will attract more and more companies to issue and see the benefits that this can offer."

The need for governments to offer incentives is also cited by ICMA's Pfaff. "We see significant growth in the market again this year and that is encouraging," he says. "But for the market to expand at the rate we need it to, and for it to reach new markets, governments should also consider intelligent incentives to encourage especially corporates to issue green bonds."

For ING's Cho, the need isn't just around more issuers coming to market; it is about ensuring that there are enough bankable green projects, especially in the emerging markets. "It is crystal clear that the amount of funding that is required for sustainable development is huge," she says. "But the key issue that needs to be solved in Asia and other emerging markets is making sure that there is a pipeline of bankable projects available to finance."

MUFG's Thomas agrees and would like to see smaller companies embracing the green bond market. "The biggest constraint to its further development is size," says Thomas. "Most investors are looking for bonds that meet the benchmark liquidity size. Most medium and small enterprises probably do not have green projects that fall into that category so they will struggle when issuing. It is here that securitisation can be an effective tool to grow the market."

The Climate Bond Initiative's Kidney believes that it is vital that the whole financial system comes together to make this market grow. "The market is far too small at present and not flourishing enough in my opinion," he says. "If we are to shift our economies at the speed and scale needed to stop the planet becoming uninhabitable in the second half of this century then we need to give it everything we have. This is about survival."

The challenges of KYC

As KYC requirements become increasingly onerous, what initiatives are under way to alleviate the burden – and what role can technology play in enabling treasurers to overcome the challenges?

For treasurers around the world, the challenges associated with know your customer (KYC) compliance have escalated rapidly in recent years. With banks required to comply with ever more stringent regulatory requirements – and facing the risk of regulatory enforcements and reputational damage if they are not compliant – the burden faced by treasurers in supplying the necessary information has likewise increased.

"If you talk to anybody who is remotely associated with the financial markets, KYC will come up as one of the big areas of focus," says Sanjeev Chatrath, Managing Director, Region Head – Asia, Financial & Risk at Thomson Reuters. "KYC is the foundation of any kind of banking relationship, in that banks need to understand their customers and what is happening in their businesses. Having said that, KYC has grabbed more attention in recent years because of some of the enforcement actions that have happened."

Indeed, Kristof Segers, a manager at Zanders, says that "monster fines" imposed due to anti-money laundering (AML) and sanctions control failings have incentivised financial institutions to strengthen their compliance frameworks and related processes.

With corporates increasingly struggling to meet KYC requirements, what specific challenges do they face – and what developments and initiatives could help them to overcome these issues?

Challenges for corporates

Dubbed a 'nightmare' by more than one treasurer, KYC compliance can be challenging for a number of reasons. For one thing, the process of opening a simple bank account is often far from simple. "While in the past a bank account could be opened in a matter of days or in some cases within the very same day, we now hear stories from multinationals who struggled for months to open a single bank account, especially for those corporates who have operations in developing and/or high-risk countries," says Segers.

Where specific challenges are concerned, simply getting banks to provide a comprehensive list of the items required can be problematic. "It can be difficult to get a complete list at the inception," says François Masquelier, Chairman of ATEL, the Association of Corporate Treasurers in Luxembourg. "Sometimes banks follow up with further requests after you deliver. And even if they are satisfied with the information, that doesn't mean that they won't come back in two years' time with additional demands."

Another issue is the duplication of effort involved in KYC. All too often, treasurers are required to provide the same KYC information again and again – both to different banks and to separate departments within a single institution. As Jack Spitzer, Treasurer of global health and wellness company Isagenix International, remarks: "I can't count how many times I have told a bank, 'You already have that'."

Even once an account is open, corporates may receive recurring requests for KYC information throughout their relationship with a bank. Furthermore, unlike some other regulatory requirements which can be leveraged for the benefit of the company, KYC compliance doesn't bring any advantages from a treasury point of view. "What makes this annoying is that it has no benefit," says Masquelier. "You don't generate any value – it's a pure compliance issue."

Lack of consistency

Compounding the challenge, the type of information requested can vary between banks and from country to country. For companies which work with multiple banks around the world, providing the necessary information can be extremely time consuming. Depending on the jurisdiction, companies may need to provide the passports, utility bills and bank statements of all signatories on a particular account.

KYC challenges in asia

Research published last year by Thomson Reuters explored the challenges faced by banks when conducting KYC and client due diligence (CDD) in Asia Pacific.

According to the Asia Pacific results of the 2016 Know Your Customer survey, which consulted 334 respondents across the region, the average time taken to onboard a new client is 26 days. The survey found that the costs associated with onboarding new clients had increased by an average of 18% over the last year and are expected to increase by another 14% in the coming 12 months.

Where specific challenges are concerned, 39% of the financial institutions surveyed cited a lack of people as the main challenge in conducting CDD/KYC processes. The research also noted inconsistent requests for information and "excessive client contact to the detriment of the client relationship" among the challenges.

Requirements may also include directors' information, such as names, addresses and dates of birth, as well as tax and legal documentation.

The lack of consistency between banks is a common challenge. "One issue is that there is no standardisation," says Bart Claeys, Head of KYC Compliance Services at SWIFT. "The regulations are strict and they are continuing to evolve. At the same time, each bank will have its own internal risk appetite and will define its internal policies."

Where specific challenges are concerned, Claeys notes that there is still a lot of physical document exchange involved in the bank to corporate space. "Sometimes these documents will need to be signed or notarised, bringing additional overhead," he says. "This varies from institution to institution. Other banks may require a different format, or may require a certified translation of the document. What this means is that every corporate is having to redo the work with every bank and for every request."

Escalating requirements

Marianna Polykrati, Group Treasurer of Chipita, a Greek based international food group of companies, points out that some the majority of banks today require corporates to provide details of their shareholding structures up to the individuals who own from 10% to 25%, depending upon either the country's Central Bank policy or the bank's own compliance policy. In some countries, the requirements can be even more arduous. "In Cyprus, there's now a requirement that each relationship manager has a face-to-face meeting with each beneficial owner," says Polykrati.

She notes that the requirements have ramped up considerably in the last two years: "Previously, we didn't have to deal with so many issues – we simply provided a declaration. But now, for example, the National Bank of Serbia requires all the certificates of directors and beneficial owners of all the intermediary companies."

Impact on bank relationships

These issues can have a significant impact on the relationship between corporate treasurers and their banks – indeed, in some cases KYC-related considerations may limit the pool of banks available to corporate treasurers. Polykrati explains that while providing the required information may not be an issue for public companies, "for a private company belonging to a fund or to wealthy individuals, there can be a reluctance to provide the necessary data such as passport copies and home addresses, primarily due to security issues."

For Chipita, which has 28 banking relationships across countries including countries India to Mexico, Ukraine and Kazakhstan, Serbia and Cyprus, Polykrati says that this has resulted in some restrictions in terms of the banks the company can work with. "In some cases the attempt to initiate a new co-operation is too bureaucratic, so we decide at the end to work only with banks which already have a relationship with our top level parent company, or a bank that our major shareholder works with," she explains.

Counting the cost

At the same time, the costs involved in KYC compliance can prompt banks to ask whether some relationships make business sense. Claeys notes that as the costs incurred by banks in doing KYC continue to rise they are, in some cases,

> If you talk to anybody who is remotely associated with the financial markets, KYC will come up as one of the big areas of focus.
>
> Sanjeev Chatrath, Managing Director, Region Head – Asia, Financial & Risk, Thomson Reuters

becoming prohibitive. "If an institution performing KYC sees the cost go up to tens of thousands of euros, they will be asking whether that justifies the business opportunity," he says. "If it doesn't, they might decide not to onboard the client."

ATEL's Masquelier says that he has direct experience of this. "In one country, one of our banks took the KYC admin burden as a reason to decline opening an account for us," he explains. "If banks start being selective in this way it will create a difficult situation – particularly for small and medium sized businesses."

All of this comes at a cost. Chatrath notes that a global survey conducted by Thomson Reuters last year found that the costs and complexity of KYC are rising with financial institutions spending on average US$60m per year on client on-boarding and KYC processes – with that cost continuing to grow around 19% a year. "A lot of financial institutions have invested pretty heavily in terms of technology and hiring," he adds. "They are recognising the need to leverage technology in order to make the customer experience much better."

Know your bank

Another consideration is that KYC isn't a one-way street. Mark Crowhurst, a Treasury Director at PwC, points out that treasurers should be asking questions about how well banks are able to protect their KYC data once it has been handed over. "Corporates want to know how well their data is being managed – they don't want it to be exposed on the ten o'clock news if someone gets hold of the files," he explains.

But there are also opportunities to benefit from banks' expertise in this area. Crowhurst says that many banks advise their clients about topics such as cyber risk, which can benefit both parties. "There's a reason why KYC and AML are important," he adds. "Treasurers should talk to banks about why the requirements are so stringent and ask how they can help them reinforce their controls."

Leveraging technology

Despite the many challenges, there are a number of developments and initiatives which may help to alleviate the KYC burden for corporate treasurers. In some locations, regulators themselves may play a part in helping to overcome the challenges. Chatrath notes, "I'm very encouraged with the amount of co-operation I've seen across regulators in Asia. They tend to be very focused around what they can do

> We are currently running a feasibility exercise and are looking at whether it is possible to define a global standard for bank-to-corporate KYC.
>
> Bart Claeys, Head of KYC Compliance Services, SWIFT

to be more enabling of the economies they operate in, while fulfilling their responsibility to avoid introducing the unnecessary risk of contagion within their regulated institutions." He adds that it is not uncommon to see a number of regulators across Asia talking to each other, learning from each other and sharing information so that they can collectively be better informed.

It is clear that technology can play a role in streamlining KYC compliance for corporates. According to Zanders' Segers, "The easiest and cheapest way is to be equally stringent towards your banks with regards to the information they request and ideally corporates should aim to agree on a standardised approach across their banking partners to prevent replication of tasks. Some companies store the relevant KYC company data in spreadsheets which they keep up to date and share with all of their banking partners on a predefined schedule."

Innovative technology is also bringing new opportunities for efficiency, and there is considerable interest in how such developments can be leveraged to streamline the processes associated with KYC and compliance as a whole. For example, the Thomson Reuters Org ID KYC Managed Service enables banks and their customers to exchange KYC related information, thereby reducing onboarding time. Other platforms include KYC.com, a joint venture between Markit and Genpact which enables corporates to upload KYC related documentation and give participating banks permission to access their data.

Aside from solutions specifically designed to improve KYC processes, technology companies are also exploring the use of technology to overcome wider compliance challenges. "We are trying to help as much as we can through our technology solutions and trusted content solutions," comments Chatrath. "For example, we've used machine learning and augmented intelligence to be able to identify fake news from trusted news, which helps us to get to things much faster using social media." He adds that the company is involved with many proof of concepts around new technologies including digital identity and distributed ledgers.

Meanwhile, Claeys says that other solutions more traditionally adopted by banks, such as sanctions screening and name screening solutions, can also play a role in supporting corporate compliance efforts. "We're seeing interest from corporate segments in getting more transparency and controls in place in order to avoid any problems later on," he adds.

Future developments

Beyond the solutions currently available, other developments could potentially help to address KYC challenges in the future. For one thing, PSD2 may provide more opportunities to make ongoing KYC processes more efficient. "Under PSD2, with a corporate's permission, a bank could access the corporate's bank statement from different banks," explains PwC's Crowhurst. "This allows the bank to look for unusual patterns in transactions." He notes that developments such as blockchain and biometrics may present further opportunities for improvements around management of AML/ KYC data and verification.

Another area of interest is the development of industry utilities. SWIFT's Claeys explains that until now SWIFT has focused on the inter-bank correspondent banking space, developing solutions to increase efficiency and transparency in KYC compliance. Particularly significant is The KYC Registry, a shared platform which enables correspondent banks to manage and exchange standardised KYC data. The Registry was launched in 2014 and is now used by nearly 4,000 banks around the world.

"This is a utility approach with one centralised environment, which means that banks only need to upload their KYC information once," says Claeys. "We check the information for completeness, accuracy and validity, and banks can then give the relevant institutions access to that data."

While The KYC Registry is designed for inter-bank rather than corporate use, Claeys says that SWIFT is increasingly receiving requests from corporates who are looking for solutions to their own KYC challenges. As such, this is an avenue which SWIFT is exploring. "We are currently running a feasibility exercise and are looking at whether it is possible to define a global standard for bank-to-corporate KYC," says Claeys. "We are considering whether a cloud based utility is something we could envisage in the bank-to-corporate segment too."

Claeys adds that SWIFT is working through some questions before deciding whether to pursue this area. In the meantime, however, he notes that there are certain questions which will need to be addressed before a solution could be developed.

"What we have seen is that it is mostly the large corporate institutions with multiple bank accounts which talk about the challenges and inefficiencies they face," he says. "But from the banks' point of view, large multinationals do not necessarily present the most challenges – rather it is the smaller corporates with fewer bank accounts which may present more difficulties in providing the expected level of transparency." As such, if SWIFT does embark on a solution in this area, decisions will need to be made about where any solution should be focused.

That said, there would be clear benefits to a solution which would enable treasurers to maintain one set of KYC information. Masquelier is an advocate of the utility approach: "Clearly it would be easier to maintain one set of data instead of 15 or 20," he says. "Any solution that would improve the situation and reduce the burden would be welcomed by corporates."

Masquelier points out that one potential obstacle is that most corporate treasurers prefer to wait until a finished product is available. "They don't want to pioneer new solutions – but we do need a few pioneers to push this through," he concludes.

Exercising options: getting back to basics with derivatives

Revered and reviled perhaps in equal measures, derivatives have been traded for many years as both a risk mitigation tool in their simplest form, and as an instrument of profit generation in their more exotic incarnation. Treasury Today goes back to basics on this multifaceted topic.

Mention derivatives and thoughts often turn to the financial crisis of 2008. Whilst it is hardly fair to blame these admittedly potentially unwieldy financial products for all of the ensuing woes, their misuse by people who either failed to grasp what they were buying into, or worse, knew exactly what they were doing, will resonate throughout the years. Not for nothing did Warren Buffett called derivatives "financial time bombs".

So, what are they that they can cause so much interest, misunderstanding and chaos? In essence, they are financial instruments where the value is generated over time on the back of the performance of an underlying asset or set of assets (commonly referred to just as the underlying) such as equities, bonds or commodities. Derivatives trade typically involves two parties – counterparties – who submit to a set of pre-agreed terms and conditions that determine individual rights and obligations.

Unless collateralised (guaranteed), the value of a derivative is dependent upon on the credit status of the counterparty. Earnings, said Buffet, are often "wildly overstated" because they are "based on estimates whose inaccuracy may not be exposed for many years".

Although sometimes highly leveraged instruments (where investment is through borrowed money – a high-risk strategy), it is important to know that derivatives can be either vanilla or exotic. There is no precise definition of either but vanilla instruments are traditionally the simplest form. These are typically used for basic risk mitigation, especially hedging, and are usually based on standard calls and puts found on major exchanges. Exotics are relatively more complex, often using non-standard underlying assets. Although they are generally used to mitigate and manage risk, derivative contracts can also be used to speculate on the price fluctuations of the underlying asset.

Using derivatives to speculate on price movements gives price exposure to an underlying asset such as a commodity, index or exchange rate or even something 'exotic' such as weather conditions in a region. Such derivative contracts – especially futures and options – are often settled in cash. Cash is just a more convenient method of executing these contracts. In a commodities deal, cash is used to pay the difference between the spot and futures price, rather than taking ownership of the physical commodity.

Corporate use of derivatives

If using derivatives to mitigate risk of future price movements in the underlying commodity, currency or interest rate, treasurers can achieve more accurate budgeting and forecasting. Fixing prices for a period also means monitoring price fluctuations of the underlying is redundant, allowing treasury to focus on more value-added tasks. Of course, derivatives are eminently tradable so treasurers are not tied in to them unnecessarily.

Trading options

Derivatives can be traded either on or off exchange. Exchange-traded derivatives (ETDs), traded through exchanges such as the Chicago Mercantile Exchange and the New York Mercantile Exchange, offer publicly available pricing. Contract terms, using standardised contracts, are non-negotiable.

However, off-exchange derivatives trades made over-the-counter (OTC) use tailored contracts with specific terms and conditions pre-agreed by the counterparties. The lack of standardisation means OTC derivatives are less liquid (because terms may not suit other buyers).

Today, most buying and selling is conducted over electronic trading networks.

Frequently used derivatives

The most common types of derivatives are options, swaps and swaptions, forwards and futures.

Options

Exchange-traded options are based on standardised contracts whereby one party has a right to purchase an agreed quantity and class of underlying at a future date at a pre-agreed 'strike' price. The right, however, is not an obligation as the buyer can allow the contract to simply expire. There are two types of option contracts that can be either bought or sold:

- **Call options** give the right but not the obligation to buy the asset at the strike price either before or on the future date. The seller is obliged to sell the asset at the strike price if the buyer exercises the option.
- **Put options** give buyers the right but not the obligation to sell the asset at the strike price either on or before the agreed expiration date. Sellers are obliged to repurchase at the strike price if the buyer exercises their option.

The nature of options means the greatest loss a treasurer will face is the cost of the premium paid to buy that option: if the market goes against them, the option is not exercised.

> Using derivatives to speculate on price movements gives price exposure to an underlying asset such as a commodity, index or exchange rate or even something 'exotic' such as weather conditions in a region.

Swaps

Swaps allow treasurers to exchange one series of future cash flows for another. The value of underlying assets, which do not need to be the same, will usually be sourced from publicly available data. Swaps are often used by treasurers to hedge against movements in interest rates. A company with a fixed interest rate may wish to swap it for a floating rate if it believes the reference rate will fall. It may also seek to fix an interest rate of a payment to eliminate some uncertainty around its cash outflows, or to hedge against an anticipated interest rate rise.

Swaptions

A non-standard method of protecting against interest movements is through a swaption. In exchange for an option premium, the buyer secures the right but not the obligation to enter into an underlying swap. A buyer securing the right to pay fixed rate and receive floating rate takes a 'payers swaption'. The right to exercise a swap where the buyer receives fixed and pays floating has a 'receivers swaption'.

Forwards

Another non-standardised derivative contract is the forward. Here, counterparties agree privately to buy or sell an asset at a specified future data at a price agreed at the time the deal is transacted. Popular types of forward contracts are currency forwards and commodity forwards. The former may be used to hedge an FX exposure when the company has a known future payable or receivable in a foreign currency.

The party agreeing to buy the underlying asset in the future assumes a long position, and the party agreeing to sell the asset in the future assumes a short position.

Futures

Futures are similar to forwards. Both give the holder the right to buy or sell an asset/commodity at a future date, although futures are exchange-traded not private agreements as per forwards. A futures contract may also require physical delivery of the underlying asset or be settled in cash. Either way, futures can be risk-laden because both counterparties are gambling on winning (when clearly only one can). At least counterparty risk is reduced because the clearing house of the exchange used to trade acts as the third party to the deal.

An account with a brokerage firm is required to buy and sell futures contracts. Having agreed a futures contract, the buyer and seller must deliver an initial margin (typically 1% to 5%) of the total purchase price of the futures contract. The profit or loss of the contract for each party is calculated on a daily basis, this being added to or subtracted from the relevant margin account. This reduces counterparty default risk.

The key regulations

Dodd-Frank Act

The Dodd-Frank Act was signed into US law in 2010. This established a new framework for regulatory and supervisory framework for the OTC derivatives market. Derivatives subject to regulation under Title VII of the Dodd-Frank Act include interest rate, credit default and equity swaps.

In meeting G20 objectives of increasing transparency and reducing systemic risk in the derivative markets, Dodd-Frank has moved all OTC derivatives onto exchanges and swap execution facilities (SEFs). This ensures most derivatives are processed through clearing houses and central counterparties.

The main requirements include reporting swap transactions to a swap data repository, clearing sufficiently liquid and standardised swaps on central counterparties, trading standardised swaps on trading platforms, and establishing higher capital and minimum margin requirements for uncleared swaps.

EMIR

The EU's European Markets and Infrastructure Regulation (EMIR) came into force in August 2012. The European Securities and Markets Authority (ESMA) drafted its Regulatory Technical Standards (RTS). These provide the detailed specifications of the regulation. EMIR applies to all OTC derivatives even when an EEA-based company is trading with a non-EEA counterparty.

The main objective of EMIR is to reduce the risks and large credit exposures seen in OTC derivative transactions. Other than some additional reporting requirements, exchange traded derivatives are less of a focus as these are already subject to rules around central clearing.

EMIR's headline requirements are for central clearing and margining of standardised OTC derivatives, the reporting of all derivative transactions to a trade repository, and risk mitigation measures for all uncleared derivatives (including collateral exchange and confirmation and reconciliation procedures).

Given their heightened importance under EMIR, firms providing central clearing services (known as central counterparties or CCPs) were subject to additional requirements around their structures and procedures.

Most non-financial companies using derivatives for hedging purposes are not expected to put their OTC derivative transactions through central clearing. This means they will not have to put up margin to cover the daily mark-to-market valuation (the most recent market price) of their derivatives.

FRS 102

For many years, derivatives non-balance sheet items. Organisations entering into OTC products recorded the impact of these instruments in their books only when settlements occurred or when they reached maturity. FRS 102, applicable to accounting periods commencing on or after 1st January 2015, changes all that.

Derivatives now have to be presented on the balance sheet at their fair value, and the credit risk to both counterparties in the transaction needs to be reflected in the calculation. This usually requires a valuation, provided by the counterparty

bank, or external advisors, deploying relatively complex derivative valuation models. Additionally, changes in the derivatives' fair value now have to be recorded in the income statement.

Under FRS 102 the derivative is accounted for independently from the hedged transaction, which can be an unrecognised cash flow – for instance, a highly probable forecast transaction, sale, or purchase in foreign currency, or future variable interest rate payments.

This means the impact of the derivative on the income statement may not occur at the same time as the underlying hedged transaction, nor in fact be represented in the same line item (that is, it not being part of EBITDA or interest expense).

Organisations can reduce or eliminate income statement volatility arising from derivatives by applying hedge accounting. But they can only do so providing they can meet certain requirements, and then actively elect to do so. These requirements are:

- To document the existence of a hedging relationship between derivative and hedged transactions.
- To demonstrate an economic relationship (that derivative and hedged transactions are expected to move in opposite ways), usually by the coincidence of the critical terms of both transactions or by undertaking a quantitative analysis of their correlation.
- To specify and quantify causes of ineffectiveness – possible mismatches between the derivative and the hedged transaction – by modelling the hedged transaction, usually using a 'hypothetical derivative' (the best possible hedge, being a proxy for the hedged risk and transaction).

Margin rules

On 1st September 2016, new initial margin (IM) and variation margin (VM) rules for non-centrally cleared OTC derivatives were introduced globally. The rules ensure appropriate collateral (such as cash, various debt securities and corporate bonds) is available to offset losses caused by the default of a counterparty.

Although only financial firms and systemically important non-financial entities are covered, each jurisdiction is able to set out its own definition of in-scope, out-of-scope and exempt entities. Most jurisdictions' rules do not yet require the exchange of margin with certain types of non-financial entity, such as those trading below the EMIR clearing threshold (ranging between €1bn and €3bn, depending on class of OTC derivative). For now, at least, threshold value alone will exclude corporate contracts.

Asia expanding derivatives

Exchange-traded equity and commodity derivatives trading is a developing market in Asia. Hong Kong and Singapore are of course the leading trading hubs, being fourth and fifth largest globally in turnover of OTC interest rate derivatives (behind the US, the UK and France).

China is now opening up overseas investors access to its foreign-exchange derivatives market. Access is limited to the hedging needs of private-sector investors' onshore bond positions. According to the State Administration of Foreign Exchange, the move in early 2017 enables hedging of bond positions and is seen as a means of driving greater investment inflow. China's interbank bond market was opened up in 2016 and can trade products including forwards, swaps, cross-currency swaps and options using domestic settlement agents. Whilst there are no specific restrictions on the notional amount of FX exposure, steps such as market access, liquidity, reporting rules, settlement dates are anticipated a future point to bring the market in line with international access.

> If using derivatives to mitigate risk of future price movements in the underlying commodity, currency or interest rate, treasurers can achieve more accurate budgeting and forecasting.

The key to securing the investment of international institutions in any new jurisdiction is the establishment of rules around close-out netting (the payment of a final sum in the event of insolvency). In this respect, Malaysia is a prime example how a framework can be used to good effect. In March 2015, the Netting of Financial Agreements Act 2015 came into force, providing legal enforceability of close-out netting provisions under Malaysian law.

In seeking to encourage derivatives market trading, Indonesia has sought to improve local banking knowledge and is now allowing international institutions to establish operations in the country in exchange for market training and guidance.

The Securities and Exchange Board of India (SEBI) also allows foreign portfolio investors to trade commodity options and equity derivatives through International Financial Services Centres. SEBI has also set up a risk-based supervision framework for brokers.

At the start of the year, Pakistan's Securities and Exchange Commission talked about developing new regulations to allow the country's stock exchange (and supported by Chinese investor cash) to issue a wider range of derivatives. This could open up the market to hedge fund trading. Cash-settled futures and single stock options were on the starting list. And in April this year, Vietnam's Hanoi Stock Exchange published listing, trading, settlement and membership rules for derivatives trade.

Global acceptance

Asia-Pacific jurisdictions seem not to be diverging too far from existing international standards and have notably been establishing processes, including confirmations timings and reporting fields, that are mostly aligned with more established trading hubs in other regions. This should serve to make market development a more cost-effective process.

But it also demonstrates that whilst emerging markets see the value of derivatives, they also heed the lessons from previous errors of judgement. The market, despite what the likes of Buffett say, is here to stay.

Time to act on climate change: engagement with consequences

Governments globally have committed to tackling climate change. The historic Paris Agreement to address climate change entered into force on 4 November 2016 with the US, China, India and Europe all ratifying their national commitments. The direction of travel is clear: keeping the global average temperature rise to well below 2°C against pre-industrial levels.

Alongside the political will for change, some of the world's largest investors, including public and private pension funds and university endowments, are increasingly recognising that they need to address the long-term financial risks and opportunities associated with the shift away from traditional energy models.

As one of the largest institutional asset managers in Europe, LGIM has always played its part by using its scale to ensure companies are addressing the transition to a low-carbon economy. In our index funds, which have to hold all the companies in the benchmark index, we have focused on using engagement with the underlying companies to drive change, rather than excluding stocks or sectors (divestment).

The investment risks surrounding climate change have become so urgent that, for the first time, we are going beyond solely engaging with companies in order to hold them to account on the issue. Companies that fail to embrace the transition to a low-carbon economy by demonstrating adequate strategy, governance and transparency will be excluded from our new Future World Fund. In all other funds where we cannot divest, we will vote against the chair of the board to ensure we are using one voice across all of our holdings. This is the first time we have pledged to do so on a global scale for the issue of climate change.

The ultimate goal is to make the companies successful in the long run by addressing the challenges of climate change and low carbon opportunities. Our innovative approach, harnessing the combined powers of divestment and voting, ensures that our engagement, on behalf of our investors, has real consequences. Representing over $1trillion of assets that we manage on behalf of our clients, this one voice can carry a lot of weight. The message is simple to all of the companies we invest in: it is no longer enough to talk. We need to act now.

The problem

The world is warming up at an alarming rate and this is starting to meaningfully alter weather patterns globally. At this rate, we will increasingly experience serious disruptions through floods, droughts, storms, bushfires, acidification and rising sea levels. Additionally, we will be impacted indirectly through interruptions to the provision of food, water and energy, and economically through the effect on trade, migration and geopolitics.

Climate change is already costing US$1.2trillion[1] a year, with 5 million deaths each year related to weather impacts and a carbon-intensive economy. Without strong action, the costs could be equivalent to at least 5% of GDP each year globally or up to 20% of GDP regionally[2].

Savings earmarked for retirement could be significantly affected by this trend, because businesses rely on strong economic growth and stable human capital. The current valuations of companies which rely heavily on policy support for their high energy consumption models are likely to be adversely affected, potentially limiting returns for investors. This means that climate change can pose a financial risk to future returns on our savings, and also raises questions about the kind of world we will want to retire in.

Finding a solution

The global temperature rise has already reached 1°C above pre-industrial levels. Scientists overwhelmingly agree that we need to limit global warming to 2°C or below in order to avoid severe consequences. Yet, 2015 was the warmest year on record.

In December 2015, 195 governments agreed in Paris to limit the temperature rise to well below 2°C. Despite this, many businesses are still basing their scenarios on a trajectory of 3°C to nearly 4°C, stating that we have no choice as energy demand is predicted to rise alongside population growth.

This is not a new story in our history. New and alternative technologies have always threatened incumbents who have too much to lose. For example, Kodak failed to embrace the powerful force of digitalisation in photography.

The market went from almost all film-based cameras to digital combined with phones cameras in 20 years. A 'Kodak moment' may sound still like picturing a precious moment, but it is a name now synonymous with myopic corporate vision and lack of adaptability.

How will energy be provided in the future? No one can predict with accuracy. But we know that a world with too much greenhouse gas is not the one we want. And continuing to finance the capital expenditure and research and development of companies whose assumptions are far from the Paris agreement will increasingly come under the spotlight.

Your money, your emissions

Everyone who has personal investments and pensions is likely to be invested in big companies which contribute significantly to global warming. As such, we all have a stake in their long-term success in order to fund our retirement.

[1]DARA and Climate Vulnerable Forum, 2012. [2]Stern Review (Stern et al.)

Some companies make a much larger contribution to global warming than others, such as utilities whose businesses generate energy from burning coal and gas. Automobile companies which manufacture cars and other vehicles running on oil also contribute a large portion of global emissions. Extractive companies that provide the sources of such fossil fuels could also play a key role in curbing emissions globally. The chart below shows the sources of greenhouse gas emissions by economic sector.

Away from those direct contributors to emissions, sectors such as agriculture play an indirect role. The ever-growing demand for food globally is currently being met by inefficient agriculture practices and a large amount of food waste. These practices not only produce large amounts of carbon emissions, but they are also the biggest threat to forestry. Forests, which work as the lungs of the planet, turn carbon dioxide into oxygen as well as providing a vital ecosystem that controls the weather and water cycles. Companies in food retail and distribution are important factors in this chain who can help address this issue.

All companies, whether they emit carbon or not, need financing. They require banks, pension funds and insurance companies to buy their shares and debt. How they invest or allocate capital holds the key to financing a 2°C world rather than a 3-4°C world, because what gets financed today is the world we will build for the future.

Making your money do the talking

Climate change is a financial issue. It is about companies succeeding in the future by setting forward-looking strategies, being efficient and financing the business models that are fit for the future. As investors in those companies, we have an interest in enhancing their value over time.

There are broadly two simple steps that can let our money do the talking. The first is for investors to find out what their funds invest in, assess their exposure to carbon, and review alternative options. LGIM has developed the Future World Fund for clients who want the potential for better risk-adjusted returns, while also protecting against the long-term risk of climate change.

The second step is for asset managers to talk to companies to assess their long-term strategies and ensure they are resilient to the forthcoming challenges of climate change. At LGIM, we are not just talking to them, but acting on it.

The LGIM climate impact pledge

We have made a commitment to address climate change by engaging directly with the largest companies in the world who hold the key to meeting the 2°C Paris target. The companies will be assessed rigorously for the robustness of their strategies, governance and transparency. Companies that fail to meet our minimum standards will be removed from our Future Fund range at LGIM. In the other funds where we cannot contractually divest, we will vote against the chair of those same companies. The Pledge is initially focused on the largest companies in the following sectors; oil and gas, metals and mining, electric utilities, automobiles, banks and insurance and food retail and distribution.

We rank all companies based on these criteria, and engage directly with them to improve their ranking. Those companies which fail to meet our minimum threshold will be excluded from the Future Funds. In all other funds where we cannot divest, we will vote against their chair of the board.

We believe this combined approach of ranking, publicising, voting and divestment can send a powerful message to all companies that their investors are serious about tackling climate change. Over time, the intention is to improve the standards and practices in these companies to make them more resilient to policy changes, more successful in providing consumers with low-carbon solutions and, ultimately, more prosperous as companies. We believe this targeted engagement can lead these key industries to be more prepared for the challenges of the future. In turn, our clients who hold stakes in these companies should benefit from their financial success in the long term.

Sending one coherent voice to companies and providing real consequences for inadequate standards is what we need to do on behalf of clients. Companies should benefit from the low-carbon transition, rather than being hampered by it. We are here to support this transition because we believe it makes financial sense.

Meryam Omi

Head of Sustainability, Legal & General Investment Management

Meryam Omi is responsible for engaging on sustainability themes globally and the development of responsible investment solutions.

Funding where it is needed

CrossLend believes that the financing space needs a shake-up and has developed a solution that aims to do exactly that.

Oliver Schimek
CEO & Founder

I like to think that CrossLend is quite unique because we are not a competitor for banks; we consider ourselves very much as a partner to the banks thus generating a true value for the existing ecosystem.

Tell us a bit about yourself and your background. How did you get into fintech and why did you want to build a cross-border marketplace lending platform?

After studying Physics and Economics at the Freie Universität Berlin, I went on to found my first company, Quantea, in 2010. This company specialised in the development of trading algorithms and currency trading IT infrastructure.

Three years later, I joined Kreditech Holding – a company which leverages technology to enable people with little or no credit history to access finance – as Chief Financial & Investment Officer. It was in this role that I became exposed to the European lending economy and it was when I developed the idea behind CrossLend.

CrossLend was founded in June 2014 and began operating officially in in September 2015. Initially, we were focused on the business to consumer (B2C) lending market, but we have since moved into the business to business (B2B) space. As a result of this work and expansion the business has grown markedly in a few years and today we have roughly 50 employees.

What were the biggest challenges getting the company off the ground?

The complexity of a highly regulated product in the B2B segment is significant. There are a lot of things that need to be developed at the same time. We're not selling clothes via an online shop. We are engaging with highly regulated entities and regulators, developing new solutions for an economy that is not particularly fast or reactive when it comes to change driven by cutting-edge technology. However, at the same time this of course is also the basis for a great opportunity. With our innovative platform we can really change something in the financial ecosystem.

What makes fintech such an exciting space and what do you find most interesting about it?

The pace of change and the solutions that are being created are what makes fintech an exciting space to work in. But I like to think that we are different to most fintechs who have decided to focus on a niche area of financial services. In some respects, these companies are competing with the banks for a finite amount of business. I like to think that CrossLend is quite unique because we are not a competitor for banks; we consider ourselves very much as a partner to the banks, thus generating a true value for the existing ecosystem.

How do you expect fintech to develop, especially in the corporate space, in the years to come?

I expect a clear consolidation in the fintech market in the next few years. Fintechs need to have a clear value proposition towards corporates in the B2B space. If you just improve single parts of the value chain of a corporate it will copy or acquire you. On the other hand, if you act as missing link or enabler for new products, you create a true value to the overall economy and create something scalable.

In corporate treasury, few are feeling the impacts of fintech as yet. Where do you think that fintech can have a real impact on the day-to-day operations of corporate treasurers?

Most fintechs so far are targeting the B2C space since many of the founders are coming from the e-commerce space. This has changed recently, however, and we are seeing more and more native fintech founders tackling B2B problems. Corporate treasurers will benefit from that development, but the ecosystem is young and needs to grow.

July 2014

Founding CrossLend

September 2015

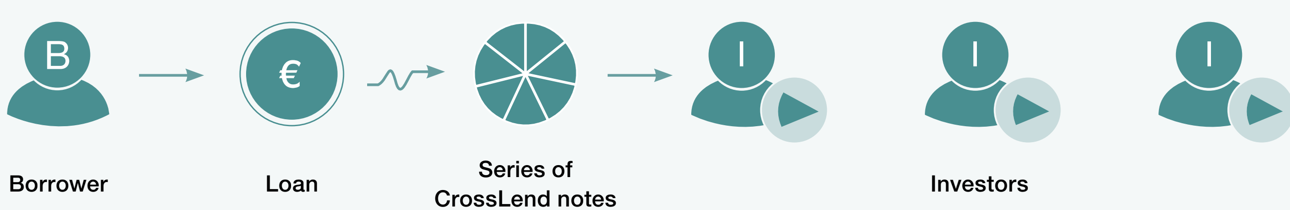
CrossLend platform goes live

September 2015

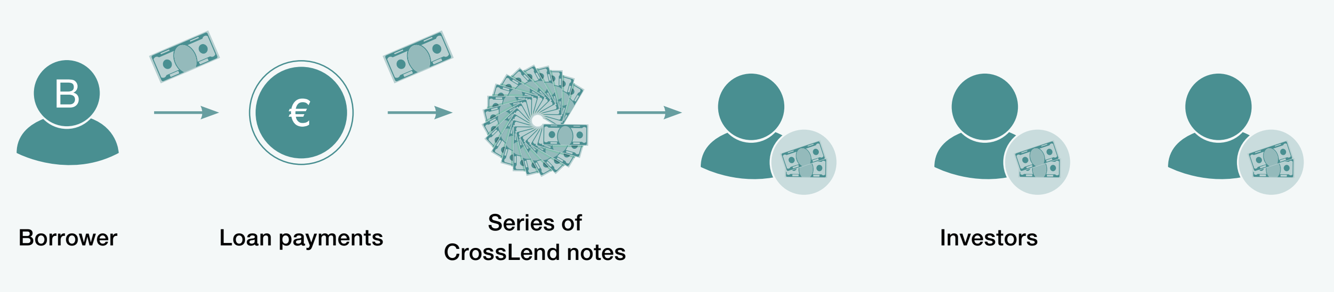
Series A Financing Round with Lakestar

How it works

The solution works by CrossLend purchasing loans that have been granted by banks and issuing a series of notes – debt securities that can be purchased by investors.



When a borrower makes their loan repayments, CrossLend makes the corresponding payments of interest and principal pro rata to the holders of the notes. Insofar as a borrower neglects to make their loan instalment payments, CrossLend owes the holders of the notes no payments. Costs for the collection of overdue loan amounts may arise, which may be deducted from any payments to the noteholders.



Transforming the credit market

CrossLend connects originators such as banks with investors such as insurance companies and pension funds. Originators can offload loans on a single loan basis from their balance sheets. CrossLend makes these available as a flexible asset to investors via 1:1 securitisation (one loan – one security, no pooling). "We have created a new European bridge between banks and investors to help bring the European Capital Markets Union to life," says Oliver Schimek, Founder and CEO at CrossLend.

Changing direction

Established in 2014, CrossLend's founders originally set about developing a European cross-border, peer-to-peer lending platform for private investors to access consumer loans. However, Europe's changing economic fortunes and the regulatory pressure on banks that is forcing them to shrink their balance sheets, seeing them able to lend less, gave Schimek and his team an opportunity to push the company in a new direction.

This new direction would see CrossLend introduce its peer-to-peer model directly to the back offices of banks, giving them a flexible instrument for refinancing their lending operations. "Our concept lets them keep the customer relationship, monetise it and service the loan without the full balance sheet implications. In that sense we make banks peer to peer capable," explains Schimek. "At the core of our approach is a new way of securitising loans where instead of issuing a bond against pools of loans, CrossLend securitises single loans with single bonds, translating the loan receivable into tradable securities with the advantage of full transparency."

"Our original idea alleviated a symptom of the sub-optional lending environment that existed in Europe," says Schimek. "Our new idea reflects the times and we think that our new solution can solve the root of the problem."

A sign of the times

"Europe is in trouble and we want to stabilise its backbone, which is the financial system," says Schimek. "Politicians and regulators have been working on the concept of a Capital Markets Union (CMU), linking savings and growth to improve conditions for savers and investors. Their action plan says we need to connect institutional and retail capital to the lending side of the economy, preferably via securitisation. Compare that to our business plan and it's basically a one-to-one match. Banks would need many years to start such a platform and it would not be independent. We are the speedboat in this market."

August 2016

Reorganisation: service for banks, insurance companies and other credit marketplaces

February 2017

Investment of Luxembourg Future Fund

April 2017

New investors: CME Ventures, Fund Promus Ventures

2017 CORPORATE TREASURY & CASHMANAGEMENT CONFERENCE

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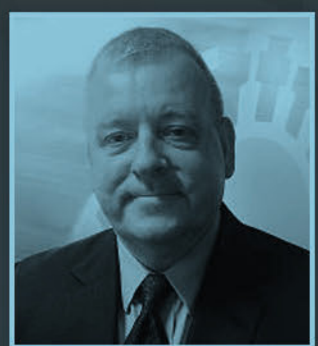

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IFRS 9

With the IFRS 9 deadline now very much on the horizon, what benefits will this bring and are corporates ready for the changes?

Pieter Sermeus

Senior Treasury and Risk Consultant

Zanders

With the mandatory implementation deadline of 1st January 2018 less than six months from now, the impact of IFRS 9 should not be underestimated. The standard significantly changes the accounting of financial instruments which can directly impact the P&L and balance sheet. The role of the treasurer may be larger than expected, as credit risk on commercial counterparties will now be more in line with the current view on financial counterparty risk.

Proactive credit risk management through forward looking provisions

While credit risks can be a significant threat to business continuity, provisions for credit losses have shown to often be 'too little too late'. IFRS 9 imposes a much more proactive credit risk methodology, moving from an incurred loss to an expected loss approach with a three stage model, where the provision is equal to the expected loss over the next 12 months or over the lifetime of the instrument, depending on its credit quality.

Correctly calculating the expected loss is based on an accurate estimation of current and future probability of default (PD), exposure at default (EAD), loss given default (LGD) and discount factors. This will increase the importance of risk models and the need for a robust governance framework. In the end, provisions under IFRS 9 will make reserves more timely and sufficient which will have a positive impact on P&L volatility.

A more principles-based hedge accounting

Although the basic hedge accounting models under IFRS 9 do not change from those under IAS 39, IFRS 9 is more principle-based, with better alignment of the accounting impact to the underlying risk management activities and an increased qualification of hedging instruments and hedged items. Hedge effectiveness criteria are now more principle-based – abandoning the mandatory 80%-125% effectiveness range – and look, for instance, at the economic relationship between the hedged item and hedging instrument.

Economic risk management objectives will be reflected better in hedge accounting under IFRS 9. It will also offer more flexibility on qualifying hedged items and hedging instruments, especially when there is an underlying economic relationship which may not have qualified for hedge accounting under IAS 39.

Market based intercompany financing

Upcoming tax regulations (such as the Base Erosion Profit Shifting project by the OECD or the Anti-Tax Avoidance Directive by the European Commission) are aimed at reducing artificial profit shifting and require arms-length pricing for intercompany loans. If the loan is not made 'at arm's length', it will have to be split in a below-market (or above-market) element and a residual loan element under IFRS 9. The below-market element will typically be recorded as an investment in the parent's financial statements while being recorded as equity in the subsidiary's financial statements. Under IFRS 9, this difference in accounting treatment can seriously impact the willingness of a corporate to issue intercompany loans which are not at arm's length.

IFRS 9 opportunities

IFRS 9 brings fundamental changes to financial instruments accounting and has its challenges, but also offers clear benefits. For corporates that are already familiar with IAS 39, the new standards of IFRS 9 introduce some useful changes to better align corporate objectives with accounting impact and financial results. The role of the corporate treasurer under IFRS 9 may be larger than expected, due to the alignment of credit risk on commercial counterparties with current financial credit risk practices. While early adopters have experienced the migration to IFRS 9 as generally positive, the main appraisal for both IFRS 9 as the corporates implementing it will be in the months ahead, with the mandatory deadline right around the corner.

For accounting periods beginning on or after 1st January 2018, IFRS 9 will be replacing IAS 39 as the accounting standard for financial instruments. However there is more to the standard than hedge accounting; it impacts how financial instruments are classified and measured, how impairments are calculated and what disclosures need to be given.

Robert Waddington

Director Corporate Treasury and Commodity Group

PwC

For corporates, the new standard has been well received, with promises that some of the frustrations of hedging under IAS 39 have been addressed. However, what are these benefits and are corporates ready for the change?

The benefits:

Alignment of accounting and risk management

The great news is that IFRS 9 provides an opportunity for alignment between accounting and your risk management. This was an annoyance of many when applying IAS 39 where what made sense from an economic point of view was not reflected in the accounting. This resulted in either P&L volatility from derivatives not being hedge accounted for or even worse, transactions that made economic sense not being entered into.

With more hedging instruments now achieving hedge accounting, I see this as an opportunity for treasurers to reassess how they manage risk.

Reduction in P&L volatility

As noted above, instruments that did not achieve hedge accounting previously might do so under IFRS 9, thus reducing P&L volatility. In addition most corporates have either used or thought about using options as a way to manage risk. Under IAS 39 the time value of an option was typically excluded from the hedging relationship and recorded in the P&L; causing more unwanted P&L volatility. Under IFRS 9, the movement in the time value of the option during its life can be deferred in reserves therefore, away from the P&L.

Hedge effectiveness has got easier

Under IAS 39, in order for a hedging relationships to be effective, the movement in the fair value of the hedging instrument divided by the fair value movement in the hedged item had to be between 80%-125%. Therefore, if the ratio was 80% then hedge accounting could be applied, however if the ratio was just 1% less at 79%, the hedge was deemed ineffective resulting in P&L volatility.

Under IFRS 9 there is now no 80%-125% threshold. However, the standard does still require you to assess effectiveness however in a different way and any ineffectiveness does still need to be calculated and recorded.

Are corporates ready for the change? At our recent IFRS 9 event, 53% of people had either:

- Not yet started looking at IFRS 9.
- Only read the standard.
- Are just about to set up a project team.

With the clock ticking it is vital that corporates focus on it now.

As IFRS 9 looms closer, many treasury teams are looking to embrace a number of advantages that will simplify hedge accounting compliance.

Bob Stark
VP Strategy
Kyriba

Under IAS 39, one of the main issues was that the pursuit of hedge accounting treatment sometimes conflicted with the reason treasury teams were hedging in the first place. Achieving a perfect 'accounting hedge' was not necessarily in sync with the ideal 'economic hedge'. Thus, a key objective of IFRS 9 was to better align the accounting treatment of a hedge with the treasury team's risk strategy.

One of the most obvious differences between IAS 39 and IFRS 9 is the lack of prospective effectiveness testing and the removal of the 80/125 rule for retrospective testing. It was felt that these particular elements of effectiveness testing could be susceptible to outside factors that falsely suggested the hedge was ineffective. Unfortunately, this could affect whether hedge accounting could continue or could even be pursued in the first place. Under IFRS 9, ineffectiveness amounts will continue to be booked to income accounts but a low effectiveness testing result will not require de-designation of the hedge.

While most corporates utilise forward contracts for hedging, some may reconsider the use of options, as the time value of options receives better treatment under IFRS 9. Under IAS 39, the time value of an option was excluded from effectiveness tests and journalised directly to P&L. This created volatility in the income statement, which is ironically what treasurers were looking to avoid in their initial pursuit of hedge accounting treatment. As a result, many avoided using options in their hedging programmes.

Fortunately, IFRS allows deferral of the option's time value to the balance sheet for a temporary period. Like the effective portions of the option's intrinsic value, the time value will ultimately be reclassified back to income accounts. But it is this initial deferral which solves a big concern for those that had previously used options to hedge prior to hedge accounting being first introduced.

Enterprises that hedge commodity risk also have much to gain under IFRS 9. One of the biggest critiques of IAS 39 was that the entire underlying commodity transaction had to be hedged. IFRS 9 takes a different approach, where individual risk components can be isolated for hedge accounting. This will mostly help organisations that have multiple risks within business contracts – and it will encourage them to hedge more because they will no longer be punished for having multiple risks within their business contracts.

With any regulatory update, there are bound to be some negatives. For most, perhaps the biggest surprise within IFRS 9 may be that hedges cannot be de-designated unless the risk management objective itself changes. Under prior legislation, treasury teams could stop their pursuit of hedge accounting and end the hedge if results didn't go their way or they wanted to try something better. That flexibility no longer exists, which puts more importance upon the setting of risk management objectives when designating the hedge in the first place.

Overall, IFRS 9 seems to have achieved its objective to solve the most popular concerns of treasury teams. The hope is that with IFRS 9 more organisations will be compelled to hedge more of their FX, interest rate and commodity risks, thus better protecting financial assets and business value of their organisations.

Next question:

"What does it take to build a digital culture within the treasury department and why should senior treasurers be looking to do this?"

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

Hawkish Fed despite low inflation

It's all change as the US tightens monetary policy and starts driving up rates in earnest. As the Trump administration looks to relax banking rules, is the world's biggest economy really freeing up market forces?

The Fed recently initiated a 0.25% rate hike and announced its intention to start decreasing its balance sheet this year. The latter means the central bank will gradually allow a fixed amount of the assets it owns to roll off. To do this, the Fed will start off by no longer investing the monthly US$10bn of bond repayments. After three months, this amount will increase to US$20bn and to US$40bn three months after that. Another increase will occur later, after which the amount will remain constant. This way, the current Fed balance sheet of about US$4,250bn will halve in about five years' time. This intended quantitative tightening will have two effects:

- It will place upward pressure on long-term interest rates.
- It will remove money from the economic system.

The two effects combined will cause a considerable increase in short-term interest rates. However, the tightening of monetary policy does not stop here as far as the central bank is concerned. Indeed, the Fed intends to raise its rates further, by another 0.25% this year. It will repeat this three more times in 2018 and then another four times in 2019. This is to achieve a Fed Funds Rate of approximately 3% by the end of 2019, the level the central bank regards as neutral – the economy is neither stimulated nor decelerated monetarily.

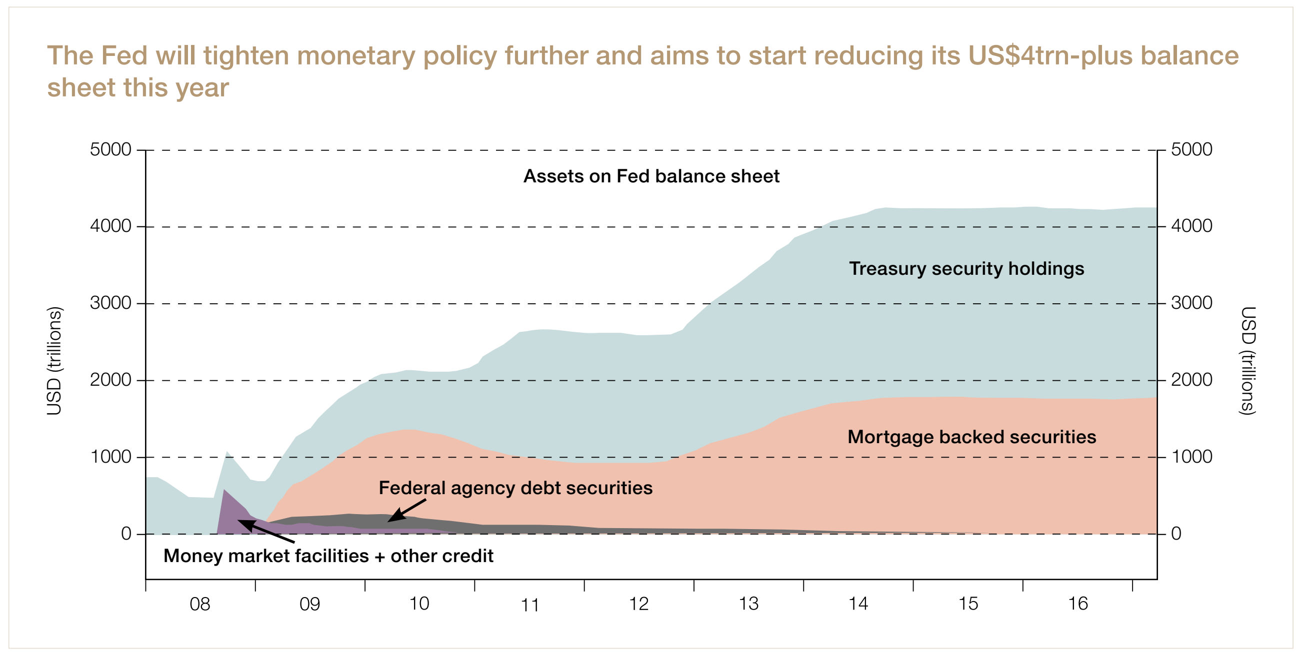
Is the Fed going too far?

Two issues are very striking:

- The Fed's intention amounts to a fairly aggressive method of monetary tightening. However, economic growth has been low and wage increases and inflation have been at persistently low levels recently. Many analysts are therefore wondering why there has been such an about-turn in the Fed's attitude. Until recently, the mantra of the central bank was "maximum economic stimulus" and consequently it refrained from rate hikes whenever possible. Now this has been reversed to "maximum tightening of monetary policy, unless this proves too heavy a burden on the economy". Many consider this to be overkill and a policy mistake in the current circumstances.
- The markets totally disbelieve the Fed and indicate they anticipate that for the time being, growth, wage increases and inflation will remain at levels so low that the Fed will barely be able to raise its rates in practice.

It is not the first time a major discrepancy exists between what the Fed indicates it intends to do and what really happens. The markets are usually proved right in these cases, so it is even more remarkable that the central bank is taking such an opposing stance. What could be the cause of this?

When answering this question, the most obvious step to begin with is to look at what the Fed itself says about this. The central bank first of all believes the recent low levels of growth, wage increases and inflation are, to a large extent, rooted in one-off developments, which will soon blow over. According to the Fed, growth will pick up soon in all likelihood, especially as monetary policy is still very loose, which is stimulating the economy considerably, while the labour market is already tight. This means that if the US economy were to continue to grow by 2% or more, the labour market would tighten further, with



Source: Thomson Reuters/ECR Research

substantially higher levels of wage increases therefore no longer being far off, despite all manner of structural forces exerting downward pressure on wage increases. Of course, the central bank could still delay further tightening of monetary policy until all this clearly emerges, but this would run the risk of the Fed suddenly having to hit the monetary decelerator hard, which could easily lead to a recession, the collapse of asset prices and the debt pyramid. Making a start with tightening monetary policy now and proceeding with this at a steady pace seems a safer policy.

Inside information and political games

What could also play a role here in the background is that the Fed might have good indications that Congress will decide upon tax reforms and tax cuts after all by the end of this year/the beginning of next year. Added to this, the White House is, at the time writing, working on a relaxation of rules for banks. These are all elements that could additionally boost growth and could ensure it ends up above 3% for several quarters next year. Given the low increase in the workforce and in productivity, this would lead to a further substantial decline in unemployment. This would therefore basically mean the markets currently have far too negative a view of growth forecasts, at least as far as the interest and capital markets are concerned, because stock markets actually foresee a very favourable future.

An entirely different angle is that the Fed is playing a political game. Indeed, many Fed members will have to step down at the beginning of next year. Combined with the positions that will have to be filled anyway, this will give Trump the opportunity in the Senate – which has to endorse the nominated Fed members – to compose the Fed entirely according to his own preferences. Trump himself has regularly changed opinion in this respect because he initially believed Janet Yellen was causing market bubbles with her low interest rates and high money creation, while he later actually complimented her on keeping rates low.

Nevertheless, there is a large group within Congress that believes the policy of low interest rates and high money creation interferes far too much with free market forces. According to them, this leads to more and more misallocation of capital, which could ultimately catch up with the economy. This group of Congress members intend to appoint new Fed members who will quickly put a stop to high money creation and low interest rates. All predictions of further rate hikes might therefore well be a pretence of the present Fed members seeking to accommodate the views of the hawks in Congress. For the interest rates it makes a huge difference what the right interpretation is.

We believe the first interpretation is the most likely as we think a combination of very easy monetary conditions, increasing purchasing power, possible tax cuts and deregulation will result in higher growth and more upward pressure on inflation in the coming quarters. In itself, the Fed could easily implement its plans for interest rates. However, it should be expecting downward pressure on inflation exerted by oil prices as well as problems in the oil sector, oil-exporting countries and with riskier bonds based on oil prices.

The statements by Fed members are evidence of the fact the central bank is harbouring more and more concerns about share prices rising ever further and declining credit spreads. In this scenario, it will not be long before the onset of bubble formation is evident. This is why we expect the Fed to initiate another rate hike of 0.25 percentage points this year, but probably not until December. The central bank might announce in September it will start downscaling its bond portfolio, but this would not have too many consequences initially, as it would remain restricted to relatively very limited amounts for the time being.

This also means that we see US (and European) long-term interest rates gradually coming under upward pressure and that a ten-year US interest rate of 3.25% in the middle of next year would not surprise us.

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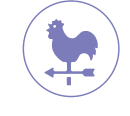

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