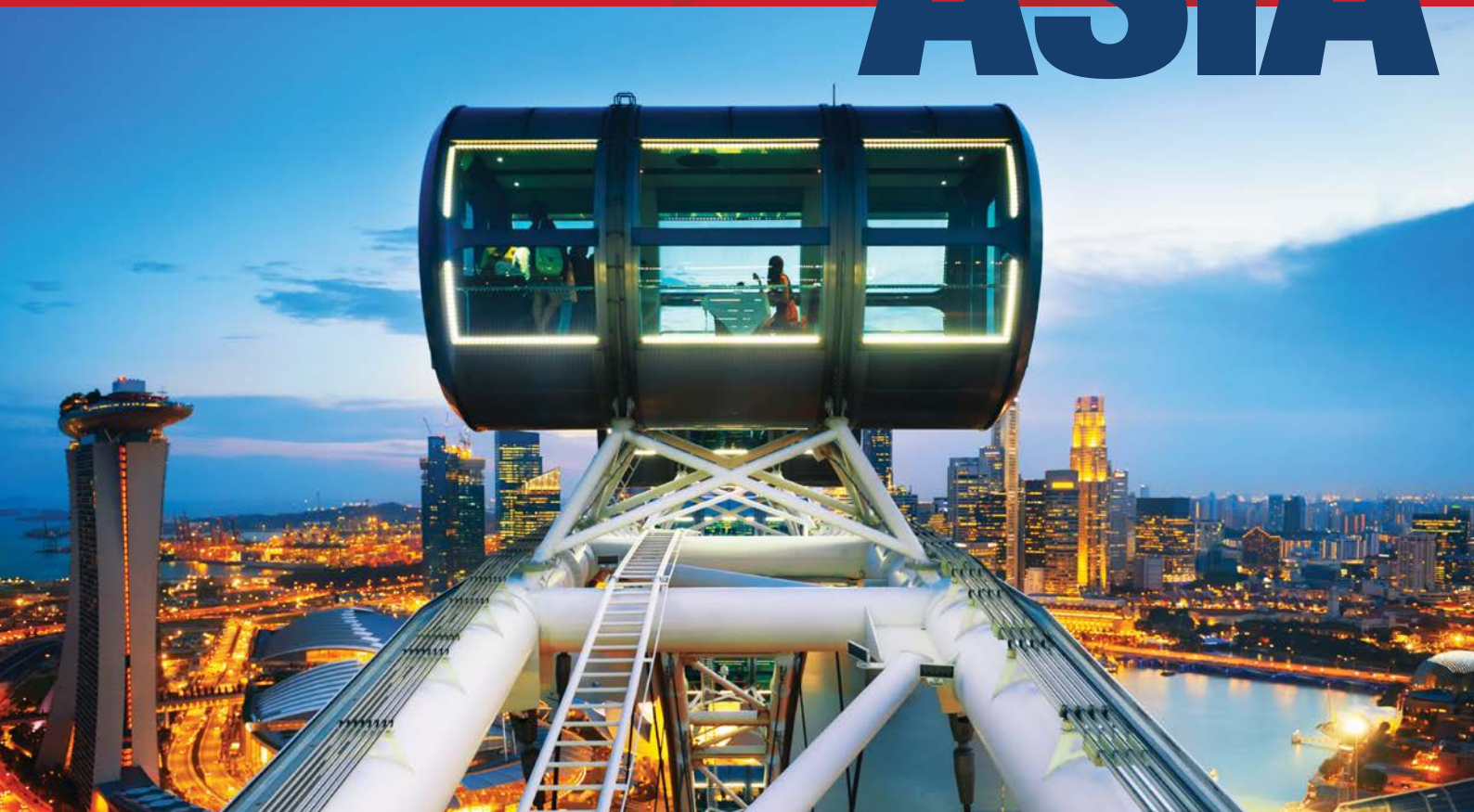


May 2013

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# ASIA



## Singapore: moving on up

Described as one of the four Asian tigers, Singapore is regularly showered with international accolades praising its open economy, efficiency and simple tax and regulatory environment. As emerging neighbouring economies develop, the city state is now reinventing itself yet again.



### Women in Treasury

Cindy Lee

Regional Head, Treasury Asia Pacific  
BASF

### Regional treasury centres

Are Asian MNCs stepping up?

### Tax and treasury

Taxing times ahead



### The Corporate View

Mikko Sopanen

Director of Treasury  
Lite-On Mobile

### Investing in the future

Sustainable and ethical options

### Back to basics

Short-term investment

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Volume 01 / Issue 3

May 2013

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**Annual Subscription Rate** £285

subscriberservices@treasurytoday.com

© Treasury Today ISSN 1759-8311

Treasury Today Asia is published bi-monthly

(6 issues) by Treasury Today Limited

Courtyard Offices • Harnet Street

Sandwich • CT13 9ES • UK

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

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

Periodicals postage paid at Jamaica NY 11431.

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

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

Air Business Ltd is acting as our mailing agent.



# Welcome to the third edition of Treasury Today Asia

Singapore is our Country Focus in this month's edition. Singapore has experienced a meteoric rise following its independence from Malaysia in the mid-1960s. The following five decades can be characterised by a steady growth and influx of foreign talent and investment as Singapore has swelled to become one of the world's most developed countries. As the government pushes for a curb in foreign workforce growth and an increase in productivity, we bring you the latest insight on Singapore's future and what that means for treasurers in the region.

Singapore is the region's most popular location for establishing a regional treasury centre (RTC). In this issue we analyse the trends surrounding Asian multinationals increasingly beginning to establish RTCs. Although historically lagging behind their Western contemporaries, is the tide beginning to turn?

Nominations for this year's Adam Smith Awards have now closed. We were delighted and overwhelmed by the quantity and calibre of nominations for our new category of Asia Pacific Regional Award for Best Practice. We look forward to celebrating the successes of all our winners in June at the Adam Smith Awards Lunch in London and we would like to thank all those who submitted. The complete list of winning corporates is available to view online; [treasurytoday.com/adamsmith](http://treasurytoday.com/adamsmith)

## To receive your copy

Treasury Today Asia is a bi-monthly magazine by the publishers of Treasury Today. The magazine reflects the trends, challenges and opportunities for treasury/finance professionals in the Asia Pacific region.

If you are a corporate based in Asia Pacific, you can register at [treasurytodayasia.com](http://treasurytodayasia.com) to receive:

- The authoritative voice on treasury and finance in the Asia Pacific region.
- Six issues per year of clear and thorough well researched information.
- Independent analysis of treasury topics specific to your region.



## Investing in the future

Although not on the treasurer's radar in every company, sustainable and ethical options are starting to become part of a corporate's investment strategy. But a reticence to engage in the discussion still exists, mainly due to the perception that there is an implicit trade-off with yield.

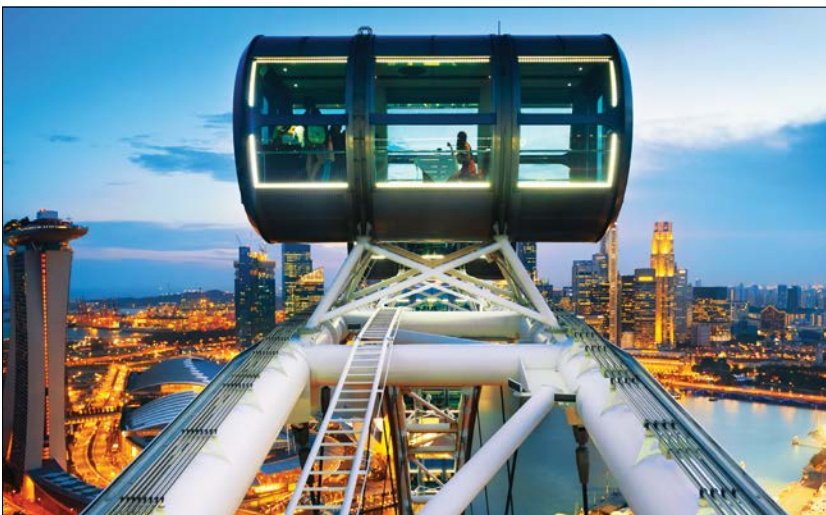


### Cindy Lee

Regional Head, Treasury  
Asia Pacific



Cindy Lee's career-defining moment was when she built the company's cash management platform in Singapore – running across 15 countries – and took on the cash management duties of nearly 35 companies. The treasury platform now supports 52 companies across 18 countries.



## Singapore – staying on top

The Singapore government is in the process of restructuring its economy again, this time to ensure growth is anchored in productivity and innovation in the medium to long term. It is moving towards a productivity-driven growth model, settling for lower growth but higher quality.



## TREASURY TRENDS

20

### Taxing times

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



## ASIA PRACTICE

23

### Leap of faith: are Asian multinationals ready for RTCs?

Many Asian corporates are mature enough that they are seriously considering setting up regional treasury centres (RTCs), if they haven't done so already. Singapore and Hong Kong remain the top locations for RTCs, but up-and-coming Shanghai is proving to be a contender.



## TREASURY ESSENTIALS

Treasury Insights	4
Women in Treasury Study	9
Question Answered	11
Back to Basics	32
Calculator Corner	35



## 26 The Corporate View

**Mikko Sopenen**  
Director of Treasury



Based in Singapore, Mikko Sopenen is leading a project in order to consolidate and centralise the cash flows, for importing and exporting, from all companies to the Asian headquarters. He refers to having had three "cash planets" within China, as each cross-border transaction and cash transfer is so restricted.

## CAPITAL MARKETS

29

### Debt capital markets in Indonesia: one to watch

Indonesia is seeing increased activity in the bond markets because the coupon rates on bonds have fallen, making it a cheaper source of funding than bank lending, both in the domestic and international bond markets. However, the country needs to look more closely at its stance on Islamic finance.





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

## Boosting corporate governance in Asia

Development finance institutes from around the world, together with the Asian Development Bank (ADB), are seeking to increase collaboration and raise the bar on better enforcement of corporate governance rules, practices and procedures in Asia. The ADB hosted the seventh Development Finance Institutions (DFIs) Corporate Governance Group Meeting in Manila in February, to review the progress made in implementing the Corporate Governance Development Framework (CGDF) by its signatories.

At the meeting, the Inter-American Development Bank (IADB) and the Brazilian Development Bank (BDB) became the latest signatories, joining 29 other DFIs from various countries/regions who signed the framework in 2011. According to Enzo Gregori, Senior Investment Specialist, ADB, the group is now starting to look at other stakeholders such as regulators, governments, regional and local institutes of company directors, as well as co-financiers.

### Why is corporate governance important and how difficult is it in Asia?

Gregori highlights the different types of companies in Asia – state-owned enterprises and privately held or family-owned entities which have different corporate governance priorities and are at different stages of maturity. The same applies across the developing world and the signatory group uses the annual meeting to investigate and share best practices and case studies to better understand how to help these companies develop their corporate governance credentials. As part of its normal due diligence process, before the ADB invests in a company, it will look at various aspects including an assessment of its corporate governance maturity. “We see if there are any significant risk implications that need to be remedied before we will invest or that may result in us not proceeding with the investment.”

He says from a company’s perspective, improved corporate governance opens up its commercial credibility in the international markets and in their local domestic markets when they seek to raise capital.

“Also, good governance goes a significant way towards the company’s long-term sustainability and viability. Obviously for long-term investors and lenders, these things are of critical importance.”

If corporates want to attract good partners, seek funds or hire the best employees, they have to develop a good corporate governance reputation, he says. “Ultimately, you are not only reducing risk but also adding value to the company, if you can demonstrate you have good corporate governance.”

On whether the European slowdown has affected Asia, he says, “companies may be enticed to buy goods and services from Asia because they perceive them to be cheaper, but they do not want to sacrifice quality. Reputational risk is a fundamental consideration before outsourcing or procuring goods.

“Good corporate governance in Asia or anywhere else in the world is a fundamental part of commercial and reputational security – the more of your business that is outsourced or reliant upon relationships, the more you want the credentials of your partners and stakeholders to be something you feel comfortable with.”

Corporate governance principles are universal but different business cultures, levels of development, historical constructs and modes of ownership require the application of those universal principals to be localised.

“Furthermore the perspective of a long-term shareholder, a short-term shareholder or a DFI may be different, which creates varied nuances and areas of focus in the corporate governance principles. In this way, principles are different from rules,” says Gregori. “Then you translate those principles in the reality of the environment that you are working with and your own institutions’ principal interest.”

He points out two sides to good governance – it is both a risk mitigant exercise and a value-add exercise.

He cited the example of pension funds typically looking for steady, long-term revenue streams to match their pension liabilities rather than opportunistic short-term gains. “When performing their corporate governance review, they will follow all the same principles but will have a preference, or lean towards components of corporate governance that ensures long-term sustainable viability.”

By contrast, a private equity firm looking to buy an asset and rearrange its strategy, management and financial structure in three to five years and then float it in the stock exchange, may well focus on the corporate governance issues associated with stock exchange regulations.

“In some cases, the local regulatory environment in which the company operates is the driver for corporate governance improvement, while in other cases the driver may be a desire to access international capital. Sometimes individual family members who own the company look to establish it on a best practice footing, as part of a succession strategy,” explains Gregori.

He concedes that some companies and countries alike have very limited capacity and appetite in developing their corporate governance frameworks and unfortunately this is the reality in the developing world.

However, corporate governance is a process of continuous improvement and not an end game in itself. ADB promotes the idea that good corporate governance is fundamental, in the same way that good environmental considerations is.

By working together with the other 30 DFI signatories to the CGDF, the ADB hopes to better promote good corporate governance principles and practices both in the companies it invests in and lends to, and also in the regulatory and governance environment that surrounds them.

## Treasurers: more pay, bigger bonus, new job

The 2013 treasury pay survey from Robert Walters shows most treasurers feel they are due a pay rise and a bonus, and most are thinking about a new job to further enhance their pay and prospects. By studying the average salary figures and expectations for a variety of treasury roles recruited between January 2012 and January 2013, the survey reveals that more than eight out of ten treasurers believe they will receive a pay rise this year, just over a quarter more than last year. The survey acknowledged that senior treasury positions were available, the most notable demand was at middle management level. A focus by companies in the first-half of 2012 on hiring junior professionals has created a “bottom-heavy” treasury environment which must now be addressed.

### The right skills for the right job

Of the companies that are recruiting permanent treasury staff, the report observes that employers have “increasingly attempted to hire for roles with an excessively wide remit with too many responsibilities”. This led to decreased interest in the position “thereby creating a smaller potential talent pool for employers to choose from”. Ridley acknowledges that it is natural for a company to try to achieve “as much bang for its buck” as possible from that role. He feels that some companies may be tempted to exploit the fact that it is a tough market, believing that they are right to expect a lot from candidates. He warns that if expectations are unrealistic there may be too few suitable candidates to choose from.

### How much are treasurers earning?

With many treasury professionals choosing to remain in situ, the reduced number of permanent jobs on the market in 2012 meant greater competition for the vacancies that did arise at all levels. Obeying the rules of supply and demand, this meant actual salaries either remained constant or even dropped slightly.

In the commercial and industrial sector, a FTSE 100 group treasurer typically added another £10k to 2012's basic £130k, but the same role in a FTSE 250 company remained unchanged at £120k. The position of treasurer at both 100 and 250 firms remained static at £85k and £80k respectively. In general, whilst an experienced (4+ years) treasury manager added £5k to last year's basic of £70k, an experienced (5+ years) treasury accountants/controllers dropped £5k from 2012's basic of £80k. Treasury analyst pay remained static at all levels, ranging from £35k for one to two years' experience, up to £55k for 5+ years' experience.

With the pegging of pay rates over the past few years, the overwhelming expectation of a pay increase for 2013 amongst treasurers has risen and is in fact significantly higher than in any other group of professionals surveyed – with compliance (69%), accounting and finance (62%), tax (60%), marketing (61%), HR (54%) and investment banking operations (51%) all lagging. More than two-thirds (35%) of treasurers are expecting a rise equating to more than 7% of their salaries, with 46% expecting it to be between 1% and 6%.

### A treasury bonus

In 2012, 58% of treasurers received a bonus pay-out. One year on and 77% of the profession is expecting a bonus payment. The expectation of a bonus in 2013 is slightly more muted amongst other professions, with 49% of accounting and finance professionals, 46% of HR, 45% of legal, 60% of tax and 61% of marketing roles anticipating the extra payment.

“People are tired of negativity and now they are hoping things will start to turn around,” comments Ridley. “When they do turn, treasurers will expect big bonuses and pay rises.” He believes that the situation will improve throughout the year and will continue to improve. “As it does, bonuses and pay will reflect that.”

Furthermore, says Ridley, the report reveals that more treasury professionals are now starting to explore new opportunities, “having sat tight in their existing roles for a sustained period”. Indeed, despite the relative optimism of treasury personnel in terms of increased pay and bonuses for this year, more than three-quarters (77%) said they are now considering a change in jobs.

### Career progression

Based on these figures, Ridley assesses the overall mood in the treasury employment space as being one of frustration, largely brought about because the market is not able to develop as quickly as many would like. He notes that treasury professionals are not perhaps getting the interesting projects because businesses are understandably more risk-averse. It may also be that treasurers have stayed in jobs because they have not felt confident in how the market is and now they feel more confident.

However, whilst 23% of treasurers cited more pay as their primary reason for changing jobs, 42% placed career progression as their main motivation. Understanding this may force companies to consider if they are developing their staff in the best way. ■

Longer versions of these articles are available at [treasurytoday.com/treasury-insights](http://treasurytoday.com/treasury-insights)

# This much I know

Cindy Lee

Regional Head, Treasury Asia Pacific



## What is your career-defining moment?

It was when I built our cash management platform in Singapore, running across 15 countries and took on the cash management duties of nearly 35 companies. I had to hire, teach, build and talk to the authorities and local companies, basically from scratch. The treasury platform now supports 52 companies across 18 countries.

## Which women in business most inspire you and why?

All my bosses inspire me. But amongst them, I had two very inspiring female bosses. The first was Odine Hanley-Steemers, who introduced me to treasury, and then Gabriele Spies from Germany took over the same role. These two women taught me everything that I needed to know, especially how to be a leader.

## What is the biggest challenge you are facing right now?

Every day is a challenge. Each day I am racing against the clock because I have to juggle three different major functions which I oversee. There are many new things in the business world. The good thing is that I love challenges. When I look at changes occurring in the treasury world, particularly in China, India and Indonesia, I am amazed.

## What couldn't you manage without?

I definitely cannot manage without my team members. They are the backbone of the whole department. Their hard work contributes greatly to my success. I also have to say that I can't manage without my BlackBerry – although it is a love-hate relationship. I love it for the convenience. If I am on the road, which I am a lot because my teams are in three different locations, it allows me to stay in touch with the office. But the hate side is that because of the convenience, I have to be very disciplined when it comes to personal holidays. I try hard not look at it but that usually proves to be quite difficult.

## What advice would you give to other women in treasury?

Stay updated with the changes in the financial world, be very focused and always challenge the status quo. Also always build up a network, especially within the treasury community, because you can learn a lot from your peers.

## What would you have done differently if you could?

To be honest, nothing. The journey has not always been easy, especially when I had to learn everything from scratch without the theoretical background, but I wouldn't change anything.

“I definitely cannot manage without my team members. They are the backbone of the whole department. Their hard work contributes greatly to my success.”

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### ON THE WEB

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To read all the interviews in this series go to [treasurytoday.com/women-in-treasury](http://treasurytoday.com/women-in-treasury)





When Cindy Lee first started in treasury, she didn't know much about the profession. Unlike the accountancy or finance sector, she hadn't heard of treasury before. She has come a long way and is a proponent of the fact that treasury is a crucial department for most companies, not least BASF. Although Lee started in the industry as a total novice, she now heads up BASF's treasury operations in Asia Pacific.

Lee joined BASF South East Asia Pte Ltd in 1996 as part of the regional controlling and reporting team for BASF Southeast Asia, based in Singapore. She entered the treasury world in 2001 as an analyst in the regional finance and treasury centre. BASF picked Singapore because the government offered a number of incentives for companies to start finance and treasury centres there.

"My initial year at BASF was mainly learning on the job," explains Lee. She had a degree in corporate communications from the University of London and when she first started the job, it was a bit of a struggle. "To be honest, I had second thoughts."

However, she had great mentors and bosses, who were very supportive as she learnt the ropes in treasury. Her first treasury boss, Odine Hanley-Steemers from New Zealand and her subsequent replacement, Gabriele Spies from Germany, were both an inspiration to her. "I have to thank Odine for putting me here," she says. BASF gave her access to training and workshops, and was also quite forgiving when she made mistakes.

In addition to learning on the job and working full-time, she also did her Masters in Corporate Finance with the City University of New York, as a long-distance student. "So while I was learning on the job, I was also learning the theory side," she explains.

Lee gradually moved up the ladder from an analyst to assistant manager, and in 2005 was made Manager of the Treasury Cash Management Platform in the Regional Finance and Treasury Centre in Singapore. Two years later, she became the Regional Manager for the platform and in 2010 was promoted to her current post as Regional Head, Treasury Asia Pacific in Hong Kong.

Her role has also widened well beyond cash management. Lee now leads Treasury Asia Pacific which consists of three different divisions – credit management, corporate finance and the cash management platform, which serves as a professional platform for front office duties of all the local companies in Asia Pacific. The three divisions are based in different cities – Singapore, Hong Kong and Shanghai for strategic reasons.

When Lee built BASF's cash management platform, she had to do everything from scratch, as well as build her knowledge on the many regulations in the different countries she manages.

"This is how treasury has evolved within BASF in Asia Pacific and shows how important it has become within the company," she explains.

She loves her job and is constantly facing challenges, racing against time, deadlines and various projects. "I love every challenge that comes along." She believes in always challenging the status quo and instead of waiting for regulators to list the rules, she believes in engaging with them. "The central banks always want to hear from treasurers, especially from developing countries," she says.

Her current role in BASF requires her to travel constantly to her three divisions, although she is technically based in Hong Kong.

How does Lee cope with all the travelling that is required of her job? There are times, in the middle of the night, when she wakes up, and has to ask herself which city she is in. "But somehow I can cope, especially since I have a supportive husband and son."

Lee will be moving back home to Singapore in June for strategic business reasons. "There will be lots of focus on credit management targeting to deep dive into understanding customers' behaviour, mitigation of risk on high risk portfolios and also further improving cash flows. Credit management sits in Singapore where our Asia Pacific Trading Centre is set up and has the highest transactional volumes."

Despite her travelling, Lee has managed to build and maintain a network within the treasury community, both in Hong Kong and Singapore, as she believes strongly in "learning from peers".

"I meet up with peer groups on a regular basis, in order to exchange ideas, see how things are being done, how central banks are dealing with certain issues and what other companies are doing."

In addition to her networking with peers, Lee also meets up with BASF's banks on a weekly basis to "hear their ideas and how their products are being developed to tackle market changes". ■



Cindy Lee is the Regional Head, Treasury Asia Pacific for BASF, a global chemical company with a production network covering 100 sites in Asia Pacific with more than 16,000 employees in the region.

Lee heads up three different divisions – credit management, finance and treasury platform, as well as a service centre for all the local companies in Asia Pacific.

She joined the regional controlling and reporting team in BASF Southeast Asia in Singapore in 1996 where she moved up the ladder and progressed to her current position in 2010.

Born in Singapore, Lee is married and has one son.

# The female perspective

*As part of our groundbreaking new Women in Treasury initiative, we are launching a major study of women working within the treasury profession. The objective of this annual study is to build up a picture of the profiles and careers of women at different levels across the treasury profession from junior positions to Group Treasurer/Financial Director/CFO positions. We believe that the findings may surprise us all.*

## Women in Treasury 2013 Study

Despite improvements, treasury and finance remain predominantly a man's world. Nowhere is this more apparent than at industry events, where women certainly do not make up half of the delegates and, more tellingly, where astonishingly few make it onto the speaker platforms. This gender bias is perpetuated as a result of individuals recruiting staff in their own image.

In order to change the status quo, it is important to understand the challenges that women may face when working in treasury. The first step in changing anything is to recognise openly and clearly that a problem exists. Once we have done this we need to assess how deep the problem is and what the potential causes of it may be. For this reason, Treasury Today is inviting female treasurers to participate in an annual study to help chart the profession's path to diversity.

A targeted study will help corporates examine how they build and maintain a best-in-class treasury function, believes Carole Berndt, Head of GTS for Europe and EMEA at Bank of America Merrill Lynch. "It also provides an opportunity to use the results as a tool to engage and to promote change. Insight gleaned from surveys can feed into employee development programmes and be applied to create best practice processes at a company."

In addition to gauging female treasurers' reaction to the hotly debated quota question, the survey will address a number of areas that are potential hurdles to successful careers for professional women across most industries, including:

- Work-life balance.
- Pay parity.
- Mentoring/networking.
- Career progression.

### Work-life balance

There is no doubt that the prevalent long hours and 'always on' culture in treasury make it harder for women who are juggling childcare with careers. The societal norm dictates that a woman has greater responsibility for the household and children and it is hard to believe that there can be any mothers for whom this has never been an issue, although some may claim so. In fact, part of the whole problem around the work-life balance question for women may relate to their inability to openly declare that there is a problem, preferring to struggle on than to admit that things can be a challenge.

The Managing Director and new Head of Transaction Services EMEA at J.P. Morgan, Sue Dean, links this issue to a well-worn myth of 'having it all'. "I think we beat ourselves up unnecessarily, thanks in part to the old school 'having it all' myth, which suggests that a truly successful woman has a fantastic career, great relationships, perfect children, a sharp wardrobe and a tidy, stylish house. No one has it all, for it is all a balance – and you drive your own balance by the choices you make."

It is a growing trend that more and more companies are beginning to adopt flexible working hours. Berndt makes the point that cash management has become an increasingly global arena with companies expanding across borders and time zones. "Today, I would argue that you can be as effective in your role working remotely at 9pm as you are working from the office at 9am."

This, as we are all aware, has changed the way in which we work and granted a freedom and life flexibility that no previous working generation has enjoyed.



## Pay parity

"The playing field is not yet equal for women, and women are evaluated differently than men. The fact is women have to negotiate things for themselves that their male colleagues take for granted," according to a University of Exeter (UE) report entitled 'Gender diversity in the financial services sector' (January 2013). The report cited a 2003 study of business students which found that 85% of men felt that it was up to them to make sure their company paid them what they were worth, whereas 83% of women assumed their worth would be determined by what their company paid them.

A Swiss-based female Treasurer raises an interrelated issue called the 'Tiara Syndrome', a term coined by Carol Frohlinger to explain the belief that by keeping your head down and delivering excellent work, people will notice – and eventually place a tiara on your head. She argues that women need to make a conscious effort to raise their profiles internally and externally, such as vocally participating in conferences, team meetings and networking events.

## Mentoring/networking

Many women in the financial services sector cite a lack of role models and mentors in the industry as one of the barriers to their own career progression, according to the UE report. It is a fact that is becoming increasingly noted, that whilst men are great at supporting one another professionally, at all levels of their career, women have been quite woefully poor at this key networking and mentoring. This has resulted in a female workforce that, although incredibly capable, are bad at self-promoting and are something of an invisible power in companies. Key mentors throughout a career are vitally important and this mentor need not be of the same gender to oneself. Dean agrees that senior level sponsorship is key to success. "We all need people who understand our potential and will advocate for us. They can be male or female – it doesn't matter. Building your network and developing advocates in this way is critical."

## Career progression

According to the UE report, a recent phenomenon is the opt-out revolution: women choosing to leave the workplace, often in their thirties or forties, when they are just beginning to achieve success. There are frequent comments that women simply are not driven by the same goals and motivations as men, but that is a simplistic answer to complex issues.

It is true that some companies think twice about hiring or promoting younger women because of the possibility that they will take a 'career break' to have a family. Companies are obviously unable to be frank about such choices and it is near impossible to prove, particularly for smaller companies, yet this has got to be something that comes into play because of the financial implications that it poses. How do we get around what appears to be quite a sticking point?

## Differing experiences

Not all professional women face the same obstacles or have similar experiences. The most noticeable differences can be seen between regions. In addition, it will be interesting to see if there is a marked distinction in responses from women under the age of 40 (versus those over 40), which is indicative of the developing career potential of treasury. Ten years ago there wasn't a career path into the profession. Instead many entered into it by chance, maybe as an accountant or controller. However, today there is specific treasury training and many are making a conscious choice, it will be interesting to see if the results reflect this hypothesis.

The results of the Treasury Today Women in Treasury Study will be published in an editorial feature in the October edition of Treasury Today. The results will be presented during a webinar and will be available on the Women in Treasury section of the website. To participate in the study, please visit:

[treasurytoday.com/women-in-treasury](http://treasurytoday.com/women-in-treasury)

# Mitigating trade finance risk

“ How can corporates in Asia mitigate trade finance risk? ”

## Anande Pande, Global Head of Trade, Royal Bank of Scotland (RBS):



Global trade is slowing as a result of the renewed uncertainty we are seeing in both Europe and the US. The latest study from the World Trade Organisation (WTO), published in April 2013, put world trade growth at 2% in 2012 and forecasts 3% growth for this year.

This downtrend will amplify trade finance risk for corporates in Asia in two respects. Firstly, the probability of customers declining shipment in certain industries may increase – something we saw a lot of during the last financial crisis. Secondly, trade flows are shifting, with more trade now taking place within Asia and more in the new corridors opening in the Middle East, Africa and the CIS nations. But while these corridors provide the corporate in Asia with a counterbalance for sluggish demand in Europe and the US, they also bring new problems.

What can a corporate do to mitigate the new risks it will inevitably face when moving into new markets? The first port of call is the credit control department. Start with the basics and evaluate the financial robustness and delivery capabilities of your buyers and suppliers. You may also want to diversify, as far as possible, the locations in which you trade. As we saw in recent years when natural calamities caused the collapse of whole supply chains in Japan and Thailand, buying from one country in order to minimise costs is a strategy which could come back to bite you.

The strength of your legal documentation is another important consideration. If you are selling to an overseas market, you must be aware of the laws of that particular country and whether a potential claim will be enforceable. So the risk function is not only mitigating the risk on the balance sheet. A company needs a very strong risk management focus that takes into account the various non-financial risks that also come with trading.

Letters of credit (LCs), like all paper documentation, are liable to occasional errors that could give the importer the right to refuse payment. To avoid this scenario, find out what your banks are offering in terms of outsourcing solutions in which they prepare the export documents on your behalf to ensure they are not discrepant. Explore electronic trade solutions whenever possible as this reduces documentation error and increases administration efficiency.

With open account as the dominant force in Asian markets, corporates may also want to consider insurance companies that provide risk mitigation for a pool of buyers. The Bank Payment Obligation (BPO) could also help. As a risk mitigant for open account transactions – although still a work in progress – it will help corporates, not only to manage risk on open account transactions, but also increase their trade volumes across the world.

## Steven Beck, Head of Trade Finance Programme, Asian Development Bank (ADB):



Corporates must not be deterred from exporting to challenging markets because of payment risks. That may sound like an imprudent thing to say, but the fact is there are ways of shifting these risks off corporates' books.

LCs and other trade finance instruments have been in existence for hundreds of years. They work well to mitigate risk. Financial institutions can 'confirm' (guarantee) trade finance instruments such as LCs, thereby removing the emerging market payment risk. To enhance commercial banks' ability to assume emerging market payment risk on behalf of corporates, the ADB established the Trade Finance Programme (TFP), which works with commercial banks to support trade in the most challenging markets.

TFP diminishes commercial bank trade finance risk. In 2012 TFP supported \$4 billion in trade in the most challenging markets. Of TFP's 18 markets, its five most active markets were Vietnam, Pakistan, Bangladesh, Sri Lanka and Uzbekistan. TFP is in the process of expanding to Myanmar, where there is huge interest from corporates, and in turn their banks, to cover payment risk associated with sales to this frontier market.

In addition to working with commercial banks to reduce payment risk, corporates can also look to insurance, covering payment risk either on buyers – in some cases this is not possible – or from a buyer's bank under trade finance instruments such as LCs.

There are ways for corporates to mitigate payment risks in frontier markets. ADB, among other multilateral development banks, is playing its part to bolster financial institutions' capacity to support corporate sales in tough markets. Corporates should be encouraged to expand into frontier markets knowing that associated risks can be managed, regardless of how challenging the market may seem.

## Simon Constantinides, Regional Head of Global Trade and Receivables Finance, Asia Pacific, HSBC:



A tectonic shift in global trade patterns is underway, forcing many exporters to seek new opportunities, but alongside those opportunities come new – or at least unfamiliar – risks. As businesses switch their focus from the moribund markets of Europe and North America to the vibrant – but more volatile – environment of the emerging economies, they are being squeezed between falling incomes and the rising cost of covering their exposure. It has never been more important to keep the costs of risk mitigation under control. There are two main areas of increased risk: new and untested customers and unpredictable currencies.

Trade finance insurance can be a key element of a broader risk mitigation strategy, but the most effective and cost-efficient way of cutting the danger of default from a customer is to work with a trusted partner which has extensive network and experience on the ground to bridge the gap between markets. Intimate knowledge of the local corporate landscape can give an inside track on potential problems before they become critical and frequently leads to lower costs for credit guarantees.

Currency risks can be less easy – and therefore more expensive – to hedge, but certain effective strategies are emerging, particularly in Asia. Loose monetary policies in the West have led to excess cash flowing in and out of emerging markets, in response to fluctuations in the capital risk/return equation. For a trader operating in such a volatile environment, an unlucky currency call can make the difference between success and failure.

Full hedging can be expensive, but certain trends are becoming apparent in emerging Asia. Professor Takatoshi Ito of the University of Tokyo calculated that after controlling for the G3 currencies (US dollar, Japanese yen and the euro), RMB accounts for between 40% and 49% of the fluctuation in the Singapore dollar, the Indonesian rupiah and the Malaysian ringgit, and between 30% and 39% for the Indian rupee, Thai baht, and Taiwan new dollar. After more than half a century as a closed book, the RMB is now establishing itself as a global currency, and the creation of a broad range of hedging instruments is part of that process. It is clear that as exporters explore new markets, they are being exposed to new risks, but with the right partner and the right strategy they can be cost-effectively minimised.

## Sridhar Kanthadai, Regional Head of Transaction Banking, North Asia, Standard Chartered:



As growth in trade continues to shift from West to East, an increasing number of Asian corporates are expanding beyond their borders. This means they have to operate in new markets with new suppliers under different local regulations. Financial and economic challenges of the past five years have refocused companies' concerns around counterparty, cross-border liquidity and bank risks. Impact of evolving regulatory requirements such as Basel III is also prompting companies to take a much closer look at how they manage their risk exposures.

Therefore it is critical that Asian corporates find efficient ways of managing risk and cost associated with trade transactions. Here are a few options for Asian corporates' consideration.

Firstly, it is important to choose the right option for your needs. Starting from the LC to pre-payment, the gamut of options available for companies is staggering. Domestic trade typically uses variants that are established in the particular market. While historically cross-border trade has relied on the documentary origins such as LC, there is an increasing acceptance of open account trade. For those who still prefer the payment certainty of an LC but want the efficiency of open account trade, the Bank Payment Obligation (BPO) is a new solution that is the best of both worlds.

Secondly, complex supply chains using procurement hubs and re-invoicing centres have resulted in significant value flows for many industries, a big portion of which is inter-company. The regulatory and capital overheads that banks now face and, the potential reduction in financing for less creditworthy names, have also driven needs of companies to manage and support supply chains while managing the risks. Corporates need to look for an experienced financial partner that is able to support these needs, whether it be through receivables financing to reduce credit exposure and improve their days sales outstanding (DSO) and working capital measures; buyer financing to accelerate their receivables and release buyer credit; or vendor financing to extend payment terms and in turn improve working capital.

Thirdly, trade credit insurance is a good risk management tool for Asian corporates to consider in order to mitigate the risks of open account trade. The insurance would help de-risk their business growth while supporting an increasing volume of financing transactions. ■

### The next question:

“Where is the best place in Asia to set up a regional treasury centre and why?”

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





# Investing in the future

*Sustainable and ethical investment instruments are not experiencing high demand from corporate treasurers, mainly due to a perceived trade-off between sustainability considerations and aspects that treasurers care most about: capital preservation, liquidity and yield.*

In the 1700s, pharmacy group Alliance Boots took its social commitments seriously by providing cheap medicines for poor people. In 2013, the same social and ethical values are part of the company's DNA. "Corporate social responsibility (CSR) is so much easier if the values are incorporated into what people do," explains Richard Ellis, Director of CSR at Alliance Boots. "So whether you are a treasurer or a beautician working for Alliance Boots, we say incorporate these values into the way you do your job."

That may be easy for Ellis to say. After all, CSR is his sole remit and he works for a company with a strong ethical brand. But how and where does a corporate treasurer fit into all of this, if at all? Does environmental, social and governance (ESG) have any applicability to what they do? Even if they work for a company where ESG and CSR are core to its brand, how can a treasurer, who is typically focused on cash preservation and liquidity, incorporate

sustainability and ethical considerations into their investment decisions?

Sustainable and ethical investments typically entail applying negative or positive screens to evaluate particular factors (tobacco, alcohol, weapons, etc), direct investments in renewables or carbon credits, investing in funds which contain issuers that are screened against ESG benchmarks, or ethical investments such as Islamic finance.

A number of EU corporate pension funds already integrate ESG into investment decisions, according to the European Sustainable Investment Forum (Eurosif). Eurosif's 2011 Corporate Pension Funds and Sustainable Investment Study found that 56% of surveyed corporate pension funds had a Socially Responsible Investment (SRI) policy in place, 60% consider that ESG factors affect a pension fund's long-term performance and 66% indicated that having an SRI policy is part of their fiduciary duty.

Pension funds, however, are typically long-term investors and are willing to tie their capital up for longer periods. Corporate treasurers, on the other hand, tend to take a more short-term view.

## A short-term investment horizon

“Most corporates are in a net debt position so if they have got cash they tend to invest that in short-term bank deposits or money market funds (MMFs),” says Michael Wallis, Group Treasurer at Marks & Spencer. “That is more about securing cash and maintaining principal, whilst still getting some sort of return.” Royston Da Costa, Group Assistant Treasurer, Treasury Systems and Development, Wolseley Group Services, states that Wolseley’s policy regarding investing surplus cash is quite specific. “We either deposit short term with our relationship banks or use a select number of MMFs, based on their relationship with our banking partners,” he explains.

In Europe, the uncertain economic outlook reinforces the need for treasurers to stay short when they are investing unless they are told otherwise, remarks Olivier Brissaud, former Managing Director of Volkswagen Group Services and Chairman of the Association des Trésoriers d’Entreprises en Belgique (ATEB). “In Europe at least, treasury is about making sure the company has – at any time – enough money to implement its business strategy. That by definition is a conservative investment profile,” remarks Brissaud. “If the treasurer goes outside the traditional constraints provided for treasury and invests in ethical or sustainable investments they might lose money.”

Finding out information about sustainable and ethical investments is also challenging for treasurers. “It is not that easy to find any ratings agencies that rate the ethical behaviour of companies,” says Brissaud. For that reason ethical investments should be done through a company’s CSR team, as they are responsible for (re)building a link between a company and society. François Masquelier, Chairman of the Association des Trésoriers d’Entreprise à Luxembourg (ATEL), says communication about potential ethical and sustainable investments is not great. “That can perhaps explain why ESG is not (yet) an issue for a vast majority of our members,” he says.

Masquelier says treasurers are more focused on counterparty risk and on how to get decent (and if possible, not negative) returns. “The recent financial crisis has focused energies and priorities on other issues,” he says. “Furthermore, even for longer-term investments, I am not convinced that CSR and ethics are top concerns. We should regret this but it is a fact. I’m convinced that things will evolve. Let’s remain optimistic and see – often treasurers are followers.”

## Shareholders versus sustainability

In the case of longer-term investments, Jeff Wallace, Managing Partner at Greenwich Treasury Advisors, says companies with huge hoards of cash may be more likely to apply sustainable and ethical investment criteria. However, long-term corporate excess cash is mostly related to interest rate securities and very little equity, which is where most sustainable and ethical investments are made. When it comes to bond investments, Wallace says treasurers are paid not to lose money. “In fact they could lose their job if a bond investment went bad,” he says.

Sometimes treasurers are involved in investment decisions made by the company pension scheme. Wallis of Marks & Spencer sits on the investment committee of the company’s pension scheme. He is not directly involved in investment decisions but says the committee takes the ESG side of things very seriously. Marks & Spencer’s pension scheme is a signatory to the UN’s Principles for Responsible Investment (PRI).

### “It is not that easy to find any ratings agencies that rate the ethical behaviour of companies.”

Olivier Brissaud, former Managing Director of Volkswagen Group Services and Chairman of the Association des Trésoriers d’Entreprises en Belgique (ATEB)

Although treasurers concede they should perhaps look at other types of high yielding investments, including sustainable and ethical investments, Da Costa says they are still governed and guided by internal policies, which are set by the board, which in turn refers to its shareholders. While some shareholders are focused on short-term returns, others like private equity firms that invest for the longer term are insisting that companies pay closer attention to ESG. New York based private equity firm, KKR, which led a buy-out of Alliance Boots in 2007, believes ESG is essential when it comes to value protection (making sure a company it invests in doesn’t lose money due to any ESG issues), value management (ensuring a company achieves best value) and value creation (integrating ESG into product sustainability to ensure operations run better).

## Smarter investment decisions

Elizabeth Seeger, sustainability lead at KKR, says sustainable and ethical investment pays off in the short term, as well as the long term. In December 2012, KKR announced \$365m in cost savings and revenue from its Green Portfolio Programme of companies by reducing greenhouse gas emissions, waste and use of water. “Environmental efficiency does have an impact on the financial performance of companies and on the bottom line in the short term,” says Seeger. However, she says most people tend to think of ESG as being separate. “Part of the problem is the terminology – ESG, CSR, etc,” she explains. “People fail to realise that just because you are thinking about cash flow doesn’t mean you are not thinking about ESG issues.”

This raises a number of important questions for treasurers. Treasurers manage cash flows, but what about the quality and sustainability of those flows? “We have a tendency to think about economic systems as though participants only need to worry about the micro issues which affect them, and everything else will fix itself,” observes David Pitt-Watson, a Senior Fund Manager and Treasurer at UK charity Oxfam. Although corporate treasurers may think their actions will have very little impact, Pitt-Watson says they should take a step back, look at what they are doing and how it fits with things happening in the rest of the world. What can they do to make sure they are supporting responsible investment? How can they modify their actions whether working on their own or with others?

But does ESG mean sacrificing capital preservation, liquidity and yield – aspects treasurers most care about when making investments? “In the minority of cases, you may have to

sacrifice profitability,” says Pitt-Watson, “but once ESG is integrated into your system it becomes less costly and often profitable. If everyone focuses on sustainability issues, we will all be much better off.”

Keith Welks, Deputy State Treasurer for Pennsylvania, says many asset owners have become accustomed to entreaties for investments that are sustainable but are not good investments from a principal preservation and yield perspective. “As a result, some of them run for the hills if they get a whiff of ESG, even if the opportunity might otherwise still be appropriate for them. I believe you can make these kinds of investments work in many instances. You need to think about the structure that works for you as an investor with multiple objectives and look at opportunities with open eyes.”

Much like a corporate treasury, Pennsylvania State Treasury has a prudent investor obligation, which means it must invest in a manner that preserves principal, maximises liquidity and generates returns or yield. In 2005 a new State Treasurer was appointed in Pennsylvania, and Welks and other members of the treasury team were asked to consider a fourth factor when making investments – an added benefit to the state’s economy, a particular segment of the population or an appropriate public policy objective.

“That is when we started looking at the energy efficiency of residential homes that would cost owners less,” says Welks. Treasury set up an investment scheme for homeowners offering them low-rate loans (11,000 loans worth \$80m) for energy efficiency measures. It recently aggregated a large number of the loans and sold them in the secondary market. The loan portfolio generated a yield of 5%. “It has outperformed fixed income investments,” says Welks, “generating appropriate and acceptable returns with limited risk, which gives us the opportunity to make funding available to 11,000 homes.”

Pennsylvania State Treasury also developed an investment fund where it provides 20% equity for making energy conservation improvements to old college buildings. By focusing on proven technologies and also providing a steady stream of income, Welks says the college fund addresses two of the most common objections to clean energy: it avoids technology risk and provides liquidity much earlier in the investment cycle.

Where it uses external investment managers, treasury also started asking them about their sustainability criteria – employment of women and ethnic minorities, environmental and sustainable practices both by the managers and the investments they review. “We’ve gotten pretty anodyne responses to our inquiries so far,” says Welks. “Right now we’re at the stage of deciding how we apply the information that we have. We still expect a good rate of return from our investments with these managers but we are also looking for double or triple line benefits. As prudent investors we try to figure out what are the attributes we should be looking for in order to make smarter investment decisions that make money for treasury.”

## MMFs with a conscience

Fund provider Amundi in France has made it easier for corporate treasurers to gain investment exposure to ESG without really having to do anything. It applies SRI criteria to

its flagship MMF, Amundi Tresor EONIA ISR, which has €25 billion in assets under management. Amundi’s SRI filter is applied to all issuers in the fund and its team of SRI analysts do all the groundwork in terms of assessing the SRI credentials of issuers.

“We are providing customers with additional analysis, which adds value,” says Patrick Simeon, Head of MMFs at Amundi, adding that most of the French corporate treasurers that invest in its SRI MMF have responded with interest. Assets under management in the Tresor EONIA ISR fund have increased by 25% since 2011. In terms of the fund’s performance, in this asset class Simeon says the main issue is that the investment universe is over weighted towards banking and financial names with an average SRI ranking. “This doesn’t weigh much on the performance of the MMF,” he explains. “It is purely adding transparency. The key element of our approach is security and liquidity. Performance is the cherry on top of the cake.”

Dominique Blanc, Head of SRI Research at Novethic, a leading CSR and SRI research centre in France, says there are significant assets in SRI MMFs in France. According to its research, in 2012 the French SRI market saw growth of 39%, following a growth of 69% in 2011. Although corporate investors are not necessarily asking for SRI, Blanc says they are not saying no to it either. “The financial and risk characteristics of these funds are the same as traditional MMFs, but as a value add they have a sustainability aspect,” he explains. A breakdown of SRI assets by type of owner shows that in 2012 corporates made up 6%, the fifth largest group behind insurers, pension funds and public funds.

## Sustainable bonds

Another asset class that presents corporate treasurers with SRI opportunities are sustainability bonds. Last year, FMO, the Dutch development bank in the Netherlands, issued a \$41.3m six-year sustainability bond for KLM Royal Dutch Airlines. Treasury and Risk Manager, Vijay Panday, made the investment on KLM’s behalf. “KLM is pleased to participate in the sustainable bond issued by FMO,” he stated. “This combines our financial strategy to further reduce our US dollar currency risk and our strategy to be leading the industry regarding sustainability.” KLM is a signatory to the UN Global Impact initiative of 1999. It also occupies the sector leadership position in the Dow Jones Sustainability Index.

“More and more investors are attaching a value to the non-financial aspects but it’s still not mainstream,” remarks Huib-Jan de Ruijter, Director of Financial Markets for FMO. The sustainability bond developed for KLM was the first issued by the development bank, which uses negative screens to exclude certain companies, and also applies environmental and social requirements such as the IFC Performance Standards on Environmental and Social Sustainability to all its financing activities. The cash flow of the bonds are not directly linked to the credit risk of a specific project and FMO has a AAA credit rating. “The bond matched the needs of KLM’s treasury and it can be tailored in terms of tenor and currency,” de Ruijter explains. He says treasurers should look at sustainability bonds in the same way as they look at other investments, but the extra bonus is the non-financial component. “I am not suggesting that they should get more on the non-financial side and give up something on the financial side. They don’t need to make that trade off.” ■



# Singapore – staying on top

*Despite lacking the natural resources of its neighbouring countries Singapore has experienced an astonishingly fast ascent to become one of the most developed countries in the world and a remarkable hub for financial activity. We examine the hows and whys of its rise and the outlook for its future.*

Following its independence from Malaysia in August 1965, Singapore, which was then a third-world nation with poor infrastructure, limited capital and most importantly no natural resources, had to develop a plan to steer its economy.

In a bid to create jobs in the early 1960s, the government set up the Jurong Industrial Estate – the first of many – and the Economic Development Board (EDB) with a \$100m budget to woo foreign investors. These two events marked the start of Singapore's path to industrialisation.

Thirty years later, the EDB shifted its focus from manufacturing to new key industries – chemicals, electronics and engineering, as well as funding growth in biomedical sciences.

The Singaporean government is once again in the process of restructuring its economy, this time to ensure growth is anchored in productivity and innovation in the mid to long term.

The 2013 budget builds on the restructuring measures put in place since 2010, with additional initiatives for businesses to upgrade, create better jobs and raise wages.

For the fourth consecutive year, Singapore has unveiled restrictions on foreign labour, with total workforce growth targeted to ease to 1%-2% annually through 2020, compared with an average 3.3% per annum over the past 30 years.

Foreign labour policies were tightened further through higher foreign worker levies, dependency ratio ceilings and more stringent eligibility requirements for certain passes, with the least productive sectors that rely most heavily on low-skilled foreign workers being hit the hardest.

"The foreign workforce can't keep growing faster than the local workforce, not indefinitely," Singapore's Finance Minister, Tharman Shanmugaratnam, told Bloomberg in March. "That's why our most important economic and social strategy is that of raising productivity to a new level."

Wrapping up the March 2013 budget debate in parliament, Shanmugaratnam warned that economic restructuring will be

painful but it cannot be put off any longer, arguing that Singapore was at a critical point in transition and that the push for a restructure was not just an economic issue but also a key social pillar.

"If we do not achieve momentum in the next three years, there's a real risk that we will be in exactly the same position as today. Both workers and businesses will be worse off," he told parliament.

Elaborating on the budget's two priorities – economic restructuring and society inclusivity – he said that productivity growth has been weak and that 2011's 2.6% decline was "miserable".

Manu Bhaskaran, Founding Director and CEO of Centennial Asia Advisors, says, "Singapore is moving towards a productivity-driven growth model, settling for lower growth but higher quality. This in the sense of the impact on income distribution and opportunities for Singaporeans, as opposed to foreign workers, etc."

He says this entails stricter controls on immigration, especially low-skilled workers and semi-professionals, coupled with several government incentives for businesses to upgrade and move up the value chain.

Citi's Head of Treasury Advisory for Asia Pacific, Gourang Shah, agrees. "Singapore used to be an electronic manufacturing centre but it was forced to move up the value chain. It has to constantly innovate to keep its developed world status and stay one step ahead of the others."

David Blair, Managing Director of Acarate in Singapore and the former Vice President, Treasury of Huawei, notes that the government remains committed to the finance sector, including treasury and is consciously trying to make Singapore more attractive for locating regional treasury centres (RTCs).

"A potential issue that has been covered recently in the press has been that by limiting the number of work permits the country runs the risk of making it harder to get expatriates into the country. However, these constraints are mainly placed on low-end service jobs and Singapore remains committed to high value-add finance jobs."

However, Blair concedes that work permit applications are now taking on average a couple of months to process instead of a few weeks, as in the past.

## Economy

According to a report published in March 2013 by the Monetary Authority of Singapore (MAS), Singapore's real GDP

### Singapore: facts and figures

Land area: 715.8 sq km.  
Total population: 5,312,400.  
Real per capita GDP: \$45,973.  
Labour force: 3,361,800.  
Gross national savings (% of GNI): 46.1.  
Literacy rate: 96.4% (aged 15 and above).

grew by 1.3% in 2012. On a quarterly basis, it grew 1.5% year-on-year in the fourth quarter, after registering zero growth in the third quarter. According to latest estimates by the Ministry of Trade and Industry, GDP in the first quarter of 2013 was a year-on-year contraction of 0.6%. MAS has forecasted a growth of 1%-3% for 2013, supported by domestic-oriented activities and some recovery in the sectors reliant on external demand. Activity is expected to remain modest in the first half, especially in the externally-exposed industries, before picking up in the latter half of the year, in tandem with the strengthening of the global economy.

2012	Q1	Q2	Q3	Q4	Full year
<b>Real sector</b>					
Real GDP growth, year-on-year %	1.5	2.3	0.0	1.5	1.3
Real GDP growth, quarter-on-quarter saar <sup>1</sup> %	7.8	0.1	-4.6	3.3	-
Index of industrial production, year-on-year %	-1.1	4.2	-1.4	-0.4	0.3
Non-oil domestic exports, year-on-year %	6.0	3.7	-3.2	-4.2	0.5
<b>Labour market and prices</b>					
Unemployment rate, sa <sup>2</sup> , % (Average)	2.1	2.0	1.9	1.8	2.0
CPI inflation, year-on-year %	4.9	5.3	4.2	4.0	4.6
Wage growth, year-on-year %	0.9	2.8	3.1	2.5	2.3

Source: Monetary Authority of Singapore

<sup>1</sup>Saar: seasonally adjusted annualised rate. <sup>2</sup>Sa: seasonally adjusted

However, domestic-oriented activities are likely to remain firm, with the construction sector expected to see significant expansion in 2013, in view of a strong pipeline of projects awarded over the past years. This could create positive spillover effects for activities such as bank lending and real estate services.

Structure of economy	Nominal value-added (% Share)	Real growth (%)
<b>Total</b>	100.0	1.3
<b>Goods producing industries</b>	26.8	1.2
Manufacturing	20.7	0.1
Construction	4.4	8.2
Utilities	1.6	3.4
Other goods industries	0.0	1.2
<b>Services producing industries</b>	68.5	1.2
Wholesale and retail trade	17.0	-0.7
Transportation and storage	7.7	2.7
Accommodation and food services	2.5	2.8
Information and communications	3.8	2.6
Finance and insurance	11.9	0.5
Business services	14.6	3.9
Other services industries	11.0	0.1
<b>Ownership of dwellings</b>	4.8	0.7

Source: Ministry of Trade and Industry

Inflation is forecast at 3.5%-4.5%, underpinned by firm accommodation and private road transport costs. However, if these two items are excluded, MAS expects that core inflation will be around 2%-3%.

The government estimates casinos contribute 1.5%-2% of GDP and employ 22,400 people. It has subsequently generated new revenue through taxes on gaming, accounting for 2.2% of total operating revenue, according to the Financial Times.

## Sovereign ratings

Singapore is the only Asian country to have AAA credit ratings from all three major credit rating agencies – Standard & Poor's (S&P), Moody's and Fitch.

In affirming the AAA rating with a stable outlook in March this year, Fitch says the ratings are underpinned by Singapore's strong sovereign balance sheet that serves to insulate the small and open economy from external shocks. Sustained fiscal surpluses have \$259.3 billion – equivalent to 5.4 months of current external payments and 65.2% of broad money supply at the end of 2012.

The sovereign's large current account surplus has been a main driver for sustained accumulation of foreign exchange (FX) reserves. The country is one of the largest net external creditors (in sovereign, bank and non-bank sectors) among AAA peers. Furthermore, its net international investment position reached 276% of GDP in 2011, the highest among AAA sovereigns.

Fitch however notes that although Singapore's ratings are supported by strong economic performance, underpinned by an attractive investment environment, a low tax regime and high quality public institutions, as a small open economy, Singapore's economic growth is more volatile than the AAA range median and is more exposed to global economic cycles.

"Nevertheless, Singapore has demonstrated its capacity to weather economic volatility, helped by its fiscal flexibility," said Fitch.

In its credit rating report last year, Moody's warns that challenges facing the country include containing consumer price and property inflation over the near term, and fostering a growth model that is driven by productivity and innovation over the longer term.

## Double taxation agreements and free trade agreements

Singapore has 69 comprehensive double taxation agreements (DTAs) and seven limited DTAs in force. Limited DTAs are restricted to tax exemption on income derived from international shipping and/or air services.

Singapore's network of free trade agreements (FTAs) covers 18 regional and bilateral FTAs with 24 trading partners. These include the ASEAN Free Trade Area (AFTA), with the US, India, China and Japan, among others.

Blair says what matters for RTCs are tax treaties and reduced withholding taxes, and these often go with FTAs. "Singapore is very strong in this respect. It is better than Hong Kong, which is viewed by many states as a tax pariah and therefore has less tax treaties," he says.

The MAS also has cross-border collateral arrangements (CBCAs) with Bank Negara Malaysia, Bank of Thailand, Bank

of England, Banque de France, Bundesbank, De Nederlandsche Bank and the Federal Reserve Bank.

Prior to these arrangements, MAS accepted only securities issued by AAA rated entities. By broadening the collateral pool to include foreign currency-denominated collateral, MAS now accepts certain kinds of collateral issued by entities with lower credit ratings but it applies larger haircuts.

Bhaskaran says Singapore's multiple trade and economic partnership agreements have improved its competitiveness as a hub for global companies to base themselves to serve Asian growth.

"The gradual progress in ASEAN economic integration through AFTA in the past and soon through the ASEAN Economic Community will help, as will our economic links with Malaysia through the Iskandar region in southern Malaysia, which is being increasingly linked to the Singaporean economy with benefits for both countries."

## Financial sector

Singapore remains ranked fourth best financial centre, together with London, New York and Hong Kong, according to the Global Financial Centres Index 2013 (GFCI) released in March this year. Hong Kong and Singapore are now only two points apart, whereas there is a 48-point difference between London in the top spot and Singapore in the fourth spot.

In the GFCI's list of questions, Singapore drew the most number of mentions as a centre that is likely to become more significant, followed by Shanghai, Hong Kong and Seoul.

In 2012, the finance and insurance sector in Singapore grew by a modest 0.5%, much lower than the 8.9% recorded in 2011, due to weak performance in sentiment sensitive segments such as FX trading and stockbroking, according to Singapore's Ministry of Trade and Industry.

Singapore's FX market saw an average daily turnover of \$337 billion in 2012, largely unchanged from 2011. Trading in major currencies such as the US dollar, euro and Japanese yen continued to dominate the market with the euro/US dollar pair registering the highest trading volume.

In 2012, the derivatives market activity in the Singapore Exchange rose by 11% to 80 million contracts. Total options trading volume rose by 126% and total futures trading volume grew by 7.9% to five million option contracts and 75 million futures contracts respectively from 2011.

In its 2012 Financial Stability Review, published in November last year, MAS says Singapore's economy and financial system have been resilient through the global financial crisis, with growth having slowed significantly. However, it says growth is still expected to be positive in 2013.

"Financial markets have remained stable despite financial fragilities and persistent macroeconomic uncertainties globally. Concerns over liquidity and counterparty credit risks have been muted in the domestic inter-bank market, while confidence in Singapore Government Securities remains high," said the report.

The MAS expects interest rates to continue to remain low, but warns that there is a risk that expectations of low interest rates for the foreseeable future will become entrenched. It cautions that while Singapore dollar funding for domestic

lending remains adequate, non-Singapore dollar funding risk should be closely monitored especially since non-Singapore dollar loan growth has outpaced non-Singapore dollar deposit over the past year. "A sudden spike in global risk aversion could trigger stresses in global US dollar liquidity, with adverse knock-on effects on the Singapore banking system."

The central bank says corporates are more leveraged now than they were a year ago, and although they seem well-positioned to cover their interest expense, this could change if interest rates rise significantly.

Fund raising in other corporate finance markets rose, with large firms issuing twice the amount of debt in the first three quarters of 2012 compared to the previous year.

## Currency interchangeability and RMB clearing

Three countries – Singapore, Malaysia and Brunei – adopted a system of free interchangeability of their respective currencies on 12<sup>th</sup> June 1967. Malaysia bowed out in 1973, but Brunei and Singapore decided to continue with the arrangement which is still in force today.

Under the arrangement, both countries undertake to accept the currency issued by the other and to exchange them at par, without charge, into their own currency.

The MAS says this arrangement can be viewed as a "currency union between two countries characterised by a one-for-one exchange rate of their currencies and a joint (but managed) float against all other currencies."

The central bank says the two currencies serve as a medium of exchange, as direct payment in trade and investment between the two countries, thereby reducing conversion costs. It also eliminates exchange-rate fluctuations.

In April this year, the MAS and the People's Bank of China (PBoC) signed a memorandum of understanding (MOU) on renminbi (RMB) business co-operation.

Under the agreement, MAS and PBoC will co-operate closely in reviewing the conduct of RMB businesses and clearing arrangements in Singapore. The two central banks also agree to establish a regular dialogue to review RMB liquidity conditions and discuss issues concerning the stability of the RMB market.

In addition, the PBoC signed an RMB Clearing Agreement with the Industrial and Commercial Bank of China (ICBC) Singapore branch in February, allowing the branch to provide RMB clearing services to participating banks and their customers for the next five years.

## Payment and settlement systems MEPS+

In order for Singapore to be a key financial hub, according to Ying Siew Ang, Head of Transaction Services in ASEAN, J.P. Morgan, it needed to leverage on operational efficiency and productivity, making sure that all payments are executed seamlessly, and allowing corporates to see payments or receipts almost instantly. Hence it developed MAS Electronic Payment System (MEPS+), which began operating in December 2006 and provides several improved features over its predecessor, MEPS.



MEPS+ offerings includes:

- Use of SWIFT message formats and networks. This allows for greater straight through processing and cost savings by banks.
- Advanced queue management capabilities which help participants to better manage settlement risks.
- Automated collateralised intraday liquidity facilities.
- Automated gridlock detection and resolution.

## CLS

Continuous Linked Settlement System (CLS), a global multicurrency settlement system, went live in September 2002 and initially settled FX transactions in seven major currencies – the Australian dollar, Canadian dollar, euro, yen, pound sterling, Swiss franc and the US dollar. The Singapore dollar was added in 2003, together with the Danish krone, Norwegian krone and Swedish krona. FX trades involving the Singapore dollar and other CLS currencies can now be settled in CLS without exposure to FX settlement risks.

For efficiency, three local banks – DBS Bank, Overseas-Chinese Banking Corp (OCBC) and United Overseas (UOB), who are CLS shareholders – established the Clearing and Payment Services Pte (CAPS), a common clearing utility to process their CLS transactions.

## Singapore ACH

The Singapore Clearing House Association (SCHA) was formed in December 1980, as an association to establish, manage and administer clearing services and facilities for cheques as well as debit and credit items of its members. In addition to MAS, at the end of 2010, it had 46 ordinary members and 51 associate members. The SCHA provides Singapore dollar cheque clearing, US dollar cheque clearing and inter-bank Giro clearing services through the automated clearing house (ACH).

J.P. Morgan's Ang says inter-bank Giro payments comprise 56% of the local ACH, with the remaining 44% in cheques.

## Cheques

Both Singapore dollar denominated cheques and US dollar cheques presented to and drawn on banks in Singapore, are cleared through the Cheque Truncation System (CTS). For US dollar cheques to be cleared in ACH, both the presenting and paying banks must be participants of ACH.

## Inter-bank Giro

Inter-bank Giro (IBG) was enhanced in July 2001 to a browser-based eGiro system, which allows participants to send and receive Giro items, including returned and rejected items, electronically via a secured communication network. With eGiro, clearing cycles for the direct credit and debit transactions are shortened significantly.

## Financial institutions

Commercial banks operate as full banks, wholesale banks or offshore banks. As of April 2013, there were a total of 123 commercial banks operating in Singapore. Commercial banks, licensed and governed under the Banking Act, may undertake universal banking. In addition to commercial banking, they may carry other businesses regulated or authorised by MAS, including financial advisory services, insurance broking and capital market services. They are however barred from engaging in non-financial activities.

There are three local banks in Singapore, with the biggest being DBS, followed by OCBC and UOB. Prior to the consolidation of the local banking industry in Singapore, some banks had already established a footprint in Asia, according to J.P. Morgan's Ang; however, the expansion increased significantly after the consolidation. DBS, which bought Kwong On Bank and later Dao Heng Bank in Hong Kong, is now focusing more on the North Asia market, while OCBC is looking into the South Asia market and UOB is looking at both.

Full banks with Qualifying Full Bank privileges may operate in a total of 25 locations. Wholesale banks can offer the same range of banking businesses as full banks but cannot carry out Singapore dollar retail banking activities.

Offshore banks can engage in the same activities as full and wholesale banks for businesses transacted through their Asian Currency Units, which banks use to book all their foreign currency transactions conducted in the Asian Dollar Market. The banks' Singapore dollar transactions are separately booked in the Domestic Banking Unit.

Fitch, in a statement in March, notes that domestic banks maintain solid asset quality and are well-capitalised, with a non-performing loan (NPL) ratio of 1.2% and core Tier 1 capital adequacy ratio of 12%-13% as of end 2012.

The credit rating agency says risks related to a potential build-up of a property bubble, spurred by prolonged negative real interest rates and optimistic prospects for Asia, led the authorities to introduce a seventh round of property cooling measures in January this year. These measures, together with the banks' strong standalone strength and healthy household balance sheets, mitigate downside risks for the domestic banking sector.

"The system may face more risks from growing exposure to high growth markets such as China, India and Indonesia, but this is not a material risk in the near term," Fitch says.

## Cash management

J.P. Morgan's Ang says, given that Singapore has no FX controls, various kinds of cash management techniques are used, whether physical cash concentration or notional pooling. "It all comes down to how well known the technique is in the market and how comfortable the corporate is in applying these techniques as each of them has its own advantages and disadvantages. It also depends on the corporate's appetite and what they require."

She says both physical cash concentration and notional pooling have been in the market for a very long time, but notional pooling is not as well known or researched. "There are also tax implications that need to be considered by the corporates and, as such, some companies tend to favour one technique over the other. But having said that, all the techniques are available in Singapore and there is no regulatory limitation as to which technique is being applied."

Blair agrees that the country is open from a tax, legal and regulatory perspective. Because of that, Singapore is the most popular hub in Asia for cash concentration arrangements like zero balance account, sweeping and pooling.

"Singapore is Asia's largest derivative centre and especially strong in FX, so it is excellent for financial risk management," says Blair. ■

# Taxing times

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

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

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

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

## Where is paying taxes easiest and where most difficult?

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

Source: Doing Business database

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

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

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

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

## Australian developments

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

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

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

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

## Asian complexity

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

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

"Treasurers across the region would benefit from co-ordinated lobbying of governments on tax policy issues."

Delores Goh, Head of Tax in Asia Pacific, Jones Lang LaSalle

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

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

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

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

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

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

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

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

## Potential for greater harmonisation?

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

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

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

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

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

"The only substantial tax change in Malaysia recently has been around new transfer pricing regulations, which is right since



most jurisdictions have transfer pricing rules. We are yet to see the application of these rules, but I would expect them to be applied in a balanced way based on previous experiences.”

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

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

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

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

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

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

of the world. The struggle of foreign retailers to get access to the Indian market is another example.”

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

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

## Adapting to change

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

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

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

## Favourable locations for RTCs: Singapore and Malaysia

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

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

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

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

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

# Leap of faith: are Asian multinationals ready for RTCs?

*As Asian multinationals continue to expand across the region, the incentives to centralise their treasury operations into regional treasury centres (RTCs) are hard to ignore. A centralised treasury centre can reduce processing times, simplify cash flows, reduce headcount and avoid unnecessary duplication, yet setting one up poses numerous challenges.*

Western multinational companies (MNCs) have become somewhat accustomed to the establishment of regional treasury centres (RTCs) in and outside of their home markets. Their Asian contemporaries have, so far, been somewhat more reticent. That distinction may be abating. With Asian giants Sony, Huawei and Lenovo, to name just three, already having made this leap, what are the options, difficulties and regional trends surrounding this development?

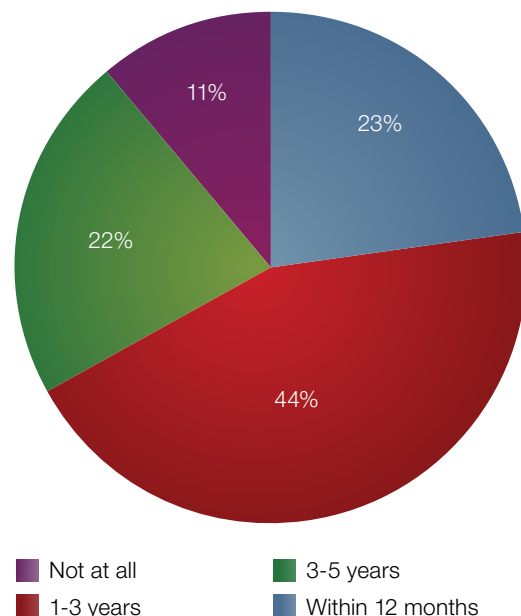
Singapore leads the field in terms of a location for a RTC and this does not seem likely to change anytime soon. Some of the world's largest companies, including DuPont and DHL, have already located their RTC in Singapore. Unilever has taken its treasury operations a step further by consolidating its former RTCs into a global infrastructure for operational treasury activities, called global treasury operations (GTO). The cornerstone of this infrastructure is the World Treasury Centre (WTC) in Schaffhausen, Switzerland. In the WTC, all daily funding, investment, liquidity and foreign exchange (FX) management activities are executed with internal group companies and external counterparts.

In Treasury Today's 2012 Asia Pacific Corporate Treasury Benchmarking Study (see Chart 2), 51% of Asian corporates surveyed cited Singapore as the preferred location for sub/regional treasury centres for the Greater China region, with Shanghai coming in second at 46%, Hong Kong third at 43% and Beijing last with just 7%.

The same study also asked respondents about their anticipated timeline for the CNH/CNY actively being used for inter-company and third-party trade settlements (see Chart 1), which is an important consideration for any company establishing a RTC in the region with interests in China. Over 60% of respondents think this will happen within the next three years.

Traditionally Asian MNCs with a strong global presence were to be found based in Japan and Korea. Taking a closer look at the first example, Japanese MNCs were historically inclined to practice a far lower level of treasury centralisation than Western MNCs. In 2005, Japanese car manufacturer

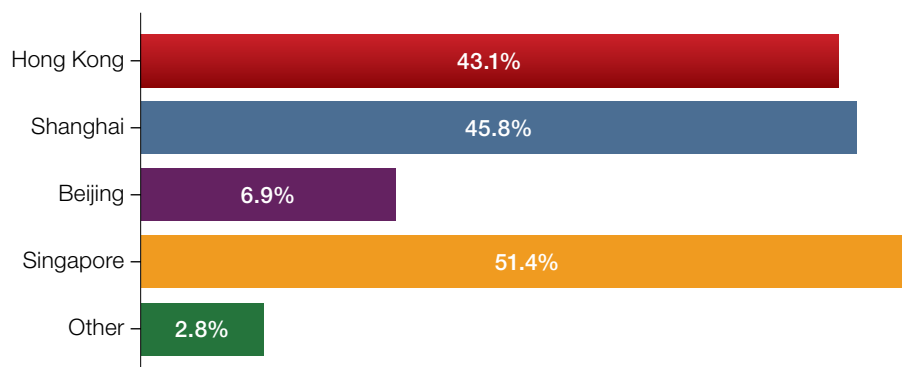
**Chart 1: Do you see CNH/CNY actively being used for intercompany and third part trade settlements?**



Source: Treasury Today's 2012 Asia Pacific Corporate Treasury Benchmarking Study

Nissan established a RTC in Singapore, yet Nissan's Japanese contemporaries did not exactly rush to follow them. However, Gourang Shah, Citi's Head of Treasury Advisory for Asia Pacific, says that "this reticence is being put under pressure by the strong competition that Japan is now facing from China, Taiwan and Korea. As a result of this, Japanese corporates are increasingly looking to centralise their treasury operations and today corporates from China and India and to a lesser degree other Association of South-East Asian Nations (ASEAN) countries, are expanding their global footprint."

**Chart 2: Which location(s) do you see emerging as the preferred location(s) for sub/regional treasury centres for the Greater China region?**



Source: Treasury Today's 2012 Asia Pacific Corporate Treasury Benchmarking Study

With the expansion of these countries comes an increasing interest in RTCs. The lure of a more cost effective and operationally efficient treasury department drives this interest, yet there is a level at which a company must be before they are ready for this step. Margaret Yao, Regional Sales Executive, Asia Pacific, Treasury Services, J.P. Morgan, notes, "in order to be able to go down the RTC road, these companies require senior sponsorship to drive the evolution and ensure a seamless re-engineering of their internal workflows, as well as have an ongoing commitment to investing in common ERP (enterprise resource planning) and TMS (treasury management systems)."

What should be done by these companies before they can be truly ready? Although there isn't a one-rule-fits-all guide there are some generic indicators. "Lots of Asian companies still need to work on their treasury function, such as cash concentration, improving visibility and access to cash," says Francois-Dominique Doll, Product Specialist, SunGard AvantGard. "Although it varies on a case-by-case basis, I would agree there are many areas for improvement, but they are catching up very quickly. European and US companies took five to ten years to transform their treasuries, whereas Asian companies are looking to achieve this within two years."

Asian treasurers are well aware of best practice techniques. Even companies that haven't centralised or transformed their treasury are aware of what is out there. However, this does require buy-in from top-level management as well as from the operating subsidiaries. "If they really want to remove any inefficiencies and improve working capital management, they will need to release resources in order to achieve that goal," says Doll.

In Asia there are many restrictions in moving cash from one country to another and each country follows different policies in terms of cash management. Lenovo's Treasurer, Damian Glendinning, explains that having cross-border loans is a major issue for corporates as many countries have FX rules. "When it comes to Asia, countries with no exchange controls are the exception rather than the rule," he says. Only the Japanese yen, Singapore dollar, Australian dollar, New Zealand dollar and Hong Kong dollar are easily convertible outside of their respective home markets.

#### **A typical regional treasury centre will perform some or all of the following functions:**

- FX dealing and management.
- In-house bank.
- Inter-company loans.
- Trapped cash management.
- Risk management.
- Asset management.
- Liability management.
- Credit and derivatives products in capital markets.

#### **Where to go**

The reality is that there are few countries in Asia that offer the depth and open markets needed by RTCs. Historically choices have been – and still are – Singapore and Hong Kong. Shanghai is emerging as a third alternative, yet with FX controls remaining in place it is not necessarily an ideal location unless a corporate's operations are solely in China. Australia used to be one of the first choices for corporates, given the language and the Western culture. However, its physical distance from the rest of Asia has resulted in many relocating their RTCs to either Singapore or Hong Kong.

Singapore will continue to be an attractive centre for MNCs due to its proximity to India and South-East Asian markets and its successful track record in market development, such as the derivative market and fund management industry. The nation's English language proficiency remains its competitive advantage and its AAA sovereign rating is an important selling point in its establishment as a wealth management centre. The government is strongly committed to high-end management education and actively encourages employment of expatriates to mitigate possible talent gaps and support future growth.

Singapore has a deep and liquid FX market, an excellent pool of well-educated labour, and world class transport and telecommunications infrastructure. Over the past ten years



the number of RTCs located in Singapore has grown steadily, with a surge in numbers since 2008.

The city state's attractive tax benefits are a strong pull, particularly the many double taxation agreements (DTAs) they have negotiated with their trading partners. And, of course, Singapore is the region's pre-eminent banking centre with a wide mix of readily spoken languages.

Up-and-coming, Shanghai has set a timetable to achieve international financial centre status by 2020. It is already the centre for the domestic renminbi (RMB) financial market in terms of the size of both the equity and bond markets. The volume of international cross-border flows is subject to the timetable of the liberalisation of the capital account. Currently the intermediation of capital outflow is through the Qualified Domestic Institutional Investors (QDII) scheme. Significant developments in the Shanghai financial markets are anticipated in the years to come.

Hong Kong can claim many of the same advantages as Singapore. Its currency, the Hong Kong dollar, is pegged to its US counterpart. It operates a 'benign' tax regime and a concentration of the world's leading banks. It is home to over 1,300 bank branches and over 200 authorised institutions. These include a number of investment banks, which serve the debt capital markets. In 2009, Hong Kong's banking infrastructure was updated and the SWIFTNet system replaced the previous high value clearing system, the Clearing House Automated Transfer System (CHATS).

For cash concentration activities, both Singapore, with its finance and treasury centre (FTC) incentives, and Hong Kong, have withholding tax on interest waivers but, for lending money, the applicable withholding tax rule is from the country that pays interest. Hence, DTAs help with withholding taxes.

An additional issue is the maturity of the infrastructure offered and the presence of a financial hub, which comes with service providers such as banks, tax and legal experts.

Managing Director of Acarate and former Vice President Treasury at Huawei, David Blair says he is seeing many Asian MNCs from South-East Asia, China and India setting up international treasury centres and RTCs in Singapore. "Motives vary but essentially they are looking for a real international financial centre not far from home," he explains. Companies will often opt to set up RTCs in China or India if there is a large enough domestic presence to justify doing so.

Similarly, Hong Kong comes up as the preferred location for a RTC for North Asian companies, but observers note that more often than not, after the initial move to Hong Kong, even these companies prefer to relocate to Singapore for tax reasons.

Lenovo's Glendinning adds an interesting note to the decision-making process stating that the criteria is often not based on hard logic. There is always a human element when deciding whether to set up a RTC and where. The human element is highlighted in the table which shows an interesting comparison between Europe and Asia in terms of the number of full-time equivalents (FTEs) employed in the treasury department. This perhaps illustrates the benefits of establishing a RTC. Almost 75% of respondents to the European Study were regional treasuries in Europe and just over half employ just one to four FTEs.

Number of FTEs employed	Europe	Asia Pacific
1-4	51%	39%
5-8	22%	20%
9-12	6%	15%
More than 12	21%	26%

Source: Treasury Today's 2012 European and Asia Pacific Corporate Treasury Benchmarking Studies

Furthermore, whilst the establishment of a RTC, whether it is South-East Asia, China, India or Eastern Europe for that matter, requires sound technology, systems, people and robust banking partners. Treasurers should not underestimate the legal implications. The scope and jurisdiction of any RTC structure will impact its legal constitution so time spent thinking about the framework of an RTC is time well spent and vital to its ongoing success.

Another consideration for the location of RTCs is the legal system and its workings. Singapore, Hong Kong and Australia are common law systems, with precedence and transparency, and the courts, lawyers and judges are all independent of the government. China meanwhile is rapidly developing its legal framework but still has a way to go before the same levels of legal protection exist as with other international financial centres. A common legal framework is very important to protect financial transactions and structures that cross borders.

The objective pros and cons are not the only consideration; there is usually a fair amount of politics involved, personal preferences and agendas that can influence the final decision. If the hurdles can be overcome however, with the right structure and location the benefits can be worth the pain.

Finally, the environment also needs some attention and banks need to respond if they are to attract the cash management mandates of companies operating in the region. Here is just a small selection of the responses from RTCs in the region when asked: "What improvements should your service provider(s) be delivering?"

"Internet access on mobile, and capability to integrate with our internal IT-SAP system."

Telecoms company based in Thailand

"Easier SWIFT connectivity, better multi-bank reporting."

Agricultural commodities company based in Singapore

"Cash repatriation mechanisms for locations with trapped cash such as China, India and Korea."

Construction company

"Cash pooling for multicurrency for multi-country."

Energy and natural resources company based in Singapore

Source: Treasury Today's 2012 Asia Pacific Corporate Treasury Benchmarking Study

We would like to acknowledge the assistance of Russell Brown, Managing Partner, LehmanBrown, in the preparation of this article. ■



# Ahead with Lite-On Mobile

**Mikko Sopanen**  
Director of Treasury



Mikko Sopanen joined the global treasury of Lite-On Mobile (LOM), formerly Perlos, in 2006. He was appointed Director of Treasury in 2008 to lead the treasury migration from Finland to Taiwan, where he stayed until 2009. After ensuring a smooth transition, Sopanen then returned to Finland, travelling to company hubs in China and Asia on an as-needed basis. But in 2011, Sopanen relocated to Singapore, where he has worked, heading up treasury there ever since. Prior to his career at LOM, Sopanen worked as CFO and co-founder of cloud software company, Nextime Solutions. He has a Master of Finance degree from the University of Oulu and is currently completing an Executive MBA at Aalto University of Helsinki.

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*Established in Finland in 1953, Lite-On Mobile (LOM) is an international design and manufacturing partner for the telecommunications and electronics industry worldwide. The company is owned by Taiwanese Lite-On Group with its core headquarters based in Vantaa, Finland. LOM provides services and commodities from design and concepts to manufacturing, final assembly and testing.*

The Lite-On Group acquired Perlos in 2007, a company with a wealth of experience, a history of dealing with mobile phone components since the 1980s. As part of the acquisition transition, many of the group operations were migrated from

Finland, where the entire operations were previously based, to Asia, says Mikko Sopanen, Director of Treasury, LOM. "Most of the central operations, such as the CFO and finance department, are now all based in Beijing. However, some

other operations are in central China where our main customer base lies. Since our funding needs are more global, we (the treasury) are based in both Singapore and Taipei.”

Employing around 14,800 people worldwide across 11 manufacturing plants in Asia and the Americas, LOM boasts a strong local presence in all major markets. Its global customers include leading handheld device brands such as Huawei, Nokia and Sony Mobile Communications.

In this relatively new structure, Sopanen describes a treasury that is mainly centralised with regards to company agenda and policy-making for major cash and foreign exchange (FX) decisions. But because the geography in which LOM conducts business is so diverse – with operations in countries such as China, India and Brazil – the electronics firm ensures that a dedicated employee is working for treasury in each location. This allows FX trade, hedging, cash management and accounts payable (AP) and receivable (AR) to be dealt with at a local level, according to Sopanen. “Effectively there are five of us that cover treasury across the globe. I’m embedded in Singapore as a director, accompanied by one assistant manager who handles FX. One director and assistant manager are based in Taiwan, mainly for cash management – effectively handling the cash flows and daily funding. The fifth person is located in Guangzhou, China, controlling the complexities of Chinese hedging and cash management,” he explains.

LOM was presented with a Logistics Efficiency Award last year (October 2012) by airport operator Infraero for its logistics work in the cargo terminals of Brigadeiro Eduardo Gomes International Airport in Manaus, Brazil. Infraero evaluated 100 best-in-class companies and their international supply chain management before selecting its award winners. Further strengthening LOM’s industrial position in the attractive emerging market location of Brazil, the firm announced a joint venture earlier this year with Yamada Electric Industrial, with the goal of developing an extended product range and more efficient deployment of manufacturing capacities on the LOM Manaus site. With net sales of €705m at year end 2012, LOM’s growth strategy appears to be working well for the company’s bottom line.

## Strategic cash structures

Mobile phone component design and manufacturing is a very rapidly developing and changing industry – a high volume, low margin business. As such, LOM’s ‘order book’ of sales is for a maximum of one week, so the confirmed sales visibility is very short. This creates certain challenges for treasury in the areas of FX and cash management, for example. As such, the financial partners that the company has opted for must be capable of meeting those demands. Says Sopanen, “we have a few global banks but, in my experience, I believe that no one bank can provide everything required in terms of special needs and location. While Citi bank is the bank that we use at a global level, we also have one or two local banks at each manufacturing location, which we will use for different areas of finance management, such as daily cash collection.”

One region that creates added complexity for the LOM treasury in relation to these ‘special needs’ is China. For over a decade, the company has been using a cash pool specific to the country’s regulations that Citi helped to set up. The pool consists of entrust loans whereby the bank basically acts as the middle man, setting up a new loan for each requirement. And being renminbi (RMB)-based, Sopanen

feels that the company has been in a good position so far. However, he has been leading a project in order to consolidate and centralise the cash flows for imports and exports from all companies, to the Asian headquarters.

According to Sopanen, there are at least two substantial benefits. “One is that by setting up the inter-company payment terms and managing the payment timing we can actually use the operative cash flows to allocate our cash between China, India, Brazil and the rest of the world. I would say that we have three cash planets, not even countries, as every cross-border transaction and cash transfer is so restricted. This is in stark contrast to cross-border transactions and funding in Singapore and Western countries which operate much more smoothly.”

This structure also allows for strategic decisions to be made regarding varying currency amounts at any given time much more simply, Sopanen continues. “For example, in China we increase RMB as much as we can so that the exposure in China (or India etc) will be minimised. I started this project back in 2009 but it has been very much a cross-organisation project. Our vendors will have to centralise their transaction and the sales team will have to globally invoice on the customer side as the company location has changed for them. This has also given us huge benefits regarding sourcing as we can now monitor and combine the orders.”

When it comes to credit facilities, LOM is part of a lending syndicate with some Taiwanese and global banks, and also holds several single bank facilities, including term loans. These revolving facilities provide a flexible funding tool for the company to manage its rapidly changing working capital needs and funding for LOM’s investment appetite.

## Technical trends

Although treasury technology may also seem to lag behind its Western counterparts (LOM’s treasury is still mainly spreadsheet-based), Sopanen – with an extensive background in the Nordics – believes that the methods used are quite advanced, nonetheless. “We have a slightly older, smaller system in our treasury – but it works well and is an excellent reporting tool. Our enterprise resource planning system (ERP), SAP, is also integrated into our existing systems and as we have not encountered any complications to date, we can see no reason to change from our excel structure.

“The decision to invest in a new system will most likely happen, but currently the cost question and the large change involved in such a modernisation plays a large part in deterring the upgrade. The salary cost that constitutes the addition of one or two people is minimal compared to a new system and we are currently very satisfied.”

Taking into account the industry Sopanen is immersed in, it’s understandable – if not assumed – that mobile treasury is a way of life at LOM. “We can use all the reports and can access the system through mobile devices, which can be really helpful as physically our treasury is so widely spread. Our IT system is so extensive that I have internet access and access to all systems everywhere. I have the same connections whether I am at home, travelling or in the office – that’s been a big advantage for the entire company, from the sales teams through the finance departments and up to Board level.”

Having access to work systems remotely – while extremely effective for home workers, frequent travellers, or in the event of



natural disasters (where travel to work is impossible) – can also play havoc with work/life balance for employees. Does Sopanen see this as a worrying trend in his treasury? “To be honest, it would be more common for our Finnish staff to work from home, but our Asian contingent would definitely use this option too – purely for reasons of convenience. One example of this is that, with the new Asian headquarters, we have significantly tighter reporting schedules compared to the timetable we previously adhered to.”

This area has improved dramatically for LOM treasury as consolidation and finance of cash flow, cash balances, and even sales costs are conducted on a daily basis, says Sopanen. “For example, one of the special reports that we do is cash closing on a monthly basis – on the first day of every month, the entire P&L (profit and loss) is balanced, regardless of whether its Saturday or Sunday. To accommodate the instances when this date falls on the weekend, we mostly opt to work at home.”

This rigid reporting process is very impressive compared to the lax reporting standards that many Western companies follow and Sopanen believes that this structure allows close scrutiny – and rapid reconciliation – of the company’s P&L operations.

## Risk and opportunity

Bearing in mind the scope of these operations – LOM company sales are \$1 billion annually worldwide – the FX transactions involved can be quite specific and the volumes can be incredibly high. Aware of their exposures, Sopanen and his colleagues keep a close eye on market trends but also deal directly with the banks over the phones or on the banks’ electronic platforms, with a preference for the vanilla products. “We love simple structures so we deal mainly with forwards and swaps, especially as we’ve been focusing a lot more on actually reducing the hedging by creating these operative positions,” says Sopanen. “We still have exposures in Indian rupee as well as for RMB in China and certain exposures for euro and the Brazilian real.”

LOM has been expanding its local hedging in India in recent months, trading both offshore and onshore currency in the region. But it is the FX operations in China that Sopanen really finds fascinating. “When hedging in China, there are three different rates (local currency, offshore RMB and CNH) so we have been optimising this for our benefit. Now there is even a fourth rate in some countries. Four different rates for the same currency makes it very interesting from a FX perspective. It’s a huge opportunity but also quite a risk to manage.”

Perlos/Lite-On was not part of the flurry of merger and acquisition (M&A) activity borne of the financial crash, as the merger occurred before the downturn in 2007. Nevertheless, Sopanen maintains that the company has felt some of the impact of the aftershocks, and the crisis in the Eurozone in particular, as global volatility (although somewhat eased now) had increased significantly, creating a domino effect with its own banking relationships. “Certain dealings with banks have changed in the sense that some international bank’s funding and FX limits have become more conservative and restricted.”

Yet, being based in Asia, the financial crisis itself did not have a hugely negative effect on the company’s operations and profits themselves, other than the acknowledgment that European demand was a little bit slower. In fact, business has been improving, says Sopanen. “Overall there have been major shifts and innovative developments in the mobile

industry worldwide. These shifts have impacted our business in a positive way, regardless of location.”

## Recruitment success

For many corporates expanding or relocating operations to Asia, one of the main concerns is the difficult recruitment arena in the region. Sopanen is rather the exception as he was, in fact, pleasantly surprised with the talent pool – and successful in his efforts to retain them. “We were always expecting recruitment to be very tough. In 2008, we began the search for employees in China for the first time but, over the past five years, the potential has grown considerably and there are very skilled people across China and Taiwan.”

Sopanen is also looking outside the box when it comes to recruiting staff for his team – and this is a result of the regional demands of some of the geographies they are operating in. For example, as a publicly listed company, heavily regulated Taiwan is very tough on LOM’s treasury. “There are many processes and activities that we must report and this has to be open and transparent. For instance, when it comes to derivatives (either foreign or not) or funding, there are many rules and regulations to follow and we need to write up a report for it all. These reports are all publicly announced so people can see what deals we have done.”

The upshot of these strict requirements is that because there is now so much reporting to be completed as part of the treasury work quota, Sopanen has been hiring people from outside treasury. “They might have a background in finance or in auditing, for example. This has been very successful as sometimes the treasurers don’t enjoy this ‘hard work’ so employing someone from a very busy company with a different background who might even be very keen on reporting can be very helpful – they must also have a passion for treasury, of course.”

The most suitable person would naturally be local to the region, for many reasons, says Sopanen, and this has been the company policy of late. Despite the fact that LOM is a very Western-managed company – CEO Cor Saris is Dutch and CFO Donal Breen is from Ireland – the ambition is to have many locally managed organisations, perhaps due to the regulatory difficulties in the geographies of the company’s hubs. “In China, for example, language and culture are essential so having local people in that context would be a real strength. They can communicate better with the sales teams and are much better at understanding the environment and liaising with the local authorities. That’s the talent we are looking for.”

## Natural growth

An organic firm, LOM has been constantly growing over the past five years and has been busy creating new hubs and enterprises in Asia. Perlos’ acquisition spelt a measured change for the company’s operations in many ways, especially for treasury. “Treasury was the first one that was required to get in line in many ways with the parent company, when it comes to treasury policy, structure and, of course, the funding,” says Sopanen.

The further opening up of RMB and cross-border funding options internationally for China, in addition to the (albeit slowly) maturing money markets in India and Brazil, will provide more interesting projects for LOM to work with in the near future. ■



# Debt capital markets in Indonesia: one to watch

*The debt capital markets in Indonesia may not be as large or as developed as others in Asia but they are moving in the right direction.*

## Growth and stability

Indonesia has worked hard to develop its domestic and international bond markets and since 2012 there has been an upsurge in the number of government and corporate bond issuances, which is very much in line with Indonesia's economic growth. It is an active market but the country's volume of issuance compared to other jurisdictions around Asia is relatively low, particularly in view of the size of the country's economy. It is fair to say that the Indonesian bond market is still in the early stages; indeed, there were no government bonds prior to 1997.

Amidst the background of an expected 6% GDP growth, 20% loan growth and low credit costs, the general trend is one of increased activity in the bond markets. Ji Liu, a Partner at

Norton Rose in Hong Kong and Ferzana Haq, Of Counsel at Norton Rose in Singapore who advise financial institutions, sovereign and corporate issuers on debt capital markets instruments and Shari'ah-compliant products, observe that interest in tapping the debt capital markets is on the rise in Indonesia. This is because the coupon rates on bonds have fallen, making it a cheaper source of funding than bank lending, both in the domestic and international bond markets. According to the Jakarta Globe, many Indonesian companies are turning to the debt market to capitalise on low borrowing costs, with Bank Indonesia having kept its benchmark interest rate at a record low of 5.75% since February last year in an effort to spur economic growth.



## Bond momentum

With a focus on Indonesian government and companies cross-border bond issuance, mostly in US dollar, Haq has seen the activity in the past three years gather serious momentum. The government has done a lot to encourage cross-border issuance, she notes, pointing to a number of “large scale” sovereign bonds, both conventional and sukuk.

As an example, both Haq and Liu led and represented the Government of Indonesia’s landmark \$1 billion sukuk issuance in November 2011 and the Government’s first international sukuk programme of up to \$3 billion in 2012, both of which were made available to US and non-US investors. These issuances were complemented this week with a further \$3 billion dual-tranche (ten and 30-year) conventional bond, predominantly allocated to US investors. This most likely concludes the country’s conventional offshore funding for this year, but further sukuk issuance may come later in the year.

The burst of activity and the size of the issuances reflect the general improvement of Indonesia’s improved credit rating, achieving investment-grade status for the first time since the 1997 Asian financial crisis. Moody’s assigned a Baa3 rating to Indonesia’s global bond offering and a stable outlook. Standard & Poor’s (S&P) currently offers a BB+ and positive outlook, whilst Fitch goes for a BBB- and stable. Becoming investment grade has made it more attractive for international institutional investors to invest in Indonesian government bonds, and it also means the government has access to a cheaper source of funding in terms of coupons.

This has had a knock-on effect. By going through the credit rating process in respect of its \$1 billion sukuk issuance in 2011, Indonesia’s credit rating was raised to investment grade, which in turn gave it access to a wider pool of investors and cheaper funds. Much of these funds were used, or are to be used, for the national budget and to develop Indonesia’s infrastructure projects. Infrastructure development remains a major requirement – and improvements to the country’s infrastructure (including road networks, transportation, utilities, etc) is a major part of Indonesia’s economic progress and would go some way to enhancing the overall profile of the country and contributing to the maintenance of its credit rating. And, as Haq points out, the sovereign’s rise to an investment grade rating creates an environment of confidence, and would enable Indonesian corporates to tap the international bond markets too.

## Stable environment

Practical delivery and trading of international debt instruments is handled entirely electronically, says Haq. Trading of non-domestic bonds takes place over-the-counter (OTC) and are cleared for international bond issuance handled either via Euroclear or Clearstream and, if issuing into the US, through the Depository Trust Company (DTC). It’s a very stable, well run process and I don’t see any concerns on that front.

The market is also a lot more stable now in terms of its general risk, but companies may span the whole range of risk profiles. At the one end of the scale are the state-owned companies and large and steady corporate entities that are highly rated and enjoy low-coupons and limited covenants because there is confidence they can meet their debt obligations. At the other end of the scale are low rated or distressed businesses that often refinance through bond

issuance, getting into the market by issuing high yield bonds which are subject to far more restrictive covenants.

The consistency of activity over the last couple of years contributes to the general impression that Indonesia is a more stable country and this has created a lot more interest from international investors, notes Haq. Companies such as the state-owned power utility, PLN, and the privately-owned national airline, Garuda, have engaged with the bond markets in the past, and she believes that current market buoyancy and the low coupon rate that highly rated entities can command will see a number of sizeable bond issuances this year. “All of this contributes to the increased confidence in Indonesia, making it much easier for other Indonesian corporates to tap the markets, ensuring the coupon rates they have to pay remain attractive.”

The level of bond issuance remains strong globally and with many banks now unable to fully fund the demand for loans, in part because of their own capital requirements, Haq sees many seeking to act as arrangers or managers to distribute bonds into the institutional bond market where there is more appetite for longer-term debt. “The bond markets still have enough room to take up that form of funding so it is covering the gap where international banks may no longer be able to, because they are facing their own credit squeeze,” she explains.

## Infrastructure, regulation and the future

Two years ago the Indonesian government announced its Rp 4,000 trillion infrastructure programme (known as MP3EI) aimed at creating more domestic jobs and spurring economic growth. The scheme covers aspects such as the redevelopment of seaports, airports, roads, water and energy facilities.

A number of state construction companies have talked about plans to tap funds from the bond market, including Wijaya Karya, Waskita Karya and Adhi Karya. In March this year, the latter announced plans to issue Rp750 billion (\$77.5m) worth of bonds to finance its various investment plans. The company said it would be offering conventional and Islamic bonds and listing the notes on the Indonesia Stock Exchange (IDX).

Some companies are not tapping the markets to fund a specific project but instead to satisfy their own capital expenditure needs. Garuda Indonesia airline is a good example of this. It announced in March this year, a Rp2 trillion (\$205.52m) corporate bond issue set for the second quarter of 2013. Earlier this year Garuda’s low-cost division, Citilink, was reported to have ordered 25 Airbus A320 aircraft (around \$2.4 billion at list price) as a means of fending off rising competition in Indonesia’s budget airline sector. The bond market, notes Ferzana Haq, presents a “logical” source of funding for such plans.

## Project bonds

Some of the infrastructure developers that have set up special-purpose project companies, as opposed to fully operational ongoing businesses, do face some extra challenges in the bond markets, says Haq. “The bond markets have not been overly amenable to project bond financing because the ability to repay bondholders is dependent on the revenue stream from the project, which,

especially in the case of greenfield projects, would take a long time to materialise and are subject to construction risks, amongst other things. Historically, the bond markets have had little appetite for that kind of risk.” However, because bank funding is becoming harder and more expensive to obtain, she believes this will change over the next three to five years.

In particular, as projects which have already gone through the construction phase come up for refinancing, the bond market may present an attractive and cheaper alternative to bank lending. The challenge is to make sure these projects get their rating up to a level that fits within the investment policy guidelines of a broader sweep of investors (typically pension funds and insurance companies). Alternatively, they must find some form of support, perhaps coming from a government-backed guarantee or an export credit agency (ECA). “I think the way bonds are structured will need to adapt – project bonds tend to have more restrictive covenants, which require more monitoring; this is a big change for bond investors.”

The established corporate bond issuances in Indonesia – such as those issued by Garuda – have a secondary market because the bonds are relatively easy to sell and bond investors are particularly keen on corporate credit. The difficulty with a project bond, even if it can achieve the correct rating, is one of liquidity; investors need to be sure they can be in it for the long term, as the secondary market is not well-established. The same requirement applies to the sukuk market, where the secondary market is not of sufficient size to ensure strong liquidity – but Islamic investors tend to adopt an ‘invest and hold’ approach anyway.

## Market regulation and legal standing

In terms of market oversight, Indonesia’s capital markets regulator, Bapepam, has worked to ensure that its laws and guidelines have not restricted domestic companies from issuing bonds, either domestically or internationally. “But when it comes to the corporate bond market, the challenge faced sometimes in Indonesia is one of perception rather than the actual rules,” notes Haq. Even though there has been increasing confidence in Indonesia, there is still a perception it presents more legal risks simply because its legal system is not viewed as being as stable as other countries in the region. There is, she explains, a concern amongst some looking to invest in the country, whether in bonds or otherwise, around what the legal risks are and whether it is certain they can enforce their rights as foreign entities.

If a dispute arises over the terms in the bond document and a judgment is granted in favour of the investors by a foreign court under foreign law, judgements will still need to be recognised and enforced by the Indonesian courts.

Uncertainty as to whether Indonesian courts will recognise a judgement in all instances can be mitigated by incorporating within the documentation provision for arbitration. This takes it out of the Indonesian court system and into an arbitration forum in a country such as Singapore, which is currently one of the main regional forums. As Indonesia is a party to the New York Convention, an arbitral award would, in general, be enforceable in Indonesia.

Challenges can also arise where bonds are secured over assets in Indonesia. For example, if security is granted over land, it raises concerns over the application of foreign ownership restrictions and thus how long it may take to enforce the security. Making sure that any monies, which are part of that security package, are held in accounts overseas can give investors more assurance that they will be able to access the security if there is a default, says Haq.

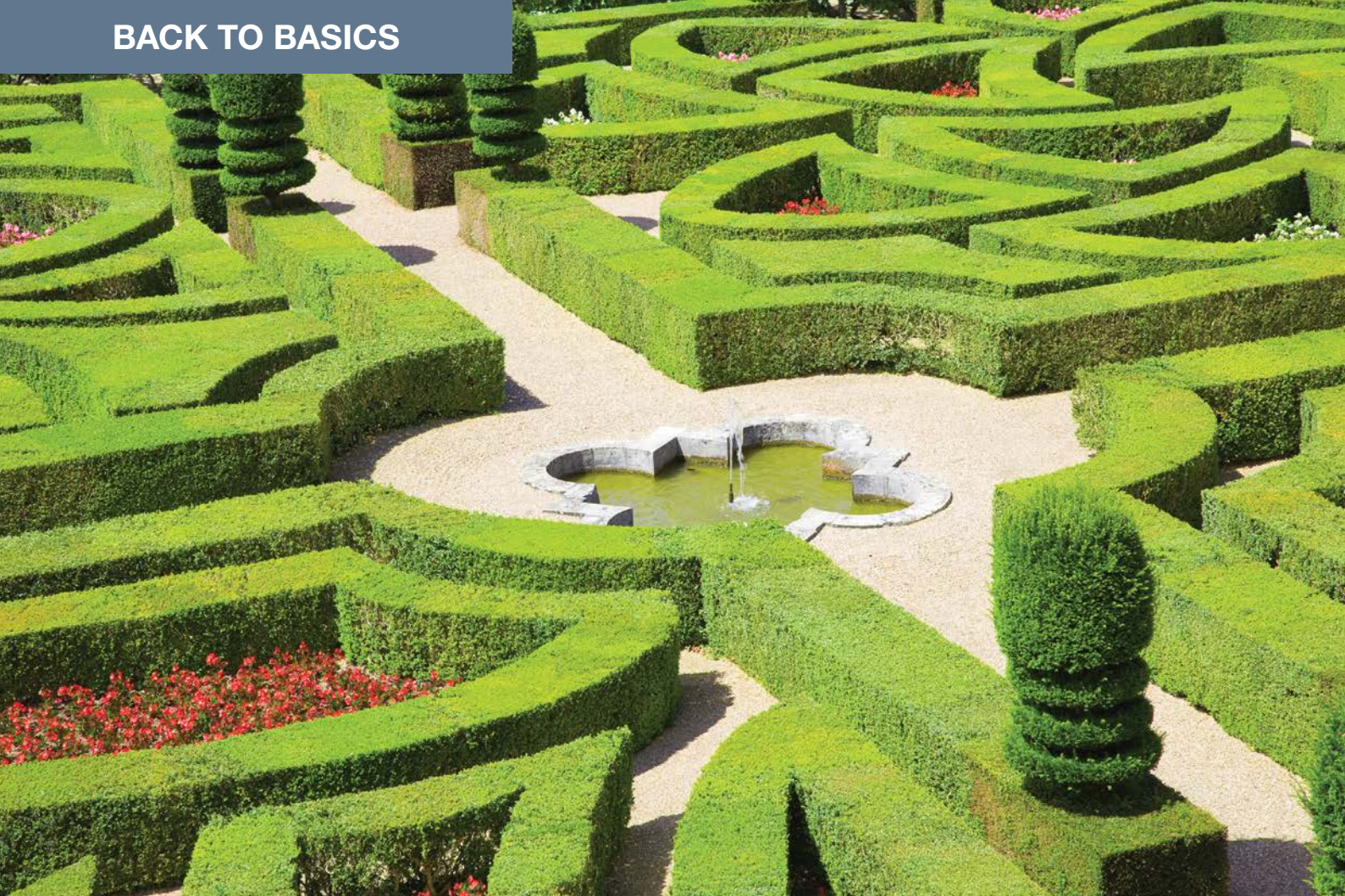
## Progress

Overall, the Indonesian debt capital markets are steadily improving in terms of access and security. The fact that the government itself has issued a number of large-scale bond and sukuk issuances shows its own commitment to turning the country into an attractive investment opportunity. However, Haq feels that the country needs to look more closely at its stance on Islamic finance. “Whilst the Indonesian government has issued sukuk internationally, a lot of the methods and structures for issuing sukuk would not be available to corporate entities in the country, in part because existing laws impose high taxes when it comes to the transfer of assets, which is a structural element of a sukuk transaction.”

By way of contrast, she notes that Singapore, which is not an Islamic country and does not have a large Islamic finance market, had passed regulations to incentivise companies to use Islamic finance, removing any additional taxes or constraints. Malaysia has the largest Islamic finance market, with much of the growth in sukuk stemming from its government’s amendment of regulations to level the playing field with conventional bond issuance.

“Indonesia, as the most populous Muslim country in the world, has huge potential for Islamic finance but it has not yet changed its regulation to allow for that; this has restricted the Islamic bond market from developing,” states Haq. Having gone to both conventional and sukuk markets over the past few years, its government has certainly given strong encouragement to corporate entities to follow suit. However, the regulations need to change and the laws need to be adapted before the sukuk market in Indonesia can reach its true potential. ■





# Short-term investments

*In the current global economic environment, corporates are finding the task of capital preservation increasingly challenging. For corporates operating in tightly-controlled Asian markets the decision as to where to invest surplus cash is often even more complex. In this article, we examine these and some of the other issues surrounding short-term investments currently facing the corporate treasurer.*

Generating profit is not usually the concern of the corporate treasurer. Treasury departments are cost centres, their function limited to managing accounts and, where possible, controlling the financial risks stemming from the company's operations.

So, why would a non-financial corporate decide to invest surplus capital? The reason in most cases is the preservation of principle. Particularly in today's low-interest rate climate, the value of corporate cash deposited with banks is vulnerable to erosion through inflation. Moreover, with the Basel III regulation requiring banks to hold extra capital against deposits, they are becoming more reluctant to hold large sums of surplus cash.

The contradiction lies in that companies in Asia, as in Europe and North America, are growing more cash-rich. For example, recent data compiled by Thomson Reuters indicates that two China-listed companies, China Life Insurance

Company and Ping An Insurance Group, have cash balances of \$82 billion and \$38 billion respectively. But for companies such as these, deciding what to do with that money can be even more complex when you factor in the restrictive monetary policies at play in China and a number of other countries in the region.

## Investment priorities

A corporate's investment decision-making is usually influenced by three main considerations: security, liquidity and yield. The relative importance of these considerations has always run in that particular order. However, in recent years the importance of yield has diminished even further in the eyes of the corporate treasurer.

Following a financial crisis which plunged the global economy into a downturn, the like of which we have not seen since the



1930s, the growing risk aversion taking hold of companies should not come as a surprise to anyone. For treasurers investing in this perilous environment, security and liquidity have become paramount. The focus, therefore, will be on developing an investment strategy that produces the optimal risk-adjusted return.

Below is a summary of the key short-term investments companies may use to achieve this objective. These include:

- Money market funds (MMFs).
- Exchange traded funds (ETFs).
- Certificates of deposit (CDs).
- Treasury bills (T-bills).
- Repurchase agreements (repos).

## MMFs

With strong security and high liquidity, MMFs remain a popular option for corporate investors. This was reflected in a recent survey by Fitch Ratings, according to which 50% of corporate treasury professionals use MMFs, making the funds their next preferred investment vehicle after bank deposits.

The funds are typically used by corporates as an alternative to bank deposits, one which offers the investor higher yield but without sacrificing liquidity. There are significant differences between the two. MMFs are asset management products where providers secure yield for their clients through the purchase of a narrow range of highly-rated assets. Secondly, MMFs are not guaranteed, whereas bank deposits are. In fact, some critics argue that their ultra-safe, deposit-like appearance often masks a deep-rooted structural instability.

The risk for investors is that there will be a run on the funds or, to put it another way, too many investors seek to redeem at the same time. As a consequence, the fund may struggle to liquidate its assets quickly enough, causing the fund's Net Asset Value (NAV) to fall below the prescribed \$1 baseline, something which is referred to in the industry as 'breaking the buck'.

The last time an event of this nature occurred was in 2008, when the reserve primary fund collapsed as investors all rushed to the door over concerns about the fund's exposure to Lehman Brothers. Such events are uncommon, however. From the industry's beginnings in 1971 until the financial crisis, only three MMFs ever broke the buck – a figure which some critics argue might be higher without the discretionary sponsor capital many are able to draw upon in times of market stress to preserve their constant NAVs (CNAV's).

No wonder then that the same Fitch Ratings survey found that CNAV investors tend to place great emphasis on the importance of the sponsor when choosing a fund to invest in. Other factors commonly taken into consideration include the credit/risk quality – with AAA being the preference – and the funds past performance.

The industry is now more tightly regulated than it was prior to the financial crisis, and there is also the prospect of further regulation on the horizon. One proposal, recently mooted by the European Systemic Risk Board (ESRB), is proving particularly contentious. The ESRB recommended in a recent review, that there should be a mandatory conversion of all CNAV funds to floating NAVs, on the grounds that this would help to reduce the 'first mover advantage' believed to be a

cause of runs on funds. But this, some say, may diminish the utility of MMFs for corporate investors, who largely prefer CNAV because of the simpler tax and accounting treatment.

In recent years, MMFs have become an increasingly popular alternative to bank deposits for companies operating in China. In the past, these companies were rather limited in their options for managing liquidity. Both yields and tenors of bank deposits are regulated in the Chinese market by the People's Bank of China (PBoC), and rates are often lower than they would be if aligned to real market yields.

The introduction of MMFs has provided an attractive alternative for investors. Most of the funds currently flourishing in China follow guidelines set by the China Securities Regulatory Commission (CSRC), which are considered to be much tighter than current international guidelines.

## ETFs

Amid all the uncertainty regarding the regulatory changes to MMFs now looming on the horizon, corporate investors may wish to consider short-duration bond ETFs. A degree of caution should be observed as these types of fund typically assume greater levels of risk, compared with traditional MMFs, in order to secure marginally higher yields. Another big difference is that the shares of short-duration ETFs, unlike CNAV MMFs, fluctuate during trading hours – much in the same way as stock prices.

Again, these could be an option a corporate operating in China may wish to consider. In China, ETFs such as FXI, the iShares FTSE/Xinhua China 25 Index ETF, invest in the equity prices of China-based companies. Similar to MMFs, the funds reduce risk through diversification, allowing investors to gain exposure to a number of different sectors such as banking, construction, energy and communications.

## CDs

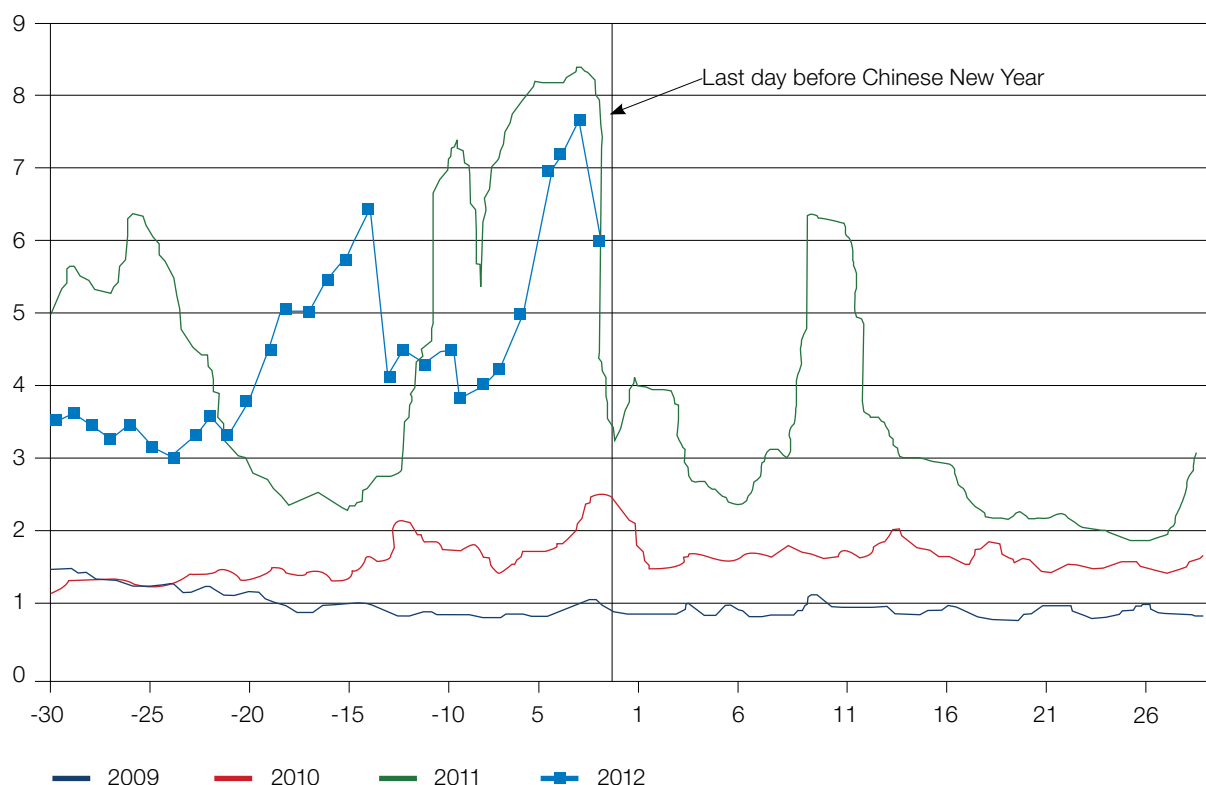
CDs are debt instruments issued by banks and other financial institutions which are widely used by corporates in place of clean, fixed bank deposits. In exchange for keeping the money on deposit for an agreed fixed-term, unlike a traditional bank deposit which can be withdrawn at will, a set rate of interest is paid to the investor. The rate that is offered is generally aligned to the maturity of the asset, which can range from only a few weeks to several years.

As is the case with any tradable instrument, the secondary market value can be impacted by investor sentiment. This is the main source of risk for corporate investors not wishing to hold on to the CD until maturity. It means that negative news concerning the issuing bank could, potentially, result in a dampening of demand for the product.

## T-bills

T-bills are a short-term money market security issued by national monetary authorities. The probability of a sovereign default is considered to be very low – recent events in Argentina notwithstanding – so T-bills are often the first point of refuge for investors during periods of market stress. The main disadvantage for investors in these securities is that yields are often minimal at best. For example, US T-bills have traded at negative yields in recent years and are currently close to zero.

**Chart 1: Seven-day repo rates before and after the Chinese New Year holiday**



Source: Bloomberg, Bank of America Merrill Lynch Global Research

## Repos

Repos involve the sale of securities such as corporate or government bonds tied to a commitment from the seller to buy them back at a later date. Investing in repos can sometimes prove complex. Such securities are therefore more suitable for large corporations with very sophisticated treasury departments able to handle the administrative burden.

In Chinese repo agreements, the collateral posted is typically a government or corporate bond. Repos cannot be entered into by foreign-invested enterprises. The yields on repos or short-term government debt are generally more attractive than short-term deposit rates.

A good time to tap the repo market is in the run-up to the Chinese New Year when banks are often short on cash as demand rises (see Chart 1). Again, when a big IPO comes to the market, exchange repo rates can be extremely high as investors rush to find ready cash. There is undoubtedly a correlation between hot stock issuance and inflated exchange repo rates. The seven-day bond repurchase rate closed at a three-year high of 7.69 at the start of 2013.

## Conclusion

The present economic climate poses a number of challenges for the corporate investor. Banks' appetite for deposits is diminishing as a result of new liquidity regulations such as Basel III. However, with interest rates near record lows across a large number of Western and Asian markets, low-risk

returns through investment vehicles such as MMFs are not easy to come by either.

The current scarcity of yield should not be the over-riding concern. New risks to global financial stability are emerging, even before the problems left by the last financial crisis have yet to be fully resolved. For corporates operating in this uncertain environment, security and liquidity will certainly be the main factors for consideration when it comes to depositing their cash, with yield now nothing more than an afterthought.

Are there ways to secure better returns without necessarily forsaking yield? There has been talk recently on the prospect of ultrashort-term ETFs being used in lieu of MMFs, should the proposed regulatory changes feared by the industry be introduced. The aim of these funds is similar to MMFs: preservation of capital. A note of caution, however – the risks assumed by investors in these funds may be greater than the norm in the MMF market. In addition, since ETF shares float and their prices are not fixed like CNAV MMFs, principle can be lost.

Finally, it is also important to remember that when it comes to returns on balances, yield is not the only factor. In recent years, banks have been developing new products – such as accounts which allow clients to use their operating balances to manage down their fees and increase their margins – which should certainly be of interest to the corporate treasurer, providing that is, they do not disappear in the wake of Basel III. ■

# Jensen's measure

*Jensen's measure is an important tool for treasurers who want to achieve the best possible return on any investment.*

Jensen's measure or Jensen's alpha, developed by Michael Jensen in 1968, is used to calculate the return on a portfolio in excess of its theoretical expected return. The theoretical expected return is based on a market model, usually the capital asset pricing model (CAPM). The CAPM provides a model for the risk-adjusted return on an investment. Any investment that performs better than its projected risk-adjusted return is said to have a positive alpha. Alpha is a measure of return over and above that explained by the securities market line and the investment's beta (volatility).

Jensen's measure is used to evaluate investment managers' performance, since a positive measure of alpha shows that the portfolio has outperformed the benchmark.

## How is it calculated?

Jensen's measure is a measure of alpha (a). It takes into account the excess return on the portfolio in relation to its beta and the return on the market as a whole.

$$a_j = R_p - R_f - \beta_p \times R_m - R_f$$

- Return on portfolio,  $R_p$ .
- Return on a risk-free investment,  $R_f$ .
- Expected return on the market as a whole,  $R_m$ .
- Portfolio volatility,  $\beta_p$ . Jensen's measure uses beta as a measure of volatility. This is the systematic risk or market risk to which the investment is subject.

## Example

Looking at an investment portfolio manager, let us assume that they have made a return of 20%. The rate of return on a risk-free investment is 3%, and the market as a whole experienced a return of 8%. The beta of the investment manager's portfolio is 1.4.

- $a = 20 - 3 - 1.4 \times 8 - 3$
- $a = 17 - 7$
- $a = 10\%$  or 0.1

The investment portfolio manager achieved alpha of 0.1, meaning that the portfolio outperformed the market by 10%.

## Efficient market hypothesis

Investment managers are constantly striving for alpha. When developing his measure, however, Jensen discovered in his research that no funds really ever did achieve alpha. The few that did, he attributed to random chance. In fact, Jensen's findings strongly correlated with the efficient market hypothesis.

The efficient market hypothesis was developed by Eugene Fama as a model for market performance. If the prices in a market reflect all available information, that market is said to be 'efficient'. This means that any external information investors may consider when making investment decisions has already been considered in the pricing of stocks. This effectively negates speculative trading and suggests that an actively managed portfolio may perform no better than a passively managed, or index, fund.

Jensen's measure is an important tool for treasurers who want to achieve the best possible return on any investment, whether that means achieving alpha or not. Jensen's measure may be used, in association with other metrics, to make predictions on the potential of a particular investment to outperform another, thus assisting treasurers in their investment decisions. ■





## COUNTRY FOCUS

### Indonesia

Indonesia has the largest economy in South-East Asia and is one of the emerging market economies of the world. However, companies need patience and perseverance to do business in Indonesia, as there are many regulatory and bureaucratic hurdles that often cause foreign investors to flee the country.

## TREASURY TRENDS

### Shifting global dynamics

The world is seeing a dramatic shift from West to East in terms of dynamic economic growth, which some have coined the 'great rotation'. Although China and India often make the headlines, other countries in South-East Asia are now coming to the fore.

## BACK TO BASICS

### FX portals

Corporate treasurers regularly need to exchange currencies, whether for trading internationally or investing overseas. Foreign exchange (FX) portals offer a quick and easy way to trade FX, as corporates can just log on and sell currencies in one area. However, uptake of this new technology has been slow. What are the barriers to adoption?

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

**Ying Siew Ang**, Head of Transaction Services ASEAN, J.P. Morgan (JPM); **Carole Berndt**, Head of GTS EMEA, Bank of America Merrill Lynch (BofA Merrill); **Manu Bhaskaran**, Founding Director and CEO, Centennial Asia Advisors; **David Blackwood**, Group Finance Director, Synthomer; **David Blair**, Managing Director, Acarate Consulting; **Russell Brown**, Managing Partner at LehmanBrown; **Dominique Blanc**, Head of SRI research, Novethic; **Olivier Brissaud**, Chairman of the Association des Trésoriers d'Entreprises en Belgique (ATEB); **Alf Capito**, Tax Policy Leader Asia Pacific, Ernst & Young (E&Y); **Royston Da Costa**, Group Assistant Treasurer, Treasury Systems and Development, Wolseley Group Services; **Sue Dean**, Managing Director and Head of Transaction Services EMEA, JPM; **Chris Devonshire-Ellis**, Principal and Founding Partner, Dezan Shira & Associates; **Francois-Dominique Doll**, Product Specialist, Corporate Liquidity Business, SunGard AvantGard; **Richard Ellis**, Director of CSR, Alliance Boots; **Damian Glendinning**, Treasurer, Lenovo; **Delores Goh**, Head of Tax, Asia Pacific, Jones Lang LaSalle; **Ferzana Haq**, Of Counsel, Norton Rose in Singapore; **Cindy Lee**, Regional Head, Treasury, BASF; **Ji Liu**, Partner, Norton Rose in Hong Kong; **Brad Maclean**, Vice President, Business Development, Corporate Liquidity Business, SunGard; **François Masquelier**, Chairman of the Association des Trésoriers d'Entreprise à Luxembourg (ATEL); **Tim Owen**, an Independent Corporate Treasury Consultant; **Vijay Panday**, Treasury and Risk Manager, KLM Royal Dutch Airlines; **David Pitt-Watson**, Senior Fund Manager and Treasurer, Oxfam; **Huib-Jan de Ruijter**, Director of Financial Markets, FMO; **Elizabeth Seeger**, Sustainability Lead, KKR; **Gourang Shah**, Head of Treasury Advisory, Asia Pacific Treasury and Trade Solutions, Citi; **Patrick Simeon**, Head of MMFs, Amundi; **Mikko Sopanen**, Director of Treasury, Lite-On Mobile; **David Smith**, Senior Advisor PricewaterhouseCoopers (PwC); **Paul Travers**, President, Finance and Treasury Association (Australia) (TOFA) and Executive Director, Oakvale Treasury; **Jeff Wallace**, Managing Partner, Greenwich Treasury Advisors; **Keith Welks**, Deputy State Treasurer for Pennsylvania; **Margaret Yao**, Regional Sales Executive, Asia Pacific, Treasury Services, JPM.

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\*Source: iMoneyNet as of 31/03/2013 and based on AUM for the Asset Management (JPMAM, PCS, PB) division of JPMorgan Chase & Co. as of 31/03/2013.

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