May/June 2015

treasurytoday ASIA

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From West to East

Whilst financial regulations often originate in the US or Europe, their impact is not limited to the West. Companies in Asia Pacific invariably find themselves in the position of having to comply with regulations that were formulated, or at least inspired, thousands of miles away.

The Corporate View

Denis Ecknauer

APAC Regional Treasurer

ABB

Regional treasury centres

With centralisation on the agenda for many corporates across Asia Pacific, competition between the region's treasury centre locations is heating up. We look at how Singapore, Hong Kong and Shanghai compare.

Trade

Understanding project finance

Know the Institution

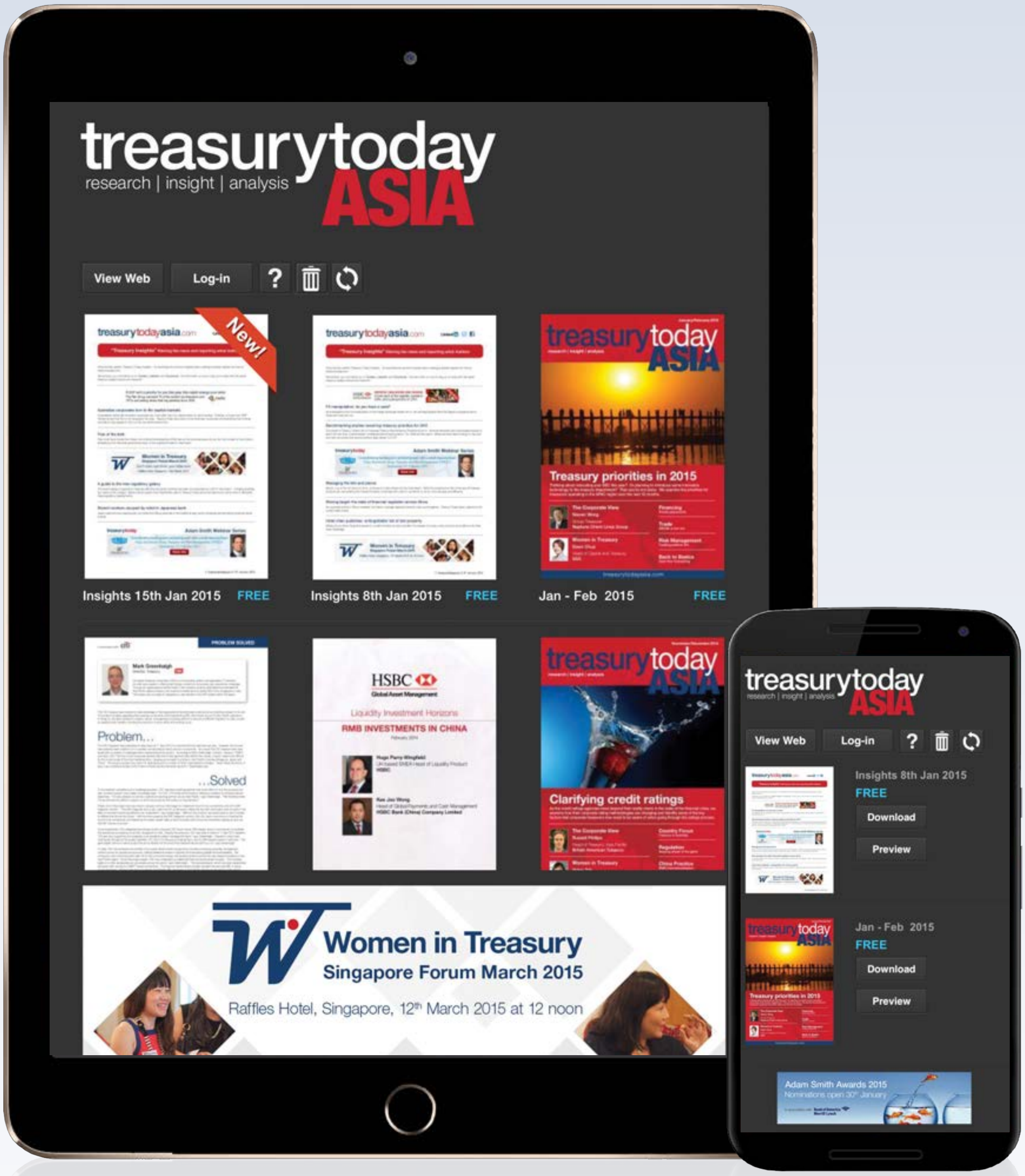
Monetary Authority of Singapore

Technology

Treasury in the cloud

Back to Basics

Accounting developments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Preview
Adam Smith Awards 2015

A step in the right direction

All eyes are on the Association of Southeast Asian Nations (ASEAN) as the ten-member bloc continues to work towards the creation of a single market. Designed to allow a free flow of goods, services, and investments, the ASEAN Economic Community (AEC) should also allow companies based in ASEAN to secure better access to raw materials, and to leverage a freer flow of capital and labour. In fact, a report released by the International Labour Organisation (ILO) and the Asian Development Bank last year suggested that the AEC could create 14 million new jobs and see the region's annual growth rise by 7.1% over the next decade.

In an effort to meet the 31st December 2015 deadline that has been set for the launch of the AEC, ASEAN finance ministers and central bank governors have recently signed a landmark agreement to allow member nations' banks to operate in each other's markets. They will also be accorded flexibilities similar to those of domestic banks in the host country.

The ASEAN Banking Integration Framework (ABIF), as the agreement is known, took five years to prepare and looks set to deliver numerous benefits, including greater access to secure funding across the region, and help to stem hot money inflows. Of course, as ASEAN moves closer to the realisation of the AEC, ABIF will also help to accelerate the pace of regional financial integration and boost cross-border trade and investment.

Before any ASEAN bank can begin to operate in another member's jurisdiction, regulators from both countries must agree on a set of rules that will bind the institution – which, if approved, will be known as a 'qualified ASEAN bank'. The aim of the collective finance ministers is to have at least one QAB up and running by 2018.

Talk of a single currency across the bloc surfaced again on the back of the ABIF, but has since been played down. In the words of Dr Zeti Akhtar Aziz, Governor of the Malaysian Central Bank: "We are too diverse and we don't have the preconditions for a single currency. We are going to approach it differently via financial integration to achieve the same objectives of greater growth, collectively."

And whilst full financial and economic ASEAN integration by the end of the year might be a stretch, for now, the ABIF represents an important step in the right direction.

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IN THIS ISSUE

treasurytodayASIA

Adam Smith Awards Asia 2015

sponsored by ANZ

Recognising the best in corporate treasury

NOMINATIONS OPEN 15TH JUNE

What are the Adam Smith Awards Asia?

As our Adam Smith Awards Asia programme enters into its second year, Treasury Today Asia are delighted to announce our partnership with ANZ for this year's awards. Our global events programme is reaching its next level and we are delighted to have ANZ's support in 2015.

The Adam Smith Awards Asia recognise best practice and innovation in corporate treasury within the Asia Pacific region. Nominations will open on 15th June 2015 and there are 15 award categories in total. If you believe your treasury team's work has gone above and beyond the call of duty, now is the moment to put yourselves forward.

Heralded as the father of modern economics, Adam Smith is the perfect representative for Treasury Today Asia's corporate treasury awards. His resounding influence can be felt today as much as at any other time in history, with his writings and analysis providing a stable platform for the modern economic era.

These awards are a celebration of those who, like Adam Smith, aim to push boundaries and think to the future. Whether through a project to restructure the company's cash pooling arrangements, embrace eBAM, or raise finance in new markets, these awards are about raising corporate treasury talent and innovation – regardless of budget, industry, or scale.

Why nominate?

The Treasury Today Group have been successfully running the Adam Smith Awards programme globally for eight years now. These awards are the pinnacle of best practice and innovation in corporate treasury and are an excellent way to demonstrate to senior management the value that treasury brings to the organisation.

The benefits of entering the Adam Smith Awards Asia extend far beyond collecting a prestigious trophy in November. Here are just three reasons why your organisation should be part of the action:

- √ Raise your treasury team's profile.
- √ Showcase innovation and thought leadership.
- √ Demonstrate excellence to your peers, partners, clients and investors.

How to enter

Nominations open on 15th June 2015. Everything you need, including the nomination form, can be found at treasurytodayasia.com/adamsmith. It is a simple case of completing and submitting the short form online – which should take no more than 15 minutes of your time.

Any number of solutions can be entered for consideration. A single project can also be nominated in more than one category, where appropriate. Nominations can be made by any corporate, and banks and service providers can assist their clients in completing the nomination form. Banks and service providers are also allowed to submit nominations on behalf of their corporate clients (with the client's approval).

All winners will receive an invitation to the Adam Smith Awards Asia Gala Presentation Lunch on 12th November at the Four Seasons Hotel in Singapore.

Should you have any queries please do not hesitate to contact us at awardsasia2015@treasurytoday.com

Top submission tips

Above all, our panel of judges will be looking for solutions that showcase the industry's best and brightest and demonstrate exceptional best practice and innovation in the Asian corporate treasury arena.

There should be evidence of true effectiveness and of how you as a company benefited tangibly from the project. Have you implemented a solution that has delivered or leveraged any of the following for example;

- Outstanding cost savings.
- Above average ROI.
- Optimal account/treasury structure.
- Quantitative improvements in efficiency.
- Cutting-edge technology.
- Exceptional implementation (budget/time).
- Quality accreditation.

Testimonials, figures, and any supporting documentation can be included with submissions.

The Adam Smith Awards Asia are open to companies operating in Asia Pacific (regardless of their home base which can be within or without the region). The examples of best practice nominated should be deals and structures that have been implemented or are in the process of being implemented in 2014 and/or 2015.

Please don't be dissuaded from submitting a nomination in the event you feel your company may not qualify for whatever reason. You do not need to be a major multinational to qualify. Focus on the problem that the solution you have implemented, or are in the process of implementing, addresses. Quantify the benefits, both qualitative as well as quantitative.

Award categories

- Treasury Today Asia's Top Treasury Team 2015
- Best Cash Management Solution
- Best Liquidity Management/Short-term Investing Solution
- Best WCM, AP/AR Solution
- First Class Relationship Management
- Best Trade Solution
- Best Card Solution
- Best Financing Solution
- Best Foreign Exchange Solution
- Best Risk Management Solution
- Best in Class Benchmarking
- Harnessing the Power of Technology
- One to Watch
- Best Solution in China
- Treasury Today Asia Woman of the Year
- A Rising Star
- Best Corporate and Social Responsibility Initiative

We at ANZ are proud to sponsor the 2015 Adam Smith Awards Asia.

As our industry continues to innovate and progress, we are delighted to support this respected benchmark for treasury talent that honours the many pioneers of corporate treasury across Asia Pacific.

Nominations open on 15th June and I invite you to rise to the challenge, submit your nomination and share your success story.

Carole Berndt
Managing Director, Global Transaction Banking
ANZ

Adam Smith Awards ASIA 2015

sponsored by ANZ

Women in Treasury Asia

proudly supported by Bank of America Merrill Lynch J.P.Morgan

Expanding inclusivity

Sunday 8th March 2015 marked International Women's Day (IWD) with thousands of events held across the globe to recognise the economic, political and social achievements of women. In this article, Treasury Today Asia looks at the wider debate surrounding the importance of diversity in the workplace and the achievements of our own Women in Treasury initiative.

Speaking at Treasury Today Asia's recent Women in Treasury Forum, held in Singapore in the week following IWD, Rachael Coleman, Director of MSD's Asia treasury centre, explained that, "gender diversity in the workplace is still such a big issue because of both perceived and real inequalities between men and women." Moreover, inequalities are not confined to the workplace, gaining access to the right social circles both within – and outside of – the workplace can be difficult for women.

In discussing the significance of gender equality, it should be considered as a concern for everybody, male or female. One problem is the stigma that is frequently attached to feminism: it has often been perceived as a divisive term and a controversial movement. These connotations can make it unappealing to be associated with and changing perceptions is both an imperative and a challenge. As Lauren Oakes, Head of Global Liquidity Sales in Asia Pacific for Goldman Sachs, explains "the workplace is a reflection of societal norms and beliefs; it's hard to change one without the other."

The change in outlook to an open-minded – and less divided – view that individuals should be recognised on their own merits (rather than on fixed gender stereotypes) is a laborious process, made more so when many companies lack diversity programmes. "Where much of society still struggles on this topic, is understanding the communication necessary and the openness to new perspectives and cultures required in order to harness the benefit of diversity," explains Shelly Maneth, CFO of ConneXions Asia, who attended the forum.

Workplace inequality

Today, the sad reality is that gender inequality still resonates loudly in the workplace. More than 100 countries have laws that restrict women's participation in the economy, in most regions working women are less likely to fill full-time positions and far fewer female executives and senior managers are employed.

Where progress has been seen, it is often sluggish and the struggle to significantly advance gender equality is slow. For example, the number of women in senior management positions globally only rose from 19% in 2004 to 22% in 2015 – furthermore, the proportion has declined in many countries since 2009 (including Canada, Mexico, Argentina, Australia, Germany and Singapore). If women's representation in the workplace continues at the current pace, female hiring, promotion and retention rates will be insufficient to adequately advance gender equality within the next decade.

Emblematic approaches

The good news is that, across the globe, comprehensive campaigns, industry specific initiatives and celebrations are raising awareness and inviting everyone to join the conversation on how to achieve gender equality. Shelly recognises the importance of Treasury Today's



Women in Treasury Forums as "they are a reminder of how much more needs to done to effectively promote diversity in the workplace." The outlook seems positive, discussing her experience at the recent forum in Singapore, Shelly said, "my key takeaway was a sense of hope – I love the fact we're talking about this, that people from major MNCs to small SMEs were represented; that there were men in the room during discussions; and that there were over 20 different nationalities and cultures adding perspectives."

When all parties involved understand the importance of equality initiatives, collaborative efforts can triumph. And since 78% of respondents to Treasury Today's 2014 Women in Treasury Global Study envisage finishing their career within a corporate treasury environment, it is increasingly important for their voices to be heard – alongside their male colleagues to shape that working space.

It is promising that recognition regarding the importance of collaborative efforts is increasing; one of the Forum's male attendees, Ivo Distelbrink, Head of Global Transaction Services, Asia Pacific, Bank of America Merrill Lynch, explained, "to address this broader issue at the enterprise level, by making changes to company policies and putting in place the structures needed to promote equality, gender needs to become a leadership issue rather than purely a women's issue."

Levelling the playing field

The Women in Treasury 2014 Study indicated major barriers to gender equality based on assumptions of aspirations, a lack of role models in senior positions and the continued existence of an 'old boys' network. Whilst the desire to encourage a beneficial and harmonious mix of identities in any professional environment is shared by most, whether to or not to approach the lack of diversity with quotas divides opinion. 38% of respondents to the study believe there should be a quota for female representation on boards and an equal amount disagree, with 24% unsure. These statistics demonstrated little change to 2013's study results yet the recent panel discussion held at the forum in Singapore saw all four members of the panel state that positions should be awarded based on merit – not quotas.

A recurring opinion is that of a general dislike for quota systems but an acknowledgement that they could, in certain circumstances, be necessary to kick-start integration in the fastest way. However, concerns from the 2014 Study also suggest that positive discrimination could be damaging for women in the long term due to the perception of achievements based solely on a 'leg-up'. According to Shelly, "if you see and understand the bias that exists in today's world, you'll recognise this necessitates the 'management' of diversity at this juncture." Currently, whether this 'management' should be dictated by numbers or left to the responsibility of businesses and associations is largely uncertain. In Asia, with the exception of Central Asian Kyrgyzstan's 30% female participation quota for parliament, the upper echelons of management have largely turned away from quotas. Even when quotas exist, their success is not guaranteed, it is estimated that 17% of companies listed on India's main stock exchanges failed to comply with new laws to appoint at least one female board director by the March 2015 deadline. At our forum, gender targets were put forward by the panellists as a potentially preferable option. This target can be judged by the extent to which diversity is embraced as the norm – where it is the pervasive culture in organisations.

All-encompassing

Discussions about gender equality often – and appropriately – open the dialogue on the importance of having diverse nationalities, age ranges, ethnicities (and so on) in the workplace. Although it is pertinent to reflect and celebrate female innovators, it is of equal importance to be aware that other identities could also require further recognition. Similarly to gender equality, problems surrounding prejudice must be tackled when striving for all-encompassing diversity in the workplace.

Deepali Pendse, Managing Director, Head of South East Asia Corporate GTS Sales, Bank of America Merrill Lynch, a panellist at the forum, explained that in her workplace, much is being done to eradicate unconscious bias. That is to say assumptions based on gender, race or any other characteristic about others that individuals can often hold but may not necessarily be entirely aware of. These expectations can unfairly affect our perception and judgement of others, but there are ways you can work towards removing the influence this bias may have over your decision-making process. "Therefore, it is about each and every manager – when hiring or considering promotions available – thinking about the bias held in their mind. By trying to remove and eliminate potential biases as much as possible, you actually give the job or promotion to the best person."

Panellist Sonia Clifton-Bligh, Director of Johnson & Johnson's Regional Treasury Service Centre, Asia Pacific, discussed the importance of nurturing diverse talent. "We all come to work with influences – our relationships, associations and experiences – and I think we should recognise them and take time to understand that people have something beyond what they present at work." Consequently, you can start to recognise people as individuals and, "as a manager, you can complement the dynamic by bringing a balance of members. Coaching and mentoring the skills from a diverse team, it's definitely a success factor for the organisation."




Getting heard

As is all too well known, success isn't certain. Christine (Jang) Tan, Managing Director, Regional Head MNCs Asia Pacific, J.P. Morgan explained in the panel discussion that "although there has been greater recognition of the challenges women face to promote inclusiveness – particularly in the areas that require greater flexibility (childcare, for example) – there is still some distance to cover". "Everybody is talking but you don't necessarily see statistics changing; creating diversity is a really tall order," affirms Chiew Bee Ng, Regional Treasurer for Tyco International Asia.

A topic which repeatedly comes up is what women can do to make their voice heard. The tendency for women to refrain from speaking up is often due to assumptions that they are being aggressive when they do, explains Lilian Sim, Head of MNC Regional Sales at J.P. Morgan. "Changing this perception is the responsibility of both organisations and individuals but will require time." What clearly gives women the confidence to be more vocal about inequality is each other. Discussing her experience at the Women in Treasury Forum, Marie Tyndall, Regional Treasury Manager for Johnson & Johnson, said that "by coming to an event like this, you can take some reassurance from the fact that you're not on your own. Hearing inspirational leaders speak about the concerns and challenges they experience along their career journey in treasury or finance, gives us all greater confidence that we can succeed, as we all experience very similar issues".

By seeing inspirational leaders speaking about shared concerns for women working in treasury or finance, greater confidence can be built." Similarly, what resounded with Lillian was the realisation that women, with the support of others, can empower themselves. "I think it will give women more confidence about what they should be speaking up for. If there's something that doesn't work for you, why not have a conversation with your management about alternative options? You could be pleasantly surprised." As Shirley Hiew, Treasurer, Asia Pacific, DuPont, points out: "To get ahead, you cannot do it alone – nobody can do it alone, we have to do it as a team." ■

E-invoicing

"Given the drive towards green business practice, is e-invoicing a technology that corporates in Asia should be embracing? If so, what recommendations can be made about successfully adopting e-invoicing solutions? Also, are there any specific developments in this space for treasurers to be aware of?"

James M. O'Neill
Senior Analyst,
Banking Group, Celent

While e-invoicing has been introduced in Asia with varying degrees of success over the past ten years or so, with the resumption of normal trade activities since the global banking crisis in 2008 and the near-completion of the ASEAN Economic Community (EC) programme during this coming year, now is as good a time as ever for corporates to examine opportunities for greater adoption of e-invoicing technologies.

As a group, the ten countries that make up the ASEAN EC enjoy an aggregate market size (in GDP terms) that exceeds three of the four BRIC countries, and while progress to date has been focused on the creation of a free trading zone within the ASEAN EC region, several bilateral trading agreements have been reached or are in process of negotiation within the greater region. Today, the European Union (EU) is the ASEAN EC's third-largest trading partner after China and Japan, and several individual member states have already negotiated bilateral trade negotiations with the EU. It is simply a matter of time before the ASEAN EC builds on these bilateral agreements to conclude block agreements with the EU and other important trading partners.

In this context, e-invoicing becomes an important strategic tool for Asian corporates that wish to take advantage of the new opportunities afforded by these free trade agreements. The UN Economic Commission for Europe has noted that e-invoicing in Asia is at a "nascent" stage, pointing to factors including the lack of a regulatory framework, a lack of industry standards, concerns regarding tax implications, and an overall lack of coordination amongst participants in the regional supply chain.

This is a regrettable situation for Asian corporates as trading partners in remote locations within Europe and North America are further along the way in terms of trade automation. In fact, some larger companies require their trading partners to send and receive critical information including invoices electronically. For the Asian corporates themselves, e-invoicing provides an opportunity to create efficiencies and reduce trading costs at several steps of the trading process. By linking billing systems directly to their accounting systems, corporates can reduce invoice preparation time, better ensure invoicing accuracy, and dramatically reduce the time of invoice delivery while also greatly improving delivery accuracy.

The leading corporates employ e-invoicing solutions that have real-time integration with their accounting systems, allowing invoicing to take place as soon as the goods or services have been delivered rather than having to wait for accounting personnel to manually push invoices to their trading partners. Ultimately, e-invoicing is part of a wider electronic ecosystem whereby both suppliers and customers are linked as well as the various banks involved in the clearing and settlement of funds relating to these trading relationships.

For Asian corporates who wish to benefit from the general uptake in regional trading that is expected to take place as the ASEAN EC vision becomes a reality, the time for upgrading to modern billing and collections processes is now.

John Pierce-Jones
Head of E-Invoicing,
Technology, Fundtech

Electronic invoicing is growing in Asia, setting a trend that will continue into the future. Corporates in Asia can look to electronic invoices not only for greener business practices, but also as an opportunity to eliminate the cost and inefficiencies of paper-based invoices, ultimately leading to more efficient processes within the treasury for more efficient payments. Each year, corporations worldwide send and receive millions of invoices and bills. Manual processing of these invoices is not only slow and error-prone, but also costly. Furthermore, inconsistencies in invoice formats from country to country can cause inconvenience for cross-border and global corporations. Customer demand for electronic invoicing is also on the rise, with many looking for digital versions of their invoice data for direct input into their accounting systems.

E-invoicing and e-billing systems centralise all of the components of this process to facilitate communication, dispute management, auditing, and reporting all in a single system. This eliminates the manual labour and costs associated with printing, mailing, archiving, and reconciling paper invoices. Potential for benefits in Asia is expected to manifest similarly to Europe where, according to a 2014 Billentis report of the public sector, savings could be €40bn. However, today less than 10% of invoices in Europe are electronic, signaling immense opportunity.

For corporates that speed up the billing process for receivables by sending their invoices electronically rather than on paper and then manage them online, instant delivery together with query management tools can lead to faster settlement and reduced Days Sales Outstanding (DSO).

Furthermore, standardised billing across all regions ensures the customers of corporates benefit from the same invoicing format and same level of service in every country; something of particular value for corporations that do cross border and international business. The opportunity to post invoice data on a central hub and make this information available to all customers online empowers them to monitor, track, search, and query their invoice and payments status.

On the Accounts Payables (AP) side, corporates can accept supplier invoices in any format straight into their e-invoicing hub which reduces manual input, eliminates errors and helps to drive down costs. There is also the option for AP departments to make an instant switch from paper to electronic by utilising a 'Paper-to-Data' service. Whether a company processes invoices by mail, email, EDI or other electronic channel, the data is captured, validated to agreed business rules, approved by nominated users and finally uploaded to an ERP or accounting system. Getting the invoice approved more quickly maximises the opportunities for taking advantage of Dynamic Discounting or Early Payment Discount schemes.

Treasurers may then also consider implementing more automated workflows and online payment options to streamline processes further. The added ease of billing or invoicing can contribute significantly to relationship satisfaction between the corporate and its customers and trading partners. While environmental issues remain important drivers, the move away from paper is being further accelerated by legislative and regulatory changes with 13 countries in Asia either having already mandated or intending to mandate electronic invoicing following government initiatives.

Amit Sharma

Managing Director, Head of eCommerce and Channels Asia Pacific, Global Transaction Services, Bank of America Merrill Lynch

As is the case with numerous digital initiatives in the Asia Pacific (APAC) treasury management space, e-invoicing is a work in progress amongst the region's corporates. It is however an industry migration that we have great confidence in and we believe adoption will grow. Aside from clear efficiency and risk management advantages, we see the added benefits of e-invoicing as consistent with the greener business practices embraced by forward-thinking corporations regionally.

However, for e-invoicing to transition from niche usage to mainstream treasury practice, several moving parts need to converge. Sending invoices electronically to the customer is one piece of the puzzle. Ensuring confidentiality and security is another pivotal consideration, and brings various parties into the wider picture. Hence, at the transaction level, the invoice issuer, receiver, processor, auditors (internal/external) and internal IT teams must play a role for e-invoicing to gain traction in APAC.

At the most immediate level, challenges exist on the audit front. In our conversations with clients, it is clear that internal corporate audit teams must be geared to accept electronic invoices and that this part of the process is a challenge that still needs to be broadly resolved. Furthermore, there is the mind-set battle across the treasury function whereby shifting attitudes from 'pushing paper' to 'clicking data' requires a wider acceptance from various internal and external parties. Also, concerns such as fraud, duplicates and authenticity remain open issues within many discussions around e-invoicing.

So what are the short-term solutions? In our view, the success of e-invoicing will rely heavily on the adoption of digital signatures. There are several factors underscoring the importance of digital signatures in the broader e-invoicing picture. Firstly, the relationship between invoicing and tax implications must be considered. This is especially true given that there are restrictions in Asia governing digital delivery of invoices in several markets. For example, China and India either have specific guardrails around e-invoicing, or in the case of the latter, do not permit the practice at present. As a result, many corporations have taken to sending a PDF copy of the e-invoice to their customers to perform digital scanning and improve the AP process via the PDF invoices. In parallel, they also send the physical copy of the invoice. With practices such as the aforementioned processes common in the market, we take the view that a legal framework governing digital signatures would have the potential to better protect participants and drive e-invoicing adoption.

The good news is that progress is clearly being made on the digital signature component. In Thailand and the Philippines, electronic invoice presentment and Payment (EIPP) is quite popular and the local banks are hosting the EIPP platform, and mainly providing distributor/dealer financing. However, this is still not addressing the end-to-end requirement of eliminating the need of sending paper invoices in these markets, unless there is a legal framework, to say the invoices hosted out of the EIPP platform can be downloaded by the customer as the true cope of the invoice. Moreover, if governments can start to adopt business to government (B2G) invoicing this is still not addressing the end-to-end requirement of eliminating the need of sending paper invoices in these markets and requires a more defined legal framework.

Once the digital standard of the invoice is agreed, ERP vendors will then embrace the platform and provide standard integration. This is the trend in EMEA where governments are adopting e-invoicing as standard which has ultimately led to the market quickly embracing it. From a long-term perspective, we take the view that to have an agreeable industry standard for transmitting the invoices in a digital format support is needed by suppliers, buyers, banks, technology providers will help increase the take up of e-invoicing. In APAC, there is still plenty of work and consideration at the government level to be done, but the right moves are clearly taking place. One thing is crystal clear though, only partnership across business functions will ensure the success of the APAC e-invoicing drive. ■

The next question:

"What value do banks' Know Your Customer (KYC) processes really add for corporates? And how will utilities help to improve the KYC process for treasurers? Also, I have heard talk of a growing trend around Know Your Customer's Customer – what impact will this have for corporates operating in Asia?"

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

Western regulations roam East

Companies and financial institutions across Asia face an increasing challenge in complying with regulations formulated on the other side of the world. Here, we consider the extent to which regulations such as EMIR, Dodd-Frank and FATCA have impacted the region and examine the intended (and unintended) consequences for treasurers and their banking partners.

The regulatory challenges facing companies in Asia are manifold. As a result, the cost of compliance in the region is high – and new regulations are pushing this up even further. According to the most recent Thomson Reuters Cost of Compliance Survey, 29% of Asian firms spent more than ten hours per week tracking and analysing the impact of regulatory developments in 2014, up from 21% in 2013. The equivalent figures for US and UK firms in 2014 were 25% and 21% respectively.

When it came to the number of companies whose compliance teams were spending more than seven hours per week amending policies and procedures to reflect the latest regulatory rules, the disparity between Asia and the US and UK was even greater: almost three in ten (29%) of Asian firms fell into this category last year, compared with 23% in 2013. Only 19% of US firms and 17% of UK firms spent more than seven hours per week amending policies and procedures in 2014. So which regulations in particular have been piling on the pressure in Asia?

Global OTC derivatives

Derivatives reform has been one of the headaches. For example, reports that the International Swaps and Derivatives Association (ISDA) asked the Basel Committee on Banking Supervision and the International Organisation of Securities Commissions (IOSCO) to delay derivatives trading reforms highlight the specific challenges of implementing new rules beyond the US and Europe.

In mid-2014 the Australian Securities and Investments Commission (ASIC) launched a consultation on proposed changes to trade reporting rules and the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission in Hong Kong began a consultation on requirements relating to mandatory reporting and related record keeping obligations. The Securities and Futures (Amendment) Ordinance 2014 was enacted in March 2014, which provides a broad regulatory framework for the over-the-counter or OTC derivatives market in Hong Kong.

The new regime introduces mandatory reporting, clearing and trading obligations of OTC derivative transactions in line with G20 commitments in reforming the global OTC derivatives markets. It is expected that mandatory reporting and related record keeping obligations will be introduced into the Hong Kong Legislative Council for vetting in the first half of 2015. The rules will become effective upon the completion of the vetting process.

"Our current priorities are to consult on the first phase of mandatory clearing requirements and the expansion of the product scope of mandatory reporting," explains a HKMA spokesperson. "We will deal with reporting requirements on other entities afterwards."

Australia's rules relating to mandatory reporting of OTC derivatives have already been enacted. In February, ASIC amended its derivative transaction rules. Sonia Goumenis, Partner at Australian commercial law firm Clayton Utz, says the G20 agreement to improve transparency in the OTC derivatives market has had a significant impact in the country, particularly on banks that are well entrenched in the cross-border OTC derivatives markets. This is either by virtue of being physically present in those jurisdictions and booking trades through overseas branches, or trading with counterparties (clients) located in foreign jurisdictions and therefore possibly being caught by regulations in those jurisdictions.

"To some extent, ASIC has borrowed heavily from the regulatory approach in the US and across Europe," adds Clayton Utz's John Tawadrous, a lawyer with experience working on the OTC reform programme at one of the major Australian banks while on secondment last year.

Other Asian jurisdictions which are not members of the G20 have been guided by its recommendations in terms of mandatory reporting and clearing as well as capital requirements for non-centrally cleared trades according to Tom Jenkins, Partner at KPMG China. "Countries in this region with an OTC derivatives market – including India, China, Japan, Korea, Malaysia and Singapore – have initiated reforms, with an initial focus on mandatory reporting.

"Japan is probably furthest down the line in terms of OTC derivatives market reform in Asia. The country has implemented mandatory reporting and some mandatory clearing since November 2012 and indicated that mandatory trading on electronic platforms will be introduced by September 2015." Jenkins observes that the range of instruments covered by the first phase of mandatory reporting and clearing is more limited in Asia than it was in either Europe or the US. But he also points to the fact that Hong Kong and Australia in particular are not that far behind their Western counterparts, while China introduced mandatory clearing for interest rate swaps much more quickly.

Dodd-Frank

PwC's Asia Pacific Financial Services Risk Leader, Chris Matten, says Dodd-Frank has created a knock-on effect across the region. US banks operating in Asia face restrictions on proprietary trading; this has forced some to consider their booking models to see whether certain transactions can be booked through an Asian subsidiary. In particular, the Volcker provision of Dodd-Frank has forced banks to look at where transactions are booked.

Many Asian financial institutions do not trigger the thresholds for the Volcker Rule to apply, so only a few would be challenged by the requirements explains Akihiko Katayama, Director at AlixPartners. "But for those impacted, some have implemented very complex manual processes that have added operational risks and unnecessary costs."

According to Niall Coburn, Regulatory Intelligence Expert at Thomson Reuters, many corporates across Asia remain uncertain about how EMIR and Dodd-Frank affect them. There are also some questions in relation to requirements around additional registration, reporting and documentation and the circumstances that firms have to act upon in order to be compliant. "The most significant outcome in terms of documentation following years of regulatory activity in the US and EU manifests itself in the form of protocols to which certain counterparties are bound to adhere to when entering into certain OTC derivative transactions.

"Hong Kong and Singapore appear to have both brought their regulations in line with the major jurisdictions with a 'substituted compliance' approach. As a result of EMIR and Dodd-Frank, the Singapore, Hong Kong and Australian markets have handled these new complex regulations and appear to be operating effectively."

Levels of preparation

One regulation for which Asian financial institutions have been well prepared is Basel III. Stricter capital requirements are nothing new to those banks in the region who experienced the Asian crisis of the late 1990s. Matten explains that there are a number of Asian countries (including Japan, Hong Kong, Singapore and Indonesia) that are full members of the Basel community. "Historically, many regulators in the region followed the provisions of Basel – albeit with a slight delay. Banking is a global business and if you are a jurisdiction that is not part of this community it makes sense to follow the provisions around capital adequacy."

Coburn observes that Asian regulators, as well as the region's financial institutions, have made considerable progress towards implementation of Basel III. Asian banks are well poised to meet its requirements and most regulators in the region have indicated their acceptance of moving towards standard rules on the basis that it will make their institutions more resilient against a financial crisis.

However, he also suggests that it is difficult for regulators to finalise policies when the Basel Committee is still consulting on some of the most important areas, such as the capital floor framework which will affect central issues such as capital ratios and relevant risk-weighted model calculations. "Since the G20 Brisbane Summit, regional regulators have been working together and accepted the need to have an improvement in consistency and comparability in bank capital ratios and an improved approach in calculating internal risk-weighted ratios that have, in the past, have been inconsistently applied.

"In Asia, the banks appear to accept that higher bank capital is inevitable to assist them in improving their resilience to any future financial crisis. The only question remaining is what those ratios will be and the outcomes of the current Basel consultation in relation to capital framework."

In Australia, the Financial System Inquiry Report (published in December 2014) had already foreshadowed the need for banks to adjust their capital ratios to ensure the financial system is less likely to be dependent on government support in the event of any failure. This report has been accepted as a working benchmark for other governments and regulators in making their markets more efficient and secure.

Remaining legwork

According to Coburn, Asian regulators respect the work of the Financial Stability Board and the Basel Committee – but they also recognise that it may take some time and patience for reforms to be implemented. This does not mean to say that Asian banks don't feel hard done by. Asian financial institutions have frequently pointed out that having been better capitalised they were not impacted by the global financial crisis – so why should they have to accept the same measures as European and US banks? "Having said that, Singapore always had higher minimum capital requirements than the Basel framework and continues to do so," adds Matten.

AlixPartners's Katayama agrees that most Asian banks are in relatively good shape with regard to Basel III requirements. In his view, liquidity requirements are more of a challenge, with holding sufficient liquidity and daily liquidity reporting continuing to be major challenges. Michael Brevetta, Head of US Regulations at PwC, says that on the issue of FATCA compliance, a good deal of work remains to be done. "For example, banks in countries that don't have inter-governmental agreements in place (such as Vietnam) may have had issues fulfilling reporting requirements." Financial institutions across Asia are still reviewing pre-existing accounts. "This is a process that could last into 2016."

Foreign financial institutions (FFIs) in Asia have been advised to review customer activity dating back to mid-2008 and beyond to ascertain whether they may be exposed to the scrutiny of US tax authorities based on information that may already be in the hands of the US Internal Revenue Service (IRS) or the Department of Justice (DOJ).

An additional complicating factor is that many Asian countries which have reached agreements with the IRS have yet to release guidance for local financial institutions. "International banks are very focused on FATCA and are mostly compliant with the legislation," says Coburn. "There have not been any violations or investigations that I am aware of that would indicate that regional firms are not complying."

Knowing your procedures

On the question of the extent to which 'Know Your Customer' (KYC) and anti-money laundering (AML) regulations are being effectively implemented across Asia, Neill Poole, Executive Director at AlixPartners, says financial institutions are constantly trying to recruit staff for their AML teams and asking for help with training. "This suggests to us that not all companies are ahead of the curve. As in other parts of the world, the region is seeing financial institutions abandoning certain classes of customer on the basis of perceived risk.

"However, this only serves to drive such business into less regulated sectors, which can have a detrimental effect overall on effective implementation of AML regulations." Poole believes that effective anti-money laundering regulations require a risk-based approach, whereas some financial institutions are applying a rule-based or 'tick the box' approach in order to ensure they comply with local regulations.

"This can result in the units responsible for investigation of suspicious transaction reports being overloaded with reports of largely innocent transactions. Until all financial institutions get to the stage where they can single out genuinely suspicious transactions more successfully from the surrounding 'noise' of legitimate transactions, implementation of AML regulations will not be truly effective."

The challenge in applying KYC processes and anti-money laundering rules effectively across Asia is that they are principles-based, adds Matten. "Even if the rules have not changed, the regulators' interpretation of what they mean in practice can shift significantly, which makes it difficult for institutions to know whether they are compliant."

According to Coburn, Asian financial institutions and firms have taken compliance with the anti-money laundering and counter-terrorist financing laws very seriously. "There is also increased emphasis on beneficial ownership. Even countries such as Malaysia are taking a heightened compliance approach given the rise of ISIS funding from the region.

"Asian regulators have introduced enhanced requirements over the past few years and anti-money laundering professionals in the region are also growing more concerned about how regulatory challenges will affect their business." AML compliance has become more focused in the past five years and regulators are now pressurising financial institutions and firms to make sure they meet best practice standards.

Fit for purpose?

When determining whether Asian regulators have been proactive in terms of implementing Western regulations and/or developing regional regulations, Coburn refers to an opinion that European regulations do not necessarily fit into the financial market structure in Asia; most of the obligations are brought about by the presence of global institutions.

"There is, however, an over-arching acceptance that international best standards are the way forward to ensure that institutions are more resilient and are more able to face another financial crisis. Hong Kong, Singapore and Australia have led the way in ensuring that the financial sector adheres to cross-border regulatory requirements. In some respects, they have a more focused vision of what works in the Asian region than regulators in Europe and America."

China has indicated that it is striving to meet international best practice in many regulatory areas and Japan has introduced a new corporate governance code for listed companies in line with international best practice. "It is fair to say that Asian regulators are playing an important part in promoting international governance through the Financial Stability Board, the Basel Committee and IOSCO, which will also help enhance regulatory and financial stability in the region," adds Coburn.

But while Asian regulators have made progress elevating the awareness of the need for more effective compliance among financial institutions, many Asian jurisdictions still lag behind the US and UK, concludes Poole. "If Asian regulators want to drive change and implement a robust culture of compliance among their constituents, they should consider holding individual members of boards of directors responsible and accountable in order to achieve the right 'tone from the top'.

"Though continual progress is being made, it won't be clear how deeply rooted these initiatives are within organisations until regulators enforce their policies as vigorously as some of their Western counterparts." ■

Five key strategic areas of focus for successful treasury leadership in 2015

Persistently low interest rates have fuelled a record-high disconnect between debt and equity, an increase in capital markets activities and growing investor appetite for return on capital. A slump in crude oil prices in early 2015 and volatility in foreign exchange (FX) markets, such as the US dollar's ongoing strength against the euro, have illustrated the magnitude of today's headwinds and the need to avoid complacency.

Since instability in developed markets often disproportionately impacts developing markets, corporate treasurers in Asia Pacific will need to make tactical decisions that demonstrate their ability to play a strategic role in their organisations.

Asia Pacific volatility expands

Macro economic environment

Central bank policies on interest rates in the US, UK, Europe and Japan that have long been quite similar are now diverging. Europe and Japan are expanding quantitative easing at the same time the US and the UK are pulling back.

Global currencies are showing tremendous volatility, fuelled by central bank decisions — in January, Switzerland's central bank abandoned its cap on the Swiss franc's exchange rate against the euro, throwing global FX markets into turmoil[1].

Oil prices also surprised the market by dropping below USD 50 for the first time since the financial crisis, and this drop will continue to have a major impact for most companies in 2015. Oil deflation could potentially have a greater impact on economies than fiscal or monetary policy.

Corporate finance

Corporates have maintained conservative balance sheets even amid the financial crisis recovery, with cash rising from 8.3% of assets in 2008 to 12.7% in 2013 and net debt dropping from 20.8% of enterprise value to 10.9% over the same period.

High internal hurdle rates, averaging 18% among a sampling of S&P 500 firms, are one driver of the cash accumulation. The rates reflect a higher risk-averse disposition towards long-term investments in an uncertain environment.

As a result, activist investors, particularly hedge fund managers, have put further pressure on corporates to acquire or spin off companies rather than stockpile cash and maintain a balance sheet with low-yielding assets.

Regulatory landscape

Regulatory changes, such as those that resulted from Basel III, are often viewed as primarily affecting banks. In fact, they have a major impact on corporates, as the increased costs of regulation lead to higher-priced bank services and a lower supply of credit.

To fuel growth in their own markets, regulators in Asia are taking significant steps toward deregulation and/or liberalisation. Regulators in China further liberalised the market in November 2014, making cross-border sweeps easier and documentation simpler. India allowed Indian subsidiaries to access funding from their international affiliates.

Regulators are also making changes to attract Regional Treasury Centres (RTCs) in certain Asian markets. Hong Kong amended its laws and announced plans to introduce attractive tax incentives, China de-regulated its policies in free trade zones, and policymakers in Malaysia and Thailand relaxed regulations to provide incentives to attract treasury centres in their markets.

Technology trends

Technology is changing significantly as countries and corporates strive to become more efficient. Across Asia Pacific, the trend is toward standardisation, including the use of SWIFT, electronification through sophisticated clearing centres and leveraging mobile penetration to solve last-mile access issues.

Developing countries throughout the region are upgrading their systems from a basic clearing and settlement infrastructure to more efficient digital treasury technology, such as the China National Advanced Payment System (CNAPS) II and an innovative real-time payments platform in Singapore, known as FAST.

Corporates are also enhancing their infrastructure, with many moving to bank-agnostic technology such as the industry standard ISO 20022 format and the SWIFT network. With a focus on treasury management systems, corporates are taking advantage of banks' investments in innovative solutions in mobile and smart banking.

Navigating 2015: a treasurer's focus

In this dynamic environment, the fundamental short-term and long-term roles of the treasurer in optimising capital and mitigating risk, while increasing operational efficiency and ensuring sufficient control, remain the same. Treasurers look to achieve these objectives by managing cash and funding working capital and capital expenditures, and at the same time, aligning capital structures by achieving the right balance between debt and equity in capital markets.

What has changed, however, are the key actions and decisions treasurers will need to take because of external factors described above. Based on that, we believe most treasurers will prioritise five key activities in 2015.

1. **Create an effective hybrid centralisation model**

To establish the appropriate treasury structure, it is important to fully understand the business drivers, from sourcing and production to how the firm manages fund flows back to the region or repatriate funds to the parent company. It is essential for treasurers to strike the optimal balance between centralisation and decentralisation by understanding what should be centralised to maximise the benefits of an RTC or in-house bank and what needs to remain local.

Particularly in Asia, where infrastructure and regulatory frameworks diverge between markets more than in other regions, achieving an optimal balance between global consistency and local flexibility is of utmost importance.

2. **Diversify sources of funding**

Amidst regulatory changes that may lead to price increases or decreases in credit supply, as well as interest rate hikes, treasurers need to identify sources of funding for both normal business activities and new opportunities. This role, and their deep understanding of the needs for supply chain and working capital funding, are critical because their assessment affects the corporate strategy and determines which projects can be funded.

It is also important for treasurers to target a capital structure that provides financial flexibility to fund growth and prioritise sustainable long-term opportunities. Strategies for successfully managing funding include diversification of sources of funds, optimising excess cash through fee offsetting, spreading maturity dates, and 'just-in-time' funding.

3. **Optimise operational efficiency**

Technological advances such as enhanced Enterprise Resource Planning (ERP) and standardisation enable treasurers to work more efficiently, ensure more effective processing and perform previously-error-prone manual tasks accurately in minutes rather than days. Benchmarking against leading players allows treasurers to critically evaluate the current situation and to better plan their operational efficiency journey.

With the help of technology and information systems, treasurers can apply their skills more effectively by channeling their time and resources into value-add activities and utilising intelligent tools for analytics in order to support and achieve their objectives in the operational efficiency journey.

4. **Develop an enterprise-wide risk agenda**

Given the increasing scope and complexity of regulatory and policy changes both regionally and globally, treasurers can only manage across risk categories well if they fully understand the entire business and what is driving risk. Traditionally, treasurers have focused on FX and liquidity risk. There is now a need to think about combined exposures.

It is also important for treasurers to forecast and manage risk more dynamically and proactively, exploiting their deep understanding of the business to formulate strategies to tackle root causes of risk, rather than hedging against temporary conditions. These include taking a holistic view when looking at changes in the world and counterparties, and devising a sustainable risk management strategy.

5. **Prepare for shareholder activism**

With the rise of shareholder activism and the pressure of bringing increased value to the table, companies are constantly looking at ways to better manage their cash and take advantage of low borrowing rates for mergers, acquisitions, capital expenditures and spin-offs.

Although treasurers do not actively make decisions on acquiring or divesting, they need to be in a position to act swiftly to integrate or adjust core treasury operations based on changes that may arise. Planning ahead ensures an effective funding approach for such activities to readily integrate core treasury operations seamlessly under tight timeframes.

Thriving in 2015

In light of high uncertainty and increasing volatility, corporate treasurers in Asia Pacific have greater opportunities than before to play a key role in achieving corporate objectives and demonstrating their strategic value to the firm. By focusing on these five priorities, treasurers can enhance the competitiveness of their company and ensure they are well prepared to take advantage of any opportunities that come their way. ■

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[1] "Swiss Move Roils Global Markets," Jan. 15, 2015, *Wall Street Journal*.

Location, location, location

As more and more corporates decide to establish a treasury centre in Asia, the competition between the different locations is heating up. In this article we look at the different considerations for corporates when picking a treasury centre location in Asia and also analyse how the big three – Singapore, Hong Kong and Shanghai match up.

It is no secret that, for many corporates, Asia represents a tremendous growth opportunity. Yet, the varying stages of development across the region and the complex regulatory landscape also represents a significant challenge for treasurers. Therefore, as European and US multinationals have grown their operations in the region they have often found it tough to manage cash remotely. To address this, many corporates have looked to centralise and establish a treasury centre in Asia in order to have a permanent treasury presence in the market and gain greater visibility and control over their cash flows.

Of course, centralisation doesn't suit everyone, but if that is the path that the organisation wishes to follow, the next decision to be made is where to locate the treasury centre. Historically, for those operating in Asia, the choice has been between the region's two key finance centres: Singapore and Hong Kong. The former was typically selected by those companies with a primary focus on South East Asia and the latter for those whose key presence was in North Asia, especially China. Today however, the choice is more complex as both the established and aspiring locations are locked in fierce competition to attract more treasury centres.

Key considerations

The decision-making process behind where to locate a treasury centre is multi-faceted, and all locations have positive and negative aspects, meaning that in many respects there is no correct answer. But there are some key considerations that must be taken into account when selecting a location. The first – and perhaps most important – is the overall strategic philosophy of the organisation: where are its key markets and where does it want to grow, for example? This initial assessment is likely to remove a number of locations where it wouldn't make sense for the company to site the treasury centre, leaving a shortlist to be more deeply analysed.

The granular analysis of the shortlist should then focus on all the different factors that will have a significant impact on how the treasury operates and the advantages and disadvantages of basing the treasury centre in a particular location. A study recently conducted by EY asked over 300 corporates about their key considerations when selecting a location to establish a treasury centre.

Unsurprisingly, the regulatory environment (including FX controls) was highlighted as the most important factor. The second consideration highlighted was the cost and availability of talent, followed by the tax environment, political stability and access to capital markets. Other factors that didn't make the top five, but were still considered important, include the location's legal system, banking costs and capabilities, operating costs and also the living environment.

So how do the various locations in the region compare?

Singapore

As well as being one of the world's prominent financial centres, Singapore is also the region's premier treasury centre location. "Its business-friendly environment, deep and well-educated talent pool and best-in-class infrastructure have made it the regional hub for the majority of Western multinationals," says Victor Penna, Head of Treasury Solutions, Transaction Banking at Standard Chartered. "It has therefore made a lot of sense for organisations over the years to base their treasury centres in the city."

Singapore benefits from a liberal regulatory environment, an excellent sovereign credit rating, a deep and liquid FX market and a legal system based on English common law. The city's status as a financial centre also allows treasurers access to best-in-class banking services, with most, if not all of the major Western and Asian banks having significant operations in Singapore.

On top of this, Singapore offers corporates a strong incentive package to locate their treasury centres in the city in the shape of its Finance and Treasury Centre (FTC) award. The FTC offers qualifying corporates a concessionary tax rate of 10% on all fee income received from treasury activities and an exemption from withholding tax on interest payments. Further tax benefits can be gained through Singapore's double tax treaty network, the most developed in Asia, reducing the withholding tax applied when carrying out functions such as intercompany lending and cash pooling.

The city-state is also considered a prime location for finding talent. Its history as a former British colony and its position as a regional hub for many multinationals means that it has developed a deep and well-educated English-speaking pool of talent. This is bolstered by talent from neighbouring countries across Asia, meaning that it is easy to find the language skills required to manage the diverse region. The city is also attractive when looking to bring in talent from overseas: "moving to Singapore is much easier than some other locations in Asia from a family perspective," says Amit Sharma, Managing Director and Head of eCommerce and Channels, Asia Pacific at Bank of America Merrill Lynch (BofAML). "Thanks to its strong international schooling system and best-in-class transportation links to the rest of Asia as well as key locations in Europe and the US."

The overall strength of Singapore as a treasury centre location for global and Asian MNCs (ex China and Hong Kong) is underlined in EY's study. For all but one of the key considerations for corporates when choosing a treasury centre location, Singapore ranked above its competitors. The only area it fell short was because of its high operating costs which is unsurprising given the city's status as the world's most expensive.

Hong Kong

Hong Kong offers a similar proposition to Singapore. The territory has a business-friendly environment, and in 2015 was again ranked the 'world's freest economy' – an accolade it has held for over a decade. The territory has a legal system based on English common law and a liberal and well-developed regulatory framework. It has a deep, well-educated, international talent pool and also, similar to Singapore, boasts a best-in-class transportation infrastructure that supplements its position in the geographical centre of Asia.

Its status as Asia's other key financial centre means that corporates have access to a wide range of banking services, with 157 foreign and local licensed banks operating in the territory. Hong Kong is also the world's largest offshore RMB centre and a key gateway into the international capital markets, making it a favourable location from which to raise capital.

"One area where Hong Kong has lagged behind Singapore is its tax regime which does not have as many double taxation agreements, nor extends concessions to companies with treasury centre activities," says Sandip Patil, Managing Director, Asia Liquidity Head at Citi. The imbalance has meant that often the tax payment on intercompany loans are larger than any interest profit earned or acquired – a big consideration when establishing a treasury centre that will be making lots of these transactions. "The 2015/2016 budget has looked to remove this imbalance in taxation and encourage a corporation to operate a treasury centre in Hong Kong, bringing the territory's incentive package in line with Singapore," says Patil.

With such a similar environment to Singapore, Hong Kong has proved a popular treasury centre location, outside of mainland China, for Chinese multinationals that are expanding out across the world. As EY's study highlights, Hong Kong was voted as the top location for seven out of ten key factors when selecting a location for a treasury centre by Chinese and Hong Kong MNCs.

"Companies that set up a treasury centre in Hong Kong, primarily do so because they have a significant presence in China," says Standard Chartered's Penna. It has been argued that unlike Singapore, where treasury centres have more of a regional focus, treasury centres in Hong Kong tend to be more China-centric and the market is set up as more of a gateway to China. In this respect, the territory's biggest advantage may also be its biggest disadvantage when it comes to attracting a wider range of treasury centres that wish to cover the region as a whole.

This has however seen Hong Kong attract treasury centres from multinationals for whom China has become their key revenue driver in Asia. American multinational Johnson Controls is one such company that has moved from Singapore to Hong Kong. "When the company first moved into the region our key areas of growth were Australia and South East Asia," says Marc Vandiepenbeeck, APAC Corporate Treasurer at Johnson Controls. "It therefore made sense to set up the treasury centre in Singapore." However, as China began to be of material importance, and business weakened elsewhere, the company reconsidered its location.

"Ideally we wanted to move to mainland China, but in 2006 the regulations were such that it wasn't practical, so we decided to set up in Hong Kong as a gateway to China."

Shanghai

Shanghai and China more broadly, is now a very different proposition for corporate treasurers than it was in 2006. The rapid pace of deregulation and modernisation has changed the treasury landscape and made Shanghai a realistic contender for multinationals deciding where to establish a treasury centre.

Johnson Controls, for example, has recently announced plans to move its Asian treasury centre from Hong Kong to Shanghai. "The company is establishing a corporate headquarters in China that will have equal authority to the headquarters in the US. And while there are still challenges when it comes to operating a treasury centre in Shanghai, they are no longer significant enough for the function to be left behind in Hong Kong," says Vandiepenbeeck.

Before analysing the challenges that corporates still face in Shanghai, what have been the positive steps that China has made? Deregulation, boosted by the Shanghai Free Trade Zone, and then rolled out nationwide has been at the heart of the changes. For example, corporates are now able to plug the country into a global cash management structure and move cash in and out of the country without much restriction – a must for any treasury centre.

"China is also taking other important steps," says BofAML's Sharma, "for example the authorities have digitised the execution of FX payments. While this may seem a small change, it highlights that the regulatory easing is continuing and China is committed to making it easier for both corporates and banks to operate." China's position of 90 in the World Bank's Doing Business survey, does however highlight that there is still a long way to go before China is as business-friendly as Singapore and Hong Kong.

Nevertheless, Shanghai is set to change further over the coming years as the government aims to establish the city as a global financial centre by 2020. Currently, the banking landscape in China is dominated by the big five state owned banks, but over 412 foreign institutions have operations in the country. Forty one of these are locally incorporated, as a result of the sector opening up further in 2006, allowing these institutions to offer a wider range of products and services to corporate clients in China. This has been an important step, as Vandiepenbeeck explains: "historically in China, the banks have been able to support us domestically but not so much regionally, as the quality of personnel wasn't there. This has now changed drastically as the big multinational banks have invested significantly in the country and have bankers that can support our operations across Asia Pacific."

While the talent in the banking sector may now be at a high level in Shanghai, can the same be said for treasury? According to the EY study, the answer is not quite yet, when compared to Hong Kong and Singapore. "This is a key area for Shanghai to focus on," says BofAML's Sharma, "the city is growing as a treasury hub but to continue this momentum it needs to build the global talent pool and quickly." For Sharma, this is a big task because of the ease of a family moving to Singapore and Hong Kong. "These locations have a large global expat community, English is a native language and there is a strong international school system, making them much more attractive locations for families.

Shanghai is also lagging in other areas. For example, it does not offer an incentive programme to match that offered by Singapore and Hong Kong. The infrastructure in Shanghai is also behind that of Singapore and Hong Kong, meaning that travelling in and out of the city can be a challenge. Also, the legal system may not be familiar to corporates outside of China, requiring experts in local legislation to be hired to resolve any legal issues.

So will Shanghai become the primary treasury centre location in Asia in the near future? For Standard Chartered's Penna, this remains to be seen: "it will depend on how aggressively China continues to liberalise, how quickly Shanghai becomes a global financial centre and also how other regulation and incentives develop. Ultimately, if Shanghai can offer a proposition as good as, or close to, what Hong Kong offers, then those corporates with a critical mass in China may think that it makes sense to move their treasury centre to Shanghai, especially if they have already established their regional headquarters there."

Greater competition

While Singapore, Hong Kong and Shanghai are leading the way in the race to become the region's top treasury centre location, they are by no means the only ones. "Most countries in the region are analysing the value of positioning themselves as a treasury centre location. This is happening in India, Malaysia, Thailand and even Macau, and I suspect that these efforts will continue," says Citi's Patil.

Outside of the 'big three,' Malaysia is perhaps the location gaining the most ground, thanks to its Treasury Management Centre (TMC) incentive package that offers corporates a 70% tax exemption for five years on income arising from qualifying treasury services. Malaysia hopes that by offering this package, local corporates will be encouraged to build a treasury centre in Malaysia, and that this, in turn, will grow the talent pool to eventually attract multinationals.

Thailand is offering a similar proposition, although currently there are only a handful of treasury centres in the country. This is primarily because there are plenty of regulatory challenges that limit the functions that can be performed by the centre. For example, capital controls limit cross-border inter-company lending and there is limited liquidity locally in foreign currencies. Trapped cash is another major issue.

The long view

So can Thailand, Malaysia and other locations in the region truly ever compete with the 'big three'? Citi's Patil thinks it is unlikely any time soon: "I don't think we will see a meaningful new centre in Asia yet because there is such a large gulf when you look at the key parameters between the established centres and the aspiring ones," he says. "There will of course be some companies domiciled in these countries, or corporates from outside with critical mass in them that will base themselves there because it makes sense for the business. But if the company has operations across the whole region then the propositions are too strong from other locations."

Despite this, increasing competition can only be a positive for corporates. After all, it is encouraging various countries to make themselves more welcoming to treasury operations, thereby reducing the complexity of running a treasury in the region. ■

Photo credit: Antonio Ledermann

The treasurer's new mindset

Denis Ecknauer
APAC Regional Treasurer
ABB

The job of the treasurer is very different from what it used to be. The scope of responsibilities has grown considerably in the past decade and many treasurers are finding the C-suite more receptive to their ideas and priorities than ever before. But to meet the growing requirements the job now places on them treasurers can no longer afford to work in isolation. In this article, Denis Ecknauer, APAC Regional Treasurer for ABB tells Treasury Today Asia why, early on in his career, he resolved to acquire a deeper understanding of the business and how this made him a better treasurer.

ABB engineers power and automation technologies for a broad base of utility, industrial, and commercial customers. Its products include everything from robots to light switches. Power products include transmission and distribution components, as well as turnkey substation systems. Automation technologies are used to monitor and control equipment and processes in industrial plants and utilities. The company has established a presence in about 100 countries, with its core businesses concentrated in power and automation markets.

Global companies need treasurers who understand, not only the constraints and opportunities within the countries or regions that they oversee, but also the business sector they operate in and their own company's strategies and objectives within that. Although this has always been true to an extent, one could argue it is especially important today, given all the talk about the modern treasurer's expanding – and increasingly strategic – role.

The remit of the treasury function has indeed grown in recent years. Daily cash management duties are still the main preoccupation of the majority in the profession, of course. But by most accounts, the treasury function is now more than a mere transactional processing unit. It's become something of much more strategic value across the organisation.

Indeed, so significantly has the role changed over the past decade one wonders what someone who moved into the treasury profession in the early 1990s makes of it all today. "I made the step from financial markets to corporate treasury about 15 years back," says Denis Ecknauer, Regional Treasurer Swiss technology multinational ABB's APAC entities. "Today I would probably not be able to make that transition again because the requirements on the corporate side have developed so much."

Ecknauer explains that nowadays corporate treasurers require not just different skill-sets, but also radically different mindsets than in days past. "The mindset change we need is to better understand what the business needs and only by doing that can we bring all the different parts together to create more value for the business and receive the recognition in a corporate organisation."

A desire to feel a closer proximity between his work in finance and the business fundamentals driving moves in the market was in fact what initially attracted Ecknauer to treasury. After he spent the first years of his career working as a trader in a bank he made the decision, after a decade, to leave financial services and take up a role in corporate treasury. Although he never anticipated back then just how close he would one day need to be to the business to execute the role faithfully, it was, even then, a massive change.

> "The mindset change we need is to better understand what the business needs and only by doing that can we bring all the different parts together to create more value for the business and receive the recognition in a corporate organisation."

When you're on a trading desk at a large bank you become almost singularly focused "like a sniper" on getting those last remaining basis points. Corporate treasurers require a wider and deeper understanding of the underlying nature of these transactions, however. At a fundamental level they are acting as real business partners to link the global economy and risks/opportunities with the products or services a company is generating its core revenues from.

Loading the 'lorry'

The extent to which the business model shapes nearly everything in treasury – from the trades being made to the applications they are being made with – is something which Ecknauer believes is often underestimated by people both within and without the profession. Take the case of treasury technology, for example. To understand how Ecknauer thinks of treasury software one needs to consider how the company he works for is structured and how they generate their main income. There must be a top-down and bottom-up dialogue to create the understanding and awareness of internal and external risks but also opportunities that software shall be able to monitor. Key transactions shall be replicated and standardised from an end-to-end perspective with a high degree of automation to finally achieve a balanced and cost-efficient approach for the operations. "A shift of efforts from collecting data to a more pro-active and decision making focus," Ecknauer says.

Despite the fact that ABB Group already operates across more than 100 different countries globally, from time to time the company still finds itself entering into new markets. But when companies attempt to establish treasury operations within a new jurisdiction rarely ever is it sensible from a cost perspective to invest in a full suite ERP solution from the beginning. So a balance must be struck. "If you try to centralise it all it will come at a huge cost to a company like ABB dealing in so many countries," he says. "Therefore, in some circumstances, there is no choice but to do work manually with Excel spreadsheets."

That said, for a company the size of ABB, sophisticated tools are required to manage treasury at the group level. Ecknauer draws an analogy with motor vehicles. "Where I'm sitting, in the country organisations, we have what I call a 'lorry', a place where we collect and load the underlying data and ship it to our colleagues at the group treasury level," he explains. "There they have a high performance TMS, which is more like a Ferrari. Once they have aggregated and netted the data we sent them, they then execute transactions accordingly."

The fog of currency war

Having confidence in the department's technology and being able to quickly get an overview of changes in the risks the company is exposed to will always be of critical importance to the treasurers of large multinationals. Yet in today's increasingly globalised markets, where multidimensional rather than vertical or horizontal supply chains are becoming the name of the game, and market volatility on the rise, this is especially true. "This is important because the world has become so fast that at any point in time something serious can happen in the market and you want to have as fast as possible the overview of your exposure," explains Ecknauer.

Market volatility is, in fact, something Ecknauer expects will get much worse before it gets better, given the policies currently being pursued by central banks in order to provide stimulus to the flagging economies they oversee. Looking exclusively at the US right now one might argue that in that respect quantitative easing has been reasonably successful. But consider all the implications outside of the narrow prism of one country's economic interests and the picture is less clear. With other central banks around the world now firing up their printing presses in retaliation it's difficult to see this ending well, says Eckanauer. Nowhere, in fact, are the risks of this experiment in monetary policy more apparent than in the Asian emerging markets that Ecknauer oversees. "The US are trapped," he says. "They cannot raise the interest rate like everybody anticipated they would because it would negatively affect the economies of some emerging market countries which are closely related to the US dollar. So that is one thing that really concerns me at the moment, the controlled reduction of these quantitative easing (QE) initiatives and how that might impact the markets we operate in."

There's one other recent economic trend that Ecknauer is keeping a close eye on: the falling oil price. He believes that, netted out across the different industries in which ABB operates, the impact on the business of the past year's dramatic fall in energy commodities has been more or less balanced. "There are many oil importing countries that are benefiting from it, and many countries that are being put at a large disadvantage. The same is true at ABB. On the one side we are winners and on the other losers, and that is reflected in our broad business portfolio and global footprint," he says.

> "Of course, you don't need to be an engineer to become a treasurer, but a real corporate treasurer is not far from a financial engineer."

ABB has what Ecknauer describes as quite a conservative approach to FX risk management: treasury policy dictates that every signed contract must be fully hedged. On the one hand, there is nothing too much out of the ordinary in what Ecknauer sees as being key to managing the risks associated with events like the tapering of QE or the falling oil price. It is simply a matter of having clearly-defined policies and strategies in place and, as far as possible, systems that allow one a quick overview of the company's exposures.

There is an additional aspect, however, which relates more to Ecknauer's belief that treasurers need to develop a better understanding of the business strategy. He recalls an anecdote from one of the corporates he worked for as treasurer earlier in his career. This particular company had outsourced much of its treasury operations to a third party, a strategy which Ecknauer believes is fundamentally wrong. Many of the trades he saw being made under this set-up were poorly judged, purely because those responsible for executing them did not understand the business model. Ecknauer made the decision to bring it all back in-house. "By understanding it and putting it back with the business model I could create a couple of million without taking any additional risk. I could also mitigate other risks that nobody had even been aware of," he says. "Of course, you don't need to be an engineer to become a treasurer, but a real corporate treasurer is not far from a financial engineer."

Vital work

All the recent market turmoil and uncertainty only serves to emphasise for Ecknauer the importance of the work he does. The CFO, board and other stakeholders need experienced treasurers, such as Ecknauer, to be on top of things when the market turns in a way that's unfavourable. "They want to be able to sleep well, safe in the knowledge that somebody has anticipated those risks and is able of reacting quickly when things are changing," he says. "I would say that in a MNC the treasury is equally important to those who generate the income in the core business since treasury' responsibility has a commonality across all company stakeholders, the end result is cash which treasury is mainly managing."

Of course the pressure to react quickly to events means that for the treasury team at ABB sticking to a rigid plan of activities each day is all but impossible these days. Today, a great deal more flexibility is required of treasurers. "You can hardly plan a day anymore. Before you are even in the office you are looking at your tablet device and seeing that this or that has happened and everything you had planned to do will go out of the window. It's not a straightforward role anymore – one cannot simply work from left to right. You have to be very pragmatic with how you deal with the things that land on your table, almost 24/7."

Breaking down silos

Given that reality, Ecknauer says it is difficult to predict what sort of external events he has to prepare for that he will be required to focus on most in the years ahead. However, he does have a clear strategy of what is likely to feature near the top of his list of priorities. Nearly two years ago when Ecknauer arrived in Asia, he was asked to define within three months a next level strategy for the treasury in the APAC region, no small challenge with Asia's unique markets and regulations. The strategy that was finally agreed was put up in three key layers. With the first, he will continue to focus upon strengthening the treasury organisation while investing in people and know-how to sustain the talents already within the organisation and encouraging a change of mindset eg business partnership, which will remain a key success factor for the entire implementation of the strategy. The second is to optimise existing but still largely individual enhanced ERP set-ups for a higher degree of data aggregation and automate processes as much as possible, while the third is to define a balanced and cost effective consolidation of responsibilities between local and centralised activities.

> "A good cash manager is gold for a company. If you have a wise cash manager, who understands what we do and what we can expect from the business side, that can help to quantify more of the uncertainty in the forecasting."

Ecknauer speaks particularly passionately about the first point, tying it back into his belief that today's treasury professionals need to develop a more collaborative mindset. "A good cash manager is gold for a company," he says. The reason, he elucidates, is that personal experience is vital when it comes to a task like cash forecasting. Data, after all, always needs to be interpreted and that is where the value of an accomplished cash manager is revealed. "If you have a wise cash manager, who understands what we do and what we can expect from the business side, that can help to quantify more of the uncertainty in the forecasting," he says.

In fact, Ecknauer believes so strongly in the importance of understanding the business that he hopes to find a way of integrating it into performance assessment. "Let's say that at least once a year treasury employees have to get out to the factory and smell the oil," he says. "The people in the factories need to understand why you do what you do, but also you need to understand the role they play and what causes them headaches and so on. That is one of the KPIs I am strongly in favour of. We need to find ways to create more value to the business and therefore we need to understand the business more closely." ■

In the zone

When the People's Bank of China (PBoC) approved the establishment of the Shanghai Free Trade Zone (SFTZ) in Q3 2013, this piqued the interest of the global audience and in 2015 there have been a number of pilot initiatives launched within the zone. But how does SFTZ compare to the nationwide programmes, and does it make a difference to treasury practice? Citi's Regional Head of Global Liquidity Management Services, Asia Pacific, Sandip Patil, has the answers.

The integration of four existing bonded zones in the Pudong district into the single Shanghai Free Trade Zone (SFTZ) has always been seen as a sign of China's commitment to reform. With the intention of simplifying the way that business is conducted within China, SFTZ is indeed a bold and progressive move. The reforms launched through SFTZ, while paced, have largely followed the original blueprint, and the mere fact that reforming measures are alive and well should be celebrated. So, some 18 months after its launch, it is worth asking what difference does SFTZ really make to a company's treasury practices and its business in China?

"It is the most significant event in China's financial history over the past decade, simply because it is seen as the test-bed for liberalisation of policies that could be rolled-out nationwide," explains Sandip Patil, Citi's Regional Head of Global Liquidity Management Services. He says that, as a pilot scheme, it is necessary to assign SFTZ "very significant importance". When it was launched, he says it had a strong driving force largely to prepare China for the challenges of liberalised trade, to promote the currency and to further open up the economy. It has since been catering to the internationalisation of China's trade effort, taking a journey towards major change such as initiating interest-rate liberalisation – before certain parts of the experiment went nationwide last year.

In February 2015, 'third wave' guidelines were issued by PBoC, opening up new financial channels for SFTZ-based entities (see the March/April 2015 edition of Treasury Today Asia for detail on the first two waves). These 'upgraded' the existing approval and quota system for companies borrowing RMB and foreign exchange outside of China. The changes afford corporates (and non-bank financial institutions) operating in SFTZ a lot more flexibility when structuring their foreign debt profiles – as indeed they do for the hived-off foreign trade accounting units (so-called FTUs) of Shanghai-based banks for all client business booked in the Zone.

Specialist zones

Considering the changes implemented to date, there were several public observations made last year questioning the value of SFTZ, notes Patil. "Our view remains that it is a very fruitful and meaningful experiment. The deregulation coming up is proving the point that it is just increasing in scope; slowly but surely China is committing itself to further deregulation of its economy, especially around capital markets and capital accounting forms." He believes that the progress seen so far has been impressive. The first major evolution is the SFTZ itself; the second is the SFTZ expanding to broader horizons within Pudong District (the original 28 sq km area is now almost four times the size) facilitating three more physical locations – for high-tech, manufacturing and financial services – creating specialised hubs within SFTZ. The third major manifestation of progress will be the expansion of 'free trade' to three more zones, namely Guangdong, Fujian and Tianjin. The suggestion is that it will afford more freedom for foreign-funded firms to retain their foreign exchange capital without converting into yuan. It is anticipated that each new district will also operate along specialist lines. "We expect formal confirmation in the near future," says Patil. Although no specific timeline has been set, he comments that it is all "clearly progressing in a very positive direction, giving a greater amount of financial liberalisation power to the entities operating in the free trade zone." Progress, he concludes, "is very satisfactory".

As a test-bed for the wider liberalisation of the Chinese economy, with planned geographic expansion, it is absolutely achieving what it was set up to, confirms Patil. As one of the first banks to set up in SFTZ, Citi's view is that there has been good adoption rate by its client-base, with billions of financial flows in and out – both core objectives. To contextualise this flow, he points out that at this time last year there were around 3,000 registered entities in SFTZ; today there are more like 16,000. "It clearly shows more and more entities are interested in establishing themselves in SFTZ and more are doing cross-border business. It is achieving its objectives – and a lot more is to come."

Broader reach

By looking at the benefits seen by the multinational corporate segment when effecting cross-border trade, tangible results can be demonstrated. Cross-border pooling has increased as more of MNCs are engaged in borrowing and lending RMB. Trapped cash has been an issue for many such businesses and, says Patil, "many clients are now able to deploy that cash in business operations outside of China". Experimentation around lowering onshore funding costs for Chinese businesses is also heading "in a positive direction". Newer concepts such as in-house banking, 'on behalf of' payments and collections, and netting have similarly risen up the agenda of MNCs seeking greater efficiencies as SFTZ delivers on its initial promise. "Since the pilot scope was expanded, it has given increased power to many more customers who are benefitting from some of these concepts by implementing them nationwide – within a controlled mechanism." This, Patil feels, should give the regulatory authorities the confidence to take the entire experiment fully nationwide. Indeed, he says, giving those companies in SFTZ many more tools to function more efficiently and now facilitating the opening of an FTU, takes the free trade zone concept "to the next level".

No project of such monumental importance is going to be delivered without first experiencing some challenges. The first of these challenges is for MNCs to connect funding with their onshore businesses, to support all of their needs; the ability, for example, to bring offshore money to fund working capital is limited by the amount that can be borrowed. The second is around China's capital account; this is an experiment in that direction too, it is not yet fully liberalised. As such, it is cheaper to fund outside of China, however, the new rules announced in February materially increased the previous limit on the amount of offshore funds a company in SFTZ can raise, which is now limited to twice its capital. In comparing SFTZ with more financially liberal spaces such as Singapore or London it is clear that SFTZ still requires the clarity and definition in terms of legal and taxation structures. "But it's likely to progress in that direction as FTU/FTZ adoption grows in size and scope," comments Patil.

Reaching further

It is also likely, given the steady progress to date, that there will be further benefits as PBoC increases the scope of reform and expands the number of FTZs. For Patil, the FTU concept has been a major recent enhancer of opportunity and driver of demand, vastly improving treasury and working capital cycles: "if your objective is to borrow or lend more offshore, across local or foreign currency, you can". Being part of an FTU in SFTZ also means being able to access FX markets onshore and offshore. "It's the best of both worlds," he comments. "A company can execute all its FX onshore with CNY (Chinese yuan) and all the associated needs it might have around these transactions. It can also gain access to the CNH market (the Chinese offshore yuan)."

Clearly, market expectation is rising with each new announcement, and the conversation is heading towards bringing the capital markets and the different types of financial instrument onshore. There are calls, too, for further liberalisation of China's capital account. Patil is anticipating a positive outcome, not least, he says, because such issues are now being discussed in the market. "It is difficult to predict when this will happen and in what form we will see these changes, but we do expect further reform."

A roll for both

Despite the advantages of SFTZ, it is still an experiment, says Patil, and as such it is unlikely to satisfy all onshore business requirements. Operating an onshore or nationwide treasury is therefore "a must" to support a major business; companies will continue to run these units simply because they have to and "SFTZ just happens to be an experiment in their journey". As far as domestic business is concerned, Patil believes that the role of onshore treasury is not going to change materially in the short run. And when specifically referring to some of the liquidity tools and techniques currently available in China, certainly more freedom in terms of onshore location is now possible. The ability to pool RMB regionally or globally, for example, means there is no circumstance where a business is 'geographically' forced to set up an entity in SFTZ. However, by the same token, this is the time for clients to finalise the roadmap of globalised treasury and execute against that in phases.

So how important is the role of a global bank? Citi is a tier one institution with a global footprint. It therefore has clients to match. It has also been in China for over 100 years and has created a local client base and a depth of capabilities and talent that goes with such longevity. This, says Patil, enables it to keep in touch with the regulators and maintain a position that helps it shape the most appropriate response to global market needs. As vice-chair of the Shanghai Banking Association, a working committee amongst banks in Shanghai, we are able to add value to our clients by providing insights from the industry to the regulator, he says. "We also play an advisory role for our clients; this is a material benefit in terms of informing them of regulatory change." In talking to, listening to and advising all parties over the years, Patil says a bank with the status of Citi can effectively communicate and demystify the changes across its network, facilitating client feedback "to help the regulators take the experiment to the next level."

Sandip Patil

Regional Head, Global Liquidity and Investments, Asia Pacific
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Unit of MAS

The central bank in the Republic of Singapore, the Monetary Authority of Singapore (MAS) is charged, amongst other things, with conducting monetary policy, issuing and managing currency and supervising the financial sector in the country. Treasury Today Asia continues its 'Know the Institution' series with a look behind the scenes.

For all the troubles certain elements of the world's financial sector have created, the watchful body of men and women in each jurisdiction known collectively as the 'central bank' are charged with putting financial matters back on an even keel (and hopefully ensuring it doesn't happen again). The Monetary Authority of Singapore (MAS) is just such a body, directing activities and moving the industry forward in one of the region's most vibrant economic centres.

Established by Act

The Monetary Authority of Singapore Act of 1970 had set in motion the government's will "to establish a corporation to be known as the Monetary Authority of Singapore, to provide for the exercise of control over and the resolution of financial institutions and their related entities by the Monetary Authority of Singapore and other authorities, and to establish a framework for the issue of securities by the Monetary Authority of Singapore and the regulation of primary dealers of such securities, and for matters incidental thereto and connected therewith." The passing of the Act saw MAS come into being on 1st January 1971, assuming authority to regulate all elements of monetary policy, banking, and finance in Singapore.

Before its establishment, monetary activities generally associated with a central bank were performed by several government departments and agencies. As Singapore's stature as a commercial centre increased, so too did the complexity of its banking and monetary environment, to the point where the status quo was unsustainable. A more dynamic and coherent policy on monetary matters was essential to take the country forward. From the outset MAS has been about the future of the country, not just the present.

MAS has a number of principal objects and functions as laid out by the Act of 1970 (and subsequent revisions):

- To act as the central bank of Singapore, conduct monetary policy, issue currency, oversee payment systems and serve as banker to and financial agent of the Government.
- To conduct integrated supervision of the financial services sector and financial stability surveillance.
- To maintain price stability conducive to sustainable growth of the economy.
- To foster a sound and reputable financial centre and to promote financial stability.
- To ensure prudent and effective management of the official foreign reserves of Singapore.
- To grow Singapore as an internationally competitive financial centre.

MAS has increased its reach into the financial space since its inception. April 1977 saw regulation of the insurance industry come under its wing. In September 1984, the various regulatory functions that were managed under the Securities Industry Act (1973) were also transferred to MAS. This makes it somewhat unusual in the world of central banks, as it is now also the domestic financial regulatory authority.

Also unlike other central banks, MAS regulates the monetary system not by changing interest rates but via a managed exchange rate model that uses the foreign exchange mechanism and intervention in the Singapore Dollar (SGD) market. Currency issuance is now a function of MAS too. This follows its merger with the Board of Commissioners of Currency on 1st October 2002, positioning MAS as the sole issuer of banknotes and coins in Singapore. The actual design of the notes and coins – their dimensions, artwork and denominations – are determined by the MAS Monetary Policy Committee with final approval required from the Government. Singapore is a prolific issuer of 'plastic' notes (made from a flexible polymer). These are said to last up to five times longer than their paper counterparts, with obvious 'green' benefits.

Organisational structure

MAS is divided into a number of groups and their departments, each with specific functions and accountabilities. These departments include:

Monetary policy and investment

Economic policy is managed by the Economic Analysis Department, maintaining the macroeconomic model of the Singapore economy. The Economic Surveillance and Forecasting Department undertakes surveillance of the domestic and international economies, providing analysis and forecasts to support monetary policy decisions. Markets and investment are part of the Monetary and Domestic Markets Management Department created to implement Singapore's monetary policy by managing the exchange rate. The Reserve Management Department takes responsibility for the management of Singapore's official foreign reserves.

Development and international

The Financial Centre Development Department is tasked with supporting the growth of Singapore as an international financial centre. The Financial Markets Development Department has the goal of promoting financial markets in

Singapore (the focus being on developing the capital market, asset management and insurance sectors) and fostering a "sound and innovative" technology, payments and exchange infrastructure. The International Department is charged with shaping the development of MAS's policies on international monetary and financial issues.

Financial supervision

This is split two ways: Banking Departments I, II and III collectively supervise licensed and regulated banks, merchant banks, finance companies, money changers and remittance agents in Singapore. Its counterpart is the Insurance Department which supervises and regulates insurance companies operating in its jurisdiction.

Capital markets

Capital Markets Intermediaries (CMI) Departments I, II and III take collective responsibility for the admission and supervision of capital markets intermediaries, including securities and futures brokers, fund managers, real estate investment trust managers, corporate finance advisers, financial advisers, insurance brokers, trust companies and credit rating agencies. Meanwhile the Market Conduct Department assumes responsibility for capital markets activities, supervising through the administration of the Securities and Futures Act, the Business Trusts Act and the Singapore Code on Takeovers and Mergers.

Markets policy and infrastructure

The Markets Policy and Infrastructure Department has supervisory responsibility for markets and infrastructures, including central counterparties and trade repositories.

Policy, risk and surveillance

This is divided three ways: The Prudential Policy Department formulates capital and prudential policies for banks, insurance companies and securities firms, aiming to promote a sound and dynamic financial sector in Singapore. The Specialist Risk Department monitors and assesses the risk management processes and controls of individual financial institutions and designated payment systems. Its counterpart, the Macroeconomic Surveillance Department, seeks to identify emerging trends and potential vulnerabilities, closely monitoring and evaluating developments in G-3 and regional economies, as well as the broader international financial markets.

Finance, risk and currency

The Finance Department manages MAS's financial resources. The Risk Management Department develops policies and strategies to mitigate MAS's business continuity and enterprise-wide risks, as well as the financial risks of its global investments. The Currency Department, as mentioned above, takes responsibility for the issuance of currency and administration of requirements under Singapore's Currency Act.

Also part of this office is MAS's Managing Director's Office within which is subsumed the Internal Audit Department which is required to conduct financial, operational and information systems audits of all MAS operations. This sub-office also oversees the Legal Department and the Corporate Planning and Communications Department.

Corporate Development

A key part of MAS is its Information Technology Department. This enables strategic use of technology and provides IT services to the organisation. As part of this requirement the department manages two nationwide financial networks: MASNET and the MAS Electronic Payment System (MEPS+).

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MASNET is essentially a communications hub, facilitating the submission of MAS returns and data exchanges between banks, FIs, the Singapore Exchange and government agencies.

MEPS+ is the national interbank payment system (real-time gross and government securities settlement). The technology department also oversees the Singapore Clearing House Association and Automated Clearing House and is keen to promote the adoption of e-payments in Singapore.

Also within the Corporate Development group are International Advisory Panel, which advises MAS on Singapore's financial sector reforms and strategies, and Singapore Note and Coin Advisory Committee, established to advise on the design, introduction and issue of new currency notes and coins.

What MAS offers the community

In carrying out its work, MAS issues various instruments under Acts, Directions (either Directives or Notices), Guidelines, Codes, Practice Notes, Circulars and Policy Statements. Each type of instrument may cover general or specific requirements and is underpinned by a different degree of legal weight, from a matter of statutory requirement to plain advisory.

Acts are passed and issued as statutory law by Parliament but under the expert guidance of MAS. There may also be subsidiary legislation issued under specific Acts, giving more detailed requirements. Directions are aimed at giving specific instructions and could be issued as a Directive, which are general legally binding requirements, or as a Notice, which is a targeted legally binding requirement.

Guidelines typically refer to best practice as should be (but not mandatorily) adopted by specific institutions. Codes meanwhile, refer to preferred conduct around specified activities. Similarly having no force of law are Practice Notes which guide specified institutions around various administrative procedures such as licensing, reporting and compliance. And whereas Policy Statements broadly outline MAS's core policies, Circulars are just information documents for public information.

Resource-rich

MAS publishes an extensive range of research materials including market commentary, advice and academic research papers, many of which can be obtained from Asia-studies.com.

The Financial Stability Review (FSR) analyses local and global economic risks, assessing their possible impact on the financial system and revealing the views of market participants, analysts and the public. Also of note are the MAS Information Papers which highlight key trends, developments and practices in the financial sector. The aim, says MAS is not to be prescriptive but to help disseminate information and enhance understanding of current issues.

> MAS is active in regional forums and initiatives in accordance with Singapore's general advocacy of regional cooperation and integration within Southeast Asia and the wider continent.

Alongside the release of the twice yearly MAS Monetary Policy Statement (MPS) comes the Macroeconomic Review. This is aimed at providing information on the Economic Policy Department's analysis and assessment of GDP growth and inflation developments in the Singapore economy which helps to explain policy decisions published in the MPS. MAS Staff Papers also analyse current issues but from individual writers' perspectives. The quarterly MAS Survey of Professional Forecasters is a useful roundup of forecasts of Singapore's key economic indicators by economists and analysts, based on economic data for the previous quarter provided by the Ministry of Trade and Industry.

Beyond Singapore

MAS is active in regional forums and initiatives in accordance with Singapore's general advocacy of regional cooperation and integration within Southeast Asia and the wider continent. MAS says it maintains regular economic and policy dialogue and technical exchanges with fellow central banks and financial regulators, "to promote the deepening of regional capital markets, strengthening of financial markets, and further developing safety nets for cross-border flows."

As part of this co-operative stance it has an active role in the Association of Southeast Asian Nations (ASEAN) and ASEAN+3, the latter being a forum that promotes cooperation between ASEAN and the Northeast Asian nations of China, Japan, and South Korea. MAS is also an active participant in a number of major regional groupings such as the Executives' Meeting of East Asia Pacific Central Banks (EMEAP) and ASEAN Central Bank Governors Meetings.

These relationships are productive. In March 2015 MAS and the Singapore Exchange (SGX) jointly signed a Memorandum of Understanding (MOU) with the Securities Commission of Malaysia and the Securities and Exchange Commission of Thailand to establish a Streamlined Review Framework for the ASEAN Common Prospectus. The Framework is an initiative under the ASEAN Capital Market Forum (ACMF) and represents a further step towards regional capital markets integration. It is intended to facilitate cross-border offerings of Equity Securities and Plain Debt Securities in the region, making it easier to raise capital across ASEAN countries. The hope is that the Framework will be implemented by Q3 2015. Malaysia, Singapore and Thailand are the first three jurisdictions to sign the MOU. Securities regulators in other ASEAN jurisdictions are expected to participate in the Framework at a later date.

Beyond Asia, MAS is also a member of global bodies such as the International Monetary Fund (IMF), the World Bank (WB), the Financial Stability Board (FSB), the Bank for International Settlements (BIS), and international standard setting bodies such as the Basel Committee of Banking Supervision (BCBS), the International Association of Insurance Supervisors (IAIS) and the International Organisation of Securities Commissions (IOSCO).

MAS has developed working relationships not only with its ASEAN and Asia Pacific counterparts but also with the likes of the US Federal Reserve Board, the European Central Bank and a number of key European and Latin American central banks and regulators.

These relationships are beneficial in MAS's work on Anti-Money Laundering and the countering the financing of terrorism. To this end it is also a member of the Financial Action Task Force (FATF), within which Singapore contributes actively to international AML/CFT standard-setting discussions. ■

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Spotlight on project finance

In addition to funding their own projects, companies with healthy balance sheets are set to increase their investment in projects that would previously have been funded from state coffers. In this article, we look at the evolving world of project finance.

PwC's Capital project and infrastructure spending outlook to 2025 report estimates that annual infrastructure spending will grow from $4trn in 2012 to more than $9trn by 2025, with $78trn spent globally between 2014 and 2025. The firm says private investors may be called upon to foot a higher proportion of costs, even for traditional public sector projects.

However, project finance is also attractive to private sector organisations because they can fund major projects off balance sheet. Project finance is the financing of long-term infrastructure and industrial projects where debt and equity used to finance the project are paid back from the cash flow generated by the project. In other words, it is a loan structure that relies primarily on the project's cash flow for repayment. A review of global project finance deals in 2014 conducted by Dealogic values total investment at $407.8bn, the third highest full year volume on record. More than 1,100 deals were completed last year – the second highest full year activity on record – with energy-related projects accounting for one third of global volume.

In a working paper on project finance published in August 2014, the Bank for International Settlements (BIS) observes that it depends on a sensible transfer of risks and returns and that if done properly, the involvement of the private sector can improve infrastructure project efficiency.

Doug Segars, Associate Managing Director of Moody's EMEA project and infrastructure finance team, explains that bank lending has picked up through Japanese banks, some European banks returning to the market and a number of new banks that are more significant now than before the financial crisis. "Public bond issues appear sporadically, but the real story is private debt – both for new projects and as a source of refinancing for existing bank loans," he notes.

Segars refers to significant appetite for greenfield projects, with investors with defined mandates chasing well-structured projects in sectors such as renewables. "Even demand-risk projects (where there is a risk that a demand forecast may not meet the actual demand) are once again financeable as long as sponsors are realistic. It is very much a borrower's market at the moment and – barring countries that present clear political and economic risk – we see interest from investors for projects across the world."

There is very strong appetite in the capital markets for infrastructure project exposure (both equity and debt) says Michael Wilkins, Managing Director Infrastructure Finance ratings at Standard & Poor's. "Commercial banks have been interested in debt exposure since the early days of project finance in the 1990s and this level of interest has risen in recent years. The other source of finance is institutional, including pension funds, insurers, sovereign wealth funds and asset managers who are looking for long-dated exposure with stable cash flows," he notes. Banks (commercial, multilaterals and export finance) account for 80% of total project finance, with the remainder made up mostly by project bond issues, he adds. "Banks like projects with strong sponsors, such as an oil and gas project backed by one of the oil majors."

Investor considerations

Yield pick-up relative to comparable asset classes is one of the factors investors will take into account when considering whether to back a project, concludes Wilkins. "The average yield on a sovereign bond is around 2%, whereas infrastructure projects generate 3.5-4%."

Most of the assets in the infrastructure space have behaved in a very predictable way, generating steady returns over a long time horizon. That is the view of Giles Frost, Chief Executive, Amber Infrastructure, who describes one of the benefits of project finance as being that the returns are largely (or in some cases completely) uncorrelated to wider economic factors.

According to the BIS, it is necessary to broaden the potential group of investors beyond direct equity investors and banks. When considering the appeal of infrastructure investment, Frost draws a distinction between the relatively small number of treasurers who have access to long-term cash – for example, those working in insurance companies who are looking for assets to match their long-term liabilities – and the much larger group who are focused on efficient cash management.

"For the latter, listed infrastructure funds are a good way of accessing this asset class. These funds show many of the characteristics of the underlying assets but can be easily traded in and out of."

He states that treasurers tend to favour investment in their domestic market, with those in the UK and US displaying the most international tendencies. "The profile of London as an international financial centre and the access to a variety of experts that this entails means UK treasurers tend to get offered a wider variety of investments."

Manish Gupta, Head of Infrastructure Corporate Finance at EY, suggests that anyone looking to invest for a period shorter than seven to eight years should be looking for alternatives to infrastructure investment. "There are many infrastructure debt instruments that are liquid, such as government guaranteed bonds issued by Network Rail or high credit quality bonds issued by infrastructure companies such as Heathrow Airport and regulated utilities. I am aware of many institutional investors who have invested in high credit rated bonds, in some cases as a replacement for gilts."

When it comes to investment preferences, he agrees that treasurers tend to prefer other markets where the same language is spoken, but adds that most treasurers in developed markets will have an aversion to considering treasury investment options in developing markets. "There is some nervousness around projects in less developed economies in Europe and further afield, particularly where the currency is not linked to the pound or dollar."

It is possible now for mid-market firms to raise facilities on a corporate level to finance long-term projects with maturities of ten years or beyond, which was not the case even two years ago explains Nedim Music, Assistant Director, Corporate Finance Debt Advisory at Deloitte UK. "The project finance market is very liquid at the moment. Insurance companies and pension funds are hungry for yields and looking to deploy capital, so there is a lot of appetite for infrastructure assets."

For corporates looking to invest in infrastructure projects that they are not directly involved in, Gavin Quantock, Assistant Director at Deloitte Corporate Finance, suggests that this might not be the most efficient way to invest surplus cash.

"Certain infrastructure assets can be an illiquid market for long-term investors, whereas a corporate treasurer would typically be looking to deploy surplus cash for as little as six and no more than 24 months. The requirement for extensive due diligence is a further reason why corporate treasurers could look elsewhere for short-term returns," says Quantock.

Increasing appeal

One of the factors that would increase the attraction of project finance investment is where the project is of strategic importance to the company and can be financed internally until it is operational and could be refinanced. An example might be a food company financing the construction of a biomass energy facility from its balance sheet in order to create a reliable source of energy and increase the sustainability of its production facility.

Rod Morrison, Editor of Project Finance International at Thomson Reuters describes availability of finance for private sector projects as very good. "There is a lot of long-term debt available from banks and institutional investors and swap rates and loan margins are very low, which is positive for clients."

Multilateral and export credit agencies are an important source of funding in less developed countries, but elsewhere there is a considerable volume of commercial debt available with the market having fully recovered from the effects of the global financial crisis, he continues. "Liquefied natural gas schemes and oil and gas projects in general are most favoured, although they are being impacted by falling oil prices. Renewable projects with strong tariffs or schemes with good sponsors are also attractive. Regionally, North America is doing well due to the shale gas boom, while Australia has benefited from major infrastructure projects."

On a transactional level, there is consistent and heavy oversubscription of project finance transactions in primary phase in both bond and loan markets as well as broad and constant demand for assets in the secondary market with far fewer sellers than over the last two to three years, says Jean-Francois Grandchamp des Raux, Global Head of Energy and Infrastructure Group at Crédit Agricole CIB.

"There is strong and robust appetite amongst the leading project finance banks to underwrite transactions and we are starting to see underwritings re-emerge as a favoured strategy compared to traditional large club transactions. Furthermore, sponsors have stronger leverage and increasing diversity of funding options available to them, which provides them with a strong ability to secure more attractive terms and conditions, particularly pricing where we have has seen large reductions across the board over the last 12-24 months," he says.

According to Grandchamp des Raux, the capital markets and institutional investors are increasing their market share particularly as the project finance bond option becomes a more mature, deliverable and readily available source of financing for private sector projects. This is particularly relevant in Europe where it has partially replaced some loss of the liquidity from those banks who exited the market in the immediate aftermath of the global financial crisis and the subsequent European sovereign crisis in 2011-12. "As the liquidity pressure on the Eurozone has receded and banks restructured their asset base as well as rebuilding their capital positions, we have seen a strong return of bank liquidity into the project finance product in 2013-2014."

He describes export credit agencies and multilaterals as continuing to play an important 'anchoring' role in emerging and developing countries to bridge liquidity gaps and help facilitate private sector financiers to gain more comfort around sovereign and political risks. There is also evidence of government intervention in the form of credit enhancement mechanisms becoming less relevant for most sectors as liquidity constraints for project financing have disappeared, with the exception of specific sub-sectors of the market which remain challenging for private sector financiers, such as nuclear power.

"The strongest global demand from international commercial lenders is for assets structured in the investment grade arena with limited construction risks. These projects typically benefit from having strong/experienced sponsors and core developed geographies in key sub-sectors such as utility networks, energy and public-private partnership transactions."

Geographic focus

Grandchamp des Raux says that countries experiencing substantial growth in investment are in North America (particularly in the energy sectors) and also in Latin America, which represents a considerable opportunity for sponsors and lenders given the macroeconomic outlook/performance combined with relatively under-invested infrastructure. "Banks, in particular, have become increasingly focused on their broader client relationships and geographic focus when deploying capital to projects as they have had to manage their balance sheet constraints in the face of the tougher regulatory environment."

There is also strong interest in projects in the Middle East and Africa as well as Europe, says Quantock. "The European Commission's infrastructure plan commits to an investment of £315 billion over the next three years, which means there are a considerable number of transport projects in the pipeline. Energy infrastructure such as solar, on- and off-shore wind, carbon capture and storage and biomass is also high on the agenda."

According to Deloitte's Music, lenders are looking for projects with solid sponsors and advisory teams. "Whilst there is more capital to be deployed than there was a few years ago, lenders will want to see evidence of previous successful project delivery. It can be hard to find financing for new technologies."

The overall financial structure and visibility of earnings also impact on credit quality, adds Music. "There is greater interest in private finance initiative or PFI infrastructure assets where there is an annual government contribution – investing in a toll road where future income depends on the number of vehicles that use the road is clearly less predictable."

Elsewhere, John-Patrick Sweny, a counsel in the project finance group at Latham & Watkins says the recent focus of multilaterals and export credit agencies appears to have shifted from developing country projects to projects in developed countries. "While the amount of capital markets debt for project finance transactions is not currently experiencing the same growth as for bank loans, project bond debt continues to make up a significant share of the overall debt mix globally and is playing an increasingly important role in the financing of projects in certain regions, for example Europe."

Transport and infrastructure projects in certain jurisdictions (US, Australia, Mexico) continue to attract high levels of investment and there are signs of increased investment in African infrastructure projects, which historically have struggled to attract private sector investment, as investors are forced to seek out more attractive yields in a low interest environment, Sweny continues. "Recent large mining deals in Australia – such as the Roy Hill iron ore project – are outliers in a sector that has traditionally relied on corporate rather than project financing and continues to experience difficulties in Africa and elsewhere."

When it comes to making a project attractive to investors, he refers to the importance of robust commercial and financing contractual arrangements that clearly allocate risk between the project, its commercial counterparties and its lenders. "For example, depending on the sector, lenders may not be willing to take construction risk and instead may expect a guarantee of the project's debt by the sponsors until it is completed to the lenders' satisfaction, or that a suitable construction contractor takes delay and pricing risk during the construction phase of the project through the negotiation of a fixed price, turnkey engineering, procurement and construction contract.

"Ensuring that internationally-reputable counterparts are engaged with respect to the development, supply and operation of the project is extremely important, as is the reputation of the project's sponsors in many cases."

In addition to core structuring and economic considerations, lenders will take into account a wide range of factors, depending on the sector and location of the project. Particularly for greenfield projects in developing countries, they will be concerned about the political stability in the host country and seek assurance that the development of the project is in line with the perceived strategic interests of the country to mitigate the risk of future expropriation or other government interference.

"It should be noted that a stable regulatory framework is a concern for lenders to projects in developed and developing countries alike, with the instability of the UK regulatory regime related to renewable energy over a prolonged period of time, for example, undermining investment in that sector," notes Sweny.

"Geopolitical events can also come into play, as demonstrated by the recent sanctions imposed by the US and EU governments, which in the case of US sanctions specifically targeted the financing of gas projects in Russia, causing certain investors to suspend their involvement in, or pull out of, a number of Russian projects which have had to rely increasingly on domestic and Asian sources of financing," he concludes. ■

Oil price drop: how treasurers might navigate current volatility

Tim Waggett
Asia Pacific Energy Sub-Sector Head
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Falling oil prices in the past ten months might be good news to companies that stand to gain from lower production costs. However, the sharp decline has unnerved boards and treasurers following years when prices were much higher. With oil prices likely to remain subdued for some time, there is a compelling case for prudent treasury strategies and robust working capital management to help treasurers navigate the current volatility.

Since June 2014, the price of benchmark Brent crude oil has fallen to around USD50 per barrel (bbl), touching the lowest point in more than five years and about 58% lower than its year-to-date peak of USD115/bbl in mid-2014.

A number of factors have caused the oil price to plummet, which include:

- Strong growth in US production, which has pushed imported crude back onto the international market.
- Resumption of significant Libyan oil production (from 200,000 barrels of oil per day (kbopd) in June to 900kbopd by the end of September).
- Weaker than expected global demand, particularly in Europe and Asia with China production rising at its slowest pace since 2008; the IMF reducing global economic growth forecast for 2015 from 4% to 3.8%; the OECD reducing its expectations for economic growth through 2015; and noting an increasing likelihood for the eurozone to re-enter recession.

This downturn has been exacerbated by Saudi Arabia and other Gulf countries being unwilling to cut production. Instead, they have preferred to defend their market share through an aggressive "price war".

As a consequence, oil majors, mid-tiered and oil services companies have been forced to implement drastic cost-cutting measures.

Braving volatilities

To weather lower oil prices, some immediate steps company boards may consider include:

i. Deferring major projects requiring significant capital expenditure (capex).

ii. Booking impairments following asset write downs.

iii. Selling and leasing back pipeline infrastructure.

iv. Making redundancies.

v. Cutting discretionary spending.

The current period of price drop is the longest peak-to-trough decline since the 1980s. Although analysts suggest oil prices are likely to remain at depressed levels for the foreseeable future, such protracted swings will not last forever.

With some market estimates suggesting USD150 billion of capex is at risk if the oil price remains around USD50/bbl, swift action is essential.

One priority is for companies to quantify their exposure under different oil price scenarios for the period ahead and to determine how resilient they are. Findings from this modelling may call for the following measures:

- Reduce usage of cash: reduce overall capital expenditure by delaying discretionary and non-essential projects. If possible, boards should consider reducing dividends to ride out the current downturn.
- Maintain adequate liquidity buffer: exploration and production companies with an insufficient liquidity buffer should consider reducing or deferring capital expenditure accordingly. Additional funding measures should be considered to repair stretched balance sheets.

- Migrate from organic to inorganic growth: delay investment or replace projects with opportunistic acquisitions. Explore the possibility of substituting organic growth with inorganic growth, which is earnings accretive. Strategic mergers and acquisitions are likely to increase as illustrated by the Halliburton acquisition of Baker Hughes in November 2014 and more recently Shell's acquisition of BG.

- Reserve for the future: acquisitive firms have maintained a lower leverage level to keep "dry powder" for future acquisitions. If leverage is not high, potential acquirers should issue now to build a liquidity buffer. If leverage is high, consider raising equity to strengthen the balance sheet.

- Reduce financing costs: consider refinancing higher cost debt and lock in lower rates available in the current low interest rate environment, replace short-term debt with longer tenor debt.

- Deploy strategic hedges: establish a hedging policy that ensures appropriate action can be taken when the opportunity arises. Issuing in US dollar provides a natural hedge as oil is a US dollar-denominated commodity.

That said, treasurers should examine tactical measures to optimise processing efficiencies and drive down often hidden costs across their treasury operating environment. These include:

- Benchmark and optimise working capital: review end-to-end treasury processes and front-to-back operations to ensure best-in-class solutions are deployed for optimal working capital management.

In that regard, we have worked with our clients using Citi's Treasury Diagnostics benchmarking tool to measure their treasury practices relative to their industry peer group. The diagnostic is specifically designed to evaluate treasury practices by measuring a company's performance relative across six critical areas of treasury operations: Governance and Controls, Liquidity Management, Cash and Working Capital Management, Subsidiary Funding and Repatriation, Risk Management and Systems and Technology.

Based on a detailed questionnaire providing insight on the client's treasury performance, a customised benchmarking report is generated. This is then evaluated against industry peers and best-in-class companies, namely, those that continually set benchmarks of truly world-class practices.

- Control and visibility of cash: treasurers should also review their existing cash flow forecasting (CFF) processes. Manually intensive processes, which typically use Microsoft Excel to gather data from operating entities before the treasurer has a clear view of cash availability across the organisation, should be improved.

As cash availability and CFF assume even greater importance, how fast this information is collated, transmitted and disseminated is critical to ensure excess cash is deployed to where it is most needed.

- Cost control for travel and entertainment spend: since discretionary spending is an obvious area for cost cutting, it is surprising that some organisations have not yet deployed regional or global solutions to capture, manage and monitor travel and entertainment spend. Implementing such a solution to capture consolidated spend data on a globally consistent platform will ensure companies' spend policy is adhered to. Redirecting spend to strategic partners can also generate volume discounts and working capital benefits.

- Utilise procurement cards: the order-to-pay process can be significantly enhanced by redirecting spend from traditional channels to procurement cards, which are also known as virtual or ghost cards.

By driving spend to strategic partners willing to take card-based payments, companies can reduce the inherent cost of traditional order-to-pay processes: cost reductions can be generated as companies' working capital benefits from a significantly longer settlement period.

For merchants accepting card-based payments for procurement, it enhances the commercial relationship, which in turn may direct more spend towards them as they become strategic partners.

- Evaluate counterparty risks: treasurers should assess the risks of counterparties embedded in their supply chain to minimise the impact on their company's financial health.

Depending on the strength of these relationships, collaborative action such as redeploying key assets following project postponement may help ensure utilisation rates and associated cash flows are maintained.

Greater oversight of account receivables processes ensuring credit limits and commercial terms are not breached are critical to reduce and eliminate the incidence of bad debts and fraud. Preemptive action is essential and an important part of ensuring the health of key suppliers does not move to impairments.

Sustained oil price weakness will continue to challenge the industry. Whilst history suggests that this episode will pass, opportunities abound for treasurers who take swift action to implement a more robust treasury operating platform so that their organisations are better placed when the upswing takes hold. Doing so is not an option, but an imperative. ■

Industry best practice in action: China National Petroleum Corporation (CNPC)

For Asia's emerging market champions with global operations, once cash transparency is achieved, the difference can be stark.

Through installing an integrated treasury system for CNPC, we assisted in transforming its decentralised treasury model into one integrating its finance functions, in-house bank and internal settlement centre.

With the set-up of corporate-to-bank and host-to-host connection, the energy giant has gained full visibility of real time, intraday domestic cash position and daily cash positions of all its accounts overseas. At the group level, CNPC can now manage its subsidiaries' account information, payments and collections, liquidity, financing and investment plans and FX transactions.

Do corporates need cloud cover?

Some commentators believe that the cloud has the power to completely transform treasury, displacing all those archaic in-house systems with something that is cheaper, more efficient and, well, more modern. Yet security remains a perennial concern. In this article, we ask industry experts to weigh up some of the pros and cons of cloud technology, and the conclusions that are reached may just surprise some readers.

Rather ironically, it was just the kind of incident that would have seemed right at home in the script of a Hollywood blockbuster. A top film studio cancels a major theatrical release starring big name actors after hackers, who had compromised the studio's systems, threaten violence in movie theatres. The Obama administration declares it to be a national security issue and blames North Korea for masterminding the attack. So what began as a cyber-breach in a famous Japanese conglomerate quickly became an international incident with the corporate caught in the middle.

Given the scale of the hack targeted against Sony Pictures and the level of negative media coverage, nobody should be too surprised that cyber security is once again back at the very top of the list of corporate concerns. After all, if cyber criminals could breach the systems of a company as technologically sophisticated as Sony – and, as it is rumoured, remain inside there for as long as a year without detection, then surely it could happen to anyone.

This realisation might just lead to a significant change in the way corporates perceive the relative safety of different technological set-ups. Everyone knows that in treasury, adoption of cloud technology has, to date, been hampered by reservations around security. That's understandable. Tell a treasurer that his or her department's computer systems, used to move money around, store financial data and manage risk, are going to be migrated to remote data centres accessible over the web, then security concerns are likely to be raised immediately. Local systems are not exactly impenetrable, of course, but there is always a tendency, when so much is at stake, for people to conclude 'better the devil you know'.

Yet, paradoxical as it might seem, some commentators believe this same technology of which businesses have been so wary, may just be the solution that prevents other companies from suffering the same fate as Sony. This is because, when it comes down to it, cloud services providers know much more about security than the typical company. And given that their whole business model depends on customers trusting them with their data, they always take great pains to secure their services from such attacks. Maybe, then, it's time for those treasurers who have been hesitant about cloud technology to give it a second consideration.

Cutting capex

Putting the security issue aside for one moment, the question must be asked: why has there been such a large influx of cloud-based providers in the treasury services market? When this question is put to various cloud providers with a presence in the treasury space, each has their own unique perspective. They all agree on one thing, however: that the cloud offers a much more cost-effective way for a business to obtain the technology it needs to manage its finances.

In Asia, usage of treasury management system (TMS) technology remains small relative to the US or Europe where we see it much more firmly established. Uptake is certainly on an upward curve, however. In today's globalised business environment even the smallest multinationals are likely to operate across numerous borders. And this creates a necessity for the kind of visibility over cash positions that only a TMS can provide. "For a high number of companies still awaiting their first TMS, it can often take them days to generate a current cash position," says Michael Fullmer, Managing Director of SaaS treasury solutions provider Kyriba's Singapore office. "So the first step we talk about is visibility."

Another element of this relates to corporate hedging processes. As the need to use derivative instruments to hedge exposures across multiple jurisdictions as a consequence of a company's growth, it begins to become clear to the treasurer that the old way of doing things – calculating the mark-to-market of derivatives trades on spreadsheets, for instance – is not only becoming increasingly difficult, but also, given the propensity for errors, rather dangerous too. "I've come across many treasurers who said to me that they have had to go back and re-report after they have closed their period because information was wrong; there was a typo and something was reported incorrectly," says Tony Singleton, Managing Director, Asia Pacific at Reval.

But the apparent benefits of TMS technology do not fully explain why more Asian MNCs are making the decision to enter the market for a system now when in the past they have been content to make do without. To find what is driving that, experts agree, we should look instead at the arrival of cloud-based treasury solutions. Rewind a half a decade or so and, in the absence of a broad range of cloud-based treasury solutions, the TMS was struggling to find much traction beyond the region's largest multinationals. It was not that the majority of treasurers at Asian companies were ignorant of the benefits of a TMS. Companies would issue an RFP and look at all the different systems on the market, only to walk away after being told the budget requirement. After all, half a million dollars upfront (not to mention the ongoing cost of repairs and updates) represents a fairly hefty initial outlay for a platform that is not even profit generating. But this is not the case today when treasurers go to talk to Reval, Kyriba or any of the other software-as-a-service (SaaS) cloud-based TMS providers in the market. "Many companies that needed a system but didn't acquire one just needed a more comfortable entry point," says Kyriba's Fullmer. The ability to move to a full TMS for a few thousand dollars a month versus spending nearly a million dollars: that is very appetising for them.

However, even in Asia where the primary rival of the TMS remains the spreadsheet, conversations around the cloud are changing. Where once the relative low cost of cloud-based TMS used to be the main focus in most vendor sales pitches, it is now the adaptability of the cloud that both vendors and users often want to talk about most. The environment in which corporate treasuries operate today is, of course, increasingly unstable and unpredictable. Regulation in particular since the last financial crisis has been in a state of flux, with a glut of new rules and standards covering everything from payments to derivatives to accounting standards arriving in the treasurer's in-tray on an almost daily basis. Of even greater impact, companies themselves are going through a period of substantial transformation in Asia too, the greatest example of which can be seen in M&A activity which reached a record $367.7bn in the first half of last year.

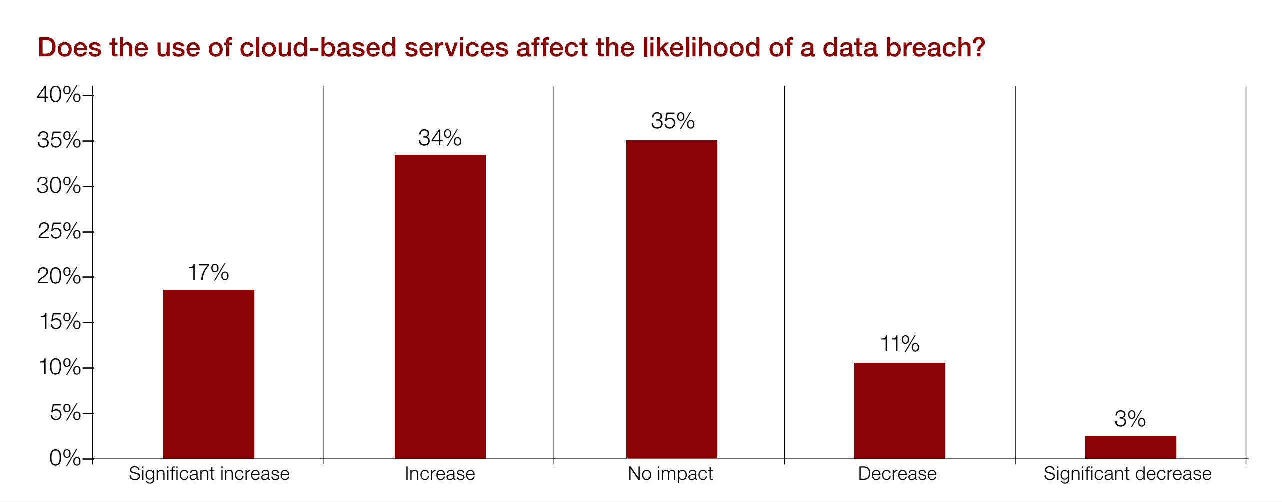
Against this increasingly changeable backdrop, the real value of cloud-based treasury solutions quickly becomes apparent. When there is an important change impacting your business, like an acquisition or a regulatory change treasuries can avoid the need for a protracted (and potentially costly) upgrade. Rather the vendor makes the necessary modifications and rolls them out to everybody. "That adaptability is really important," says Reval's Singleton. "We have clients like the job portal Seek, for example, who have been very acquisitive and bought job boards in Malaysia and South America. But by virtue of the treasury system being cloud-based they are delivering treasury and risk services to all of those acquired entities."

Safety first

Cheaper, lighter and more flexible solutions are certainly something treasurers should be in the market for, providing that security is not compromised as a result. And although many cloud-based treasury providers say they are registering less anxiety around the concept of cloud technology from prospective customers than they did a year or two back, the fact of the matter is that, for some corporate professionals, cloud-security still sounds like an oxymoron.

A survey of 613 US-based IT and IT security practitioners conducted by the Ponemon Institute in June 2014 underscores this fact. A substantial majority of respondents (66%) said that by using cloud-based services, their organisation's ability to protect confidential or sensitive information was 'diminished'. A further 64% believed that it's more difficult to secure business-critical applications as a result of their organisation's use of cloud-based services.

Of course, the cloud industry believes that the reality about security is very different from the common perception. To Koester, for instance, it is utterly unfathomable that any cloud-based business service would be more vulnerable than



Source: Ponemon Institute 2014

an in-house platform. It is quite the opposite, he argues. "Our entire business model, and that of all true cloud-based providers, is predicated on the highest level of data security. I think that security, for genuine cloud-based providers, is actually an advantage."

A 'world without walls'

Phil Huggins, Vice President of cyber security experts' Stroz Friedberg's London office agrees that most cloud providers, at the least the ones he is familiar from doing business with, take security issues with the utmost of seriousness. After all, like Koester says, any cloud-based provider of treasury solutions that was not cognisant of security issues wouldn't be in business for very long. A certain amount of "buyer beware" is to be expected though, he explains, especially considering that there are known instances in recent years in which treasuries have been specifically targeted by "pieces of malware".

Regardless of whether or not they are warranted, Huggins believes that in the long run the shift of business systems to the cloud will not be impeded by treasurers' security concerns. Sooner or later, he boldly predicts, almost everything that corporates do – especially in their back offices, if not in their production environments too – will be using the cloud in some form or another. This seismic shift, he says, is going to demand a new way of thinking about security from corporate finance professionals.

"Traditionally, businesses have treated themselves like a castle, occasionally letting down the drawbridge for other people when they have to deal with them," he says. But in the new world Huggins describes there are no walls. "The business is actually in other peoples' system and the drawbridge is down all the time because of connectivity." This is not necessarily a bad thing, however. Cloud providers have to automate quite a lot, and manual processes are much more likely to be at the source of a security breach. "So they catch a lot of the problems, purely because they automate so many things," says Huggins. "That is one of the reasons why all the cloud providers that I've dealt with have provided a better level of security than many of the businesses I know of that have dealt with security internally."

This is not saying that treasurers can now afford to relax when it comes to IT matters. The risks have not gone away, Huggins explains, they are simply manifesting and concentrating themselves in new areas of the IT infrastructure such as the web browser. That the web browser is one of the most hacked parts of any computer is something of which treasurers should take note.

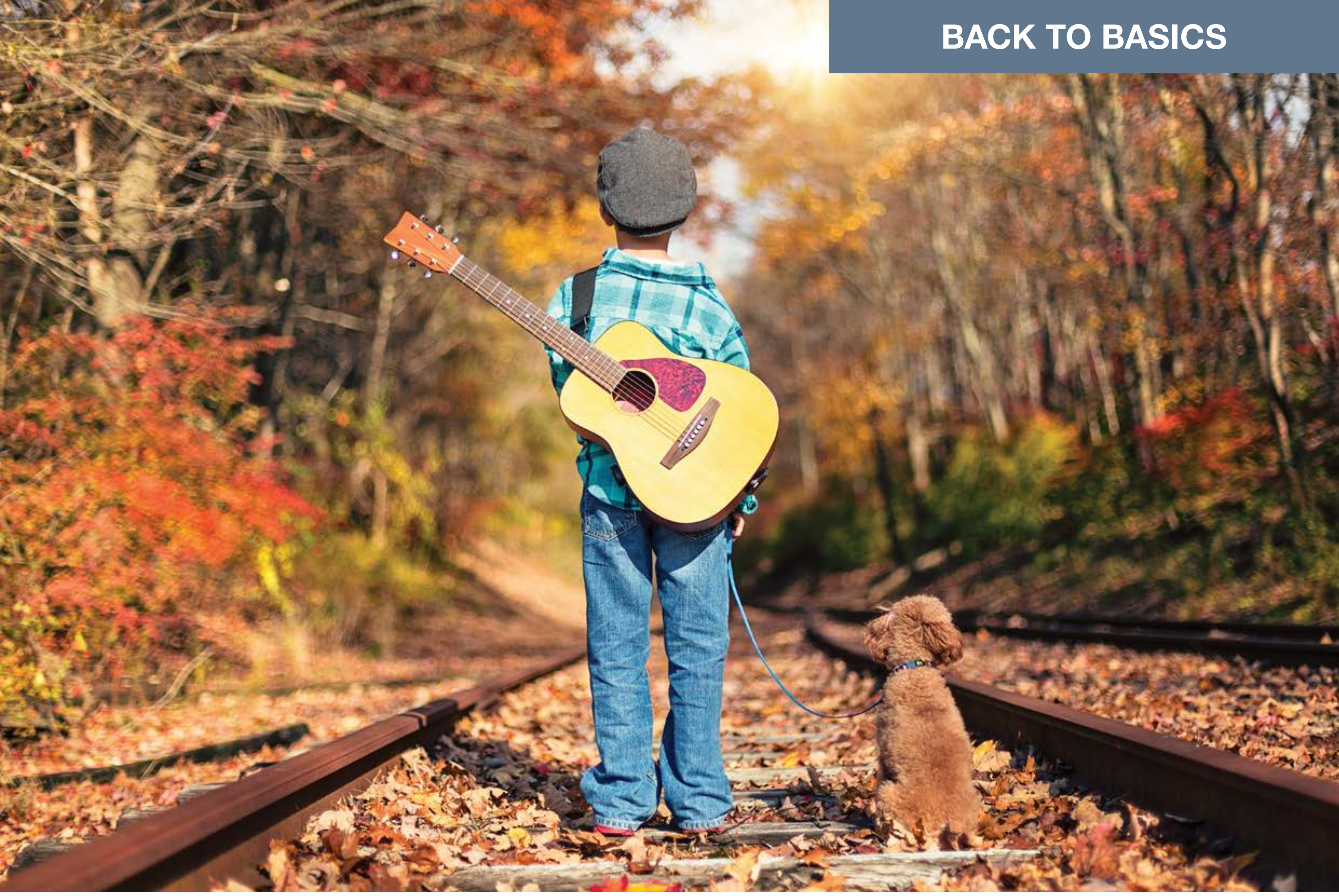
"The web browser and the browsing habits of treasury staff suddenly matter a lot," he says. "Traditionally, malware might come in through some malicious web or email route to target a treasury application installed locally. Now there is effectively one less step. In terms of security, it is about understanding, clearly, that the PCs that the treasurers use and the user accounts they have within the business are high value targets. Where they prioritise their security activities in terms of managing risk, in terms of monitoring issues, they are a high value asset that the organisation needs to spend some time thinking about."

Is the future still in the cloud?

Back in 2011, in the aftermath of the first high-profile hack to which Sony fell victim, there was much speculation about whether such incidents would cause businesses to rethink plans to move to cloud-based computer systems accessible over the web. The Wall Street Journal, no less, ran a story with the headline "Sony hack casts cloud over cloud computing". And they were far from being the only media outlet to ponder the future of the technology at the time.

Yet it is notable that in the aftermath of the latest Sony hack there has been very little of this kind of talk, despite the incident being far greater both in terms of its scale and its severity. It shows, perhaps, just how far we have come in the past few years.

Cloud computing is now no longer a radical, esoteric technology existing on the fringes of the corporate world. Of course, there is still a degree of reticence amongst some corporate professionals to the cloud, as recent surveys demonstrate. But increasingly it is entering into the mainstream and, as it does, one would expect these fears to continue being quelled through experience. ■



Accounting in Asia: latest developments

Inevitably, for a region whose nations are at such different stages of economic development, application of international accounting and reporting standards varies widely across Asia. We examine the major changes taking place, from convergence with IFRS to the rising popularity of integrated reporting.

The concept of international convergence of accounting standards first arose in the late 1950s in response to post World War II economic integration and related increases in cross-border capital flows. Indeed, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) have been working together to improve and converge US generally accepted accounting principles – also known as GAAP – and International Financial Reporting Standards (IFRS) since 2002.

Impetus for convergence in Asia has grown since 2013 when Japan and China started working to converge their standards with IFRS. A table detailing the application of International Financial Reporting Standards across Asian-Oceanian Standard-Setters Group (AOSSG) member jurisdictions updated in March 2015 shows that the standards are required for all domestic listed companies in 15 of the 25 jurisdictions.

Audit reports state compliance with IFRS in 14 jurisdictions, although there are some discrepancies between these two groups. For example, Cambodian International Financial Reporting Standards are mandatory for entities that are required to submit their financial statements for audit and have 'public accountability', while Nepal Financial Reporting Standards are being implemented for listed companies and government-owned business entities over a three year period starting in 2014. India, Indonesia, Japan, Thailand, Vietnam and Uzbekistan are in the process of converging with IFRS – a process that has been completed in China.

Richard Martin, Head of Corporate Reporting at the Association of Chartered Certified Accountants (ACCA), observes that while IFRS is the key standard that will be affecting corporates in Asia, some elements will be more important than others. "The accounting standards for financial instruments tend to be among the most problematic for many companies – currently IAS 39, IAS 32 and IFRS 7 on disclosures. Corporates (and of course banks, insurers and those with treasury operations) are now gearing up for the new standard IFRS 9."

Most corporates, according to Martin, are also planning the implementation of IFRS 15 Revenue from Contracts with Customers, which deals with revenue recognition – clearly fundamental as it affects the most quoted number in the accounts. Ian Mackintosh, Vice Chairman of the IASB agrees, adding that when getting ready for the revamped IFRS 9 and IFRS 15 standards, companies "have to invest time in understanding the new requirements and creating an implementation plan and there may be a need for system changes, new ways of gathering data and training of staff. It is important that companies engage with their stakeholders throughout the process, ensuring shareholders in particular are kept informed about what changes they are anticipating so there are no surprises."

Country-specific issues

Specific countries may face challenges linked to certain standards as they transition to IFRS and these challenges can differ from country to country, adds Mackintosh. "IFRS is principles-based and as such aims to accommodate local variations in culture, practice and law. In the long run, we believe the benefits of principles-based standards are greater than more rules-based standards."

Here, Mohini Singh, Director of Financial Reporting Policy at the CFA Institute, highlights some specific differences in IFRS adoption across Singapore, India, China and Japan. Singapore has adopted all effective IFRS (except for IFRIC 2 Members' Shares in Co-operative Entities and Similar Instruments) and has made several modifications primarily to transition provisions and effective dates of the IFRS that it has adopted. Accordingly, the standards, known as Singapore Financial Reporting Standards (SFRS), are largely aligned with IFRS.

Under the Singapore Companies Act, Singapore incorporated companies (both listed and non-listed) are required to use accounting standards as prescribed by the Singapore Accounting Standards Council (ASC) in their consolidated and separate financial statements.

In India, the Indian Ministry of Corporate Affairs (MCA) has released a revised roadmap for the adoption of Indian Accounting Standards (Ind AS), which are largely converged with IFRS. In April 2014, the Institute of Chartered Accountants of India (ICAI) publicly released a summary of its recommendations to the MCA on the timetable for the adoption of Ind AS, which proposed that listed and large entities should mandatorily apply the new standards in consolidated financial statements for accounting periods beginning on or after 1st April 2016.

As mentioned, the MCA has now released a revised roadmap that has been drawn up after what it describes as 'wide consultations with various stakeholders and regulators'. In essence, companies with a net worth of Rs. 500 crore or more (approximately $80bn) will have to mandatorily follow Ind AS from 1st April 2016. Corporates that have a net worth of less than Rs. 500 crore but are listed, or in the process of getting listed and companies with a net worth of Rs. 250 crore or more will have to follow the new norms from 1st April 2017.

Convergence appeal

The adoption of Ind AS is expected to attract significant foreign investment into India. Yet, despite wide acceptance of the international financial integration benefits, few domestic companies have implemented operational plans for the change to date – owing to transitional costs, compliance burdens and/or pending evaluations. Singh points out that the new roadmap exempts banking, insurance and non-banking finance companies. The roadmap for financial institutions and insurance companies is being determined in a separate process, in consultation with the Reserve Bank of India (RBI) and the Insurance Regulatory and Development Authority (IRDA).

The impact of convergence with IFRS will be significant for banks in India in areas such as loan loss provisioning, financial instruments and derivative accounting. This is likely to have a large impact on financial position and financial performance, directly affecting parameters like capital adequacy ratios.

In China, the use of IFRS is not permitted for domestic companies. All Chinese companies whose securities trade in a public market in the country are required to use Chinese Accounting Standards for Business Enterprises (ASBEs) for financial reporting within mainland China. These are substantially converged with IFRS. It should be noted, however, that Chinese companies whose securities trade on the Stock Exchange of Hong Kong may choose among IFRS, Hong Kong Financial Reporting Standards (HKFRS) and Chinese Accounting Standards (ASBEs) for purposes of financial reporting to Hong Kong investors.

Voluntary application of IFRS for consolidated financial statements by companies in Japan that meet certain criteria has been permitted since March 2010. As of February 2015, 65 listed companies had either started to use IFRS or had publicly announced their intention to use IFRS as a basis for preparing consolidated financial statements as required by the Financial Instruments and Exchange Act (FIEA).

Regional disparity

Despite progress towards IFRS convergence, key accounting and reporting issues affecting corporates in Asia still vary significantly by jurisdiction explains Singh. "For example, in India the adoption of Ind AS will largely impact revenue recognition and financial instruments, while fixed assets will present practical difficulties."

Key accounting areas that need to be viewed with a healthy dose of scepticism in China are revenue recognition, inventory and cash, he continues. "There is a proposed new foreign investment law, which appears to change the way China will look at variable interest entities, focusing on who actually controls the entity versus who is the owner of record. That could create problems for many variable interest entities structures that would be found to have prohibited foreign investment."

In Korea, the key accounting issue relates to party transactions, Singh explains. "The primary reason for intra-group manipulations – such as cross debt guarantee practices and intra-group transactions – is to arbitrarily relocate profits and expand their external size." International Standard on Quality Control 1 (ISQC1) establishes a firm's responsibility to set up and maintain a system of quality control for all audit and assurance engagements. Major Asian economies have largely either adopted or are committed to adopting ISQC 1, says Fayez Choudhury, CEO of the International Federation of Accountants (IFAC).

"In addition, members of the Forum of Firms – who audit the vast majority of public companies globally and in Asia – commit to apply ISQC 1 across their networks. The International Auditing and Assurance Standards Board (IAASB) has a project under way on the topic of quality control, in particular to consider inspection findings and implementation challenges that have been identified and may find it necessary to revise ISQC 1 as a result of these deliberations. Jurisdictional regulators/professional accountancy organisations across Asia monitor the application of the requirements in their oversight programmes and national auditing standard setters and professional accountancy organisations may also develop guidance to assist in the effective implementation of ISQC 1."

Integrated reporting

Elsewhere, the ACCA's Martin says there is significant interest from Asian companies in both integrated reporting and sustainability reporting and that some are already doing it – albeit at a lower level than in Europe or Australasia. "We see this as likely to be of increasing significance in the future. In 2013, we conducted an integrated reporting roundtable in Malaysia. The main finding from this event was the view that integrated reporting will improve communication about company value, as well as playing a vital role in increasing transparency."

Choudhury describes the uptake of integrated reporting and sustainability reporting as variable, while acknowledging that a number of Asian jurisdictions and companies have clearly led in implementing and promoting enhanced corporate reporting such as sustainability reports under the Global Reporting Initiative guidelines and integrated reporting. The chairman of the Singapore Accountancy Commission (SAC) has described integrated reporting as a significant innovation and "the future of corporate reporting". A market-led steering committee has been created to move from concept to execution, with committee members including the Institute of Singapore Chartered Accountants (ISCA), the Singapore Institute of Directors and Singapore Stock Exchange.

The Japan Investor Relations Association estimates that around 130 Japanese businesses are practising integrated reporting currently. Professor Kitagawa from the Graduate School of International Management at Aoyama Gakuin University believes that between 300 and 400 Japanese businesses will adopt it over the next two reporting cycles.

One of the proposals in the national growth strategy revealed by Japan's Prime Minister Shinzō Abe in June 2014 is the establishment of a platform consisting of investors, business and interested bodies for the purpose of discussions on the future of corporate reporting and how to promote constructive dialogues between business and investors. Integrated reporting is referred to in the 'future of corporate reporting' agenda.

In India, the International Integrated Reporting Council (IIRC) has created a multi-stakeholder integrated reporting lab through collaboration with the Confederation of Indian industry (CII). Designed to facilitate knowledge sharing, it is chaired by Koushik Chatterjee, CFO of Tata Steel, and includes CFOs of leading Indian companies, academics and regulators. Following the launch of the initiative in August 2014, the Securities and Exchange Board of India (SEBI) requested an industry-led roadmap setting out the plan for business adoption of integrated reporting over the next decade.

The Malaysian Securities Commission has embedded integrated reporting within its capital markets plan, which has a strategic focus on inclusiveness. Integrated reporting is seen as an essential part of the infrastructure underpinning this strategy and the Malaysian Securities Commission is encouraging businesses to adopt the framework.

Following the lead?

The OECD is pushing the Common Reporting Standard as a key component of its single global standard for exchange of financial information. According to Choudhury, several Asian countries have committed to implementing the Common Reporting Standard by 2018, including China, Hong Kong, Indonesia, Japan, Malaysia and Singapore. "A primary concern around the standard is how the associated compliance burden and technical capacity can be addressed in developing countries. This is as much a concern in Asia as it is in the rest of the world and will really only be resolved with the experience of implementation."

On the subject of compliance burdens, Singapore and Hong Kong have extremely well run regulatory and compliance systems in place and make an effort to be transparent and help local companies do the same explains Chris Devonshire-Ellis, Managing Partner at Asia Dezan Shira & Associates. "Others, such as India are difficult to understand and vary so much within the country that it can be nearly impossible to fully understand the system from both the regulatory and compliance viewpoints. China meanwhile continues to treat local companies (and especially state owned enterprises) in a different fashion to foreign investors, despite both having to abide by the same rules.

"Other emerging countries are still developing both their regulatory platform and their monitoring of it, so it is a moving target. But by and large, General Anti-Avoidance Act (GAAR) is a good benchmark and is used by most internationally minded companies as a standard to refer to when things become uncertain." While internationally minded businesses refer to IFRS as an operating standard, locally focused businesses may not as it could be more advantageous for them to take advantage of the more lax local arrangements, he continues.

Devonshire-Ellis refers to similar inconsistency around integrated reporting and sustainability reporting. "The majority of Asian firms remain small and although they may have relationships with other practices, such as Singapore practices with other firms in Jakarta and Kuala Lumpur, very few have actually reached out to establish and invest in their own subsidiaries in other Asian countries. There are very few firms that have a viable Asian-wide presence and can integrate financial reporting."

The OECD, he says, is viewed in Asia as an organisation with roots in international trade development. Accordingly initiatives promoted by it – and others – tend to be recognised, in the main, by businesses that are operating across borders, which by definition means larger companies. "At a local level, throughout the region, businesses will not be so aware and currently have little opportunity or reason to improve upon that until they start to gain a more international awareness," he concludes. ■

Bank regulation and the next crisis

According to our treasury insider, there is a structural asymmetry in bank regulation – bankers have bigger budgets than regulators, and they use that advantage to 'game the system'. Moreover, the complexity of the current round of post-crisis regulation is allowing banks to extract ever higher rents. Does all this mean the next banking crisis will come sooner rather than later?

At a recent conference, the moderator closed a panel discussion on the future of transaction banking by asking for our thoughts on the future impact of the current regulatory tsunami. My answer: there is a structural asymmetry in bank regulation – bankers are paid more than regulators. Regulations essentially provide cover under which banks maximise their rents. When banks have finished the 'cover your back' part of compliance, they will start working on how to game the system, thereby sowing the seeds of the next banking crisis.

Is this just David having a rant against the banks, I hear you ask? Well, if so, I am in distinguished company. In fact, many of my closest friends are bankers and I have been working with bankers for 30 years. Bankers, like the rest of us, are subject to collective delusions, as the interesting research into many lost personal fortunes in the sub-prime debacle illustrates. Gillian Tett at the FT concluded: "it is groupthink and wishful thinking – not deliberate malevolence – that poses the biggest risk in finance."

The root of our current fragile banking system lies in the conflicts of interest and distortive incentives that Western societies have created in the banks' playing field. Our governments set the laws that define the rules of the game; bankers then go out and play their best. This is fair enough, if the rules align with societal needs. They do not.

In many ways, the global financial crisis was the result of banks responding enthusiastically to government incentives to increase home ownership. The policies that supported this supposed social good, and the institutions like Fanny Mae and Freddie Mac, were complemented by banks energetically slicing and dicing credit so that more risk could be absorbed. Of course, we have now seen that no amount of financial engineering can convert sub-prime into AAA – at least outside of the magical world of credit ratings.

A little history

It has not always been so. A multitude of metrics show that finance has grown enormously since the wave of deregulation in the 1980s. And the run of ever larger financial crises suggests that finance has grown out of control.

The FT's Martin Wolf – interviewed by Boston Consulting Group (BCG) – made some interesting observations about the new normal: "The leverage we're seeing now — 25 to one — is quite new. It's not the way banks used to run in the UK and the US, which I know best, 60, 70, 80 years ago. They used to have leverage of, at most, ten to one, often even just five to one. So, moving to such extreme leverage as we see today, where the sound institutions have leverage of around 20 to one, is actually relatively new. Having such undercapitalised banks, in my view, is one of the reasons why they give us so little in terms of growth and development."

Finance pay which ran around 100% of US average pay post war through the 1980s, has since blown out to 180% – nearly doubling – according to Simon Johnson in The Atlantic. Finance's share of GDP quadrupled from 2% to 8% in the same period, according to the US Bureau of Economic Analysis. And it is the same story with finance's share of stock market values and share of profits.

"The root of our current fragile banking system lies in the conflicts of interest and distortive incentives that Western societies have created in the banks' playing field. Our governments set the laws that define the rules of the game; bankers then go out and play their best."

No value added

Some bankers would probably argue, and perhaps even believe, that these global and function-spanning masters of the universe with their hair raising leverage are contributing to a more efficient world; and that their generous salaries pale in comparison with the social good they generate. The data suggests the opposite. Not only are banks skimming off more and more value, they are doing it to the detriment of the real economy.

> Research by economist Thomas Philippon at New York University shows that the cost of financial intermediation has risen from 2% to 9% over the last century. For context, retail and wholesale trade have both shrunk by about 20% in this period, on the back of the same lower costs and rising efficiency that is available to the financial sector.

Even more worrying is the extensive evidence that banks are not adding value to society, but on the contrary, are taking value out – extracting higher and increasing the cost of financial intermediation. As Martin Wolf told BCG: "If you look at what the banks have been doing, they've predominantly been lending to leverage up property assets. Most of it has been collateralised by property, mortgages of various kinds. They have been doing very little lending to small and medium-sized enterprises, while the big corporates are all dependent on the bond market. So, actually, the link between bank lending and growth has become incredibly weak."

Indeed, US Bureau of Economic Analysis data shows that the growth of bank profits is a mirror image of the decline of manufacturing profits – the banks have been eating the real economy's lunch!

And that's not all. Research by economist Thomas Philippon at New York University shows that the cost of financial intermediation has risen from 2% to 9% over the last century. For context, retail and wholesale trade have both shrunk by about 20% in this period, on the back of the same lower costs and rising efficiency that is available to the financial sector.

Philippon concludes that 'financialisation' has been a disservice to society: "According to this measure, the finance industry that sustained the expansion of railroads, steel and chemical industries, and the electricity and automobile revolutions was more efficient than the current finance industry."

Next steps

If you accept my two main points so far (that bankers will end up gaming the post-crisis banking regulatory system because they structurally have more firepower than regulators, and that globe-spanning universal banks are draining value from the real economy) then you will want to know what can be done to improve the situation.

The answer, in a nutshell, is "not much" – now that Wall Street's regulatory capture of Washington (and the equivalent on the other side of the Atlantic) has essentially set the rules for the current cycle. The key rule is that moral hazard is preserved. This means that banks are empowered to exploit the privatisation of profits backed by the socialisation of losses in the "too big to fail" sector.

Adding fuel to the fire, the complexity and newness of the latest wave of regulation gives bankers a massive playground of obfuscation in which they can confuse customers and shareholders alike to maximise their rents. They will be smart enough not to repeat the error of the banker who said of Basel III: "The client doesn't want to do simple calculations because treasuries are full of morons."

My conclusion is that we will probably need another derailing to stop this train. And it might not be too long coming.

What's the alternative?

Clearly something had to be done in response to the global financial crisis. Even if we accept that some of the problems, such as sub-prime and excess leverage in real estate, were politically driven, the crisis clearly showed the fragility of the banks. But rather than ever more complex regulation, and the inevitable collateral damage and unintended consequences of it, we might have tried structural reform.

Re-enforcing the separation of investment and commercial banking that was shattered by the repeal of Glass-Steagall in the 1980s was proposed by many eminent observers and experienced regulators. But, apart from limited take up of the Vickers report in Britain, the banks managed to quash the idea. In fact, the American solution to the systemic risk posed by Goldman-Sachs (previously a pure investment bank) was to inject a dose of heart-warming moral hazard by turning it into a bank holding company!

> Adding fuel to the fire, the complexity and newness of the latest wave of regulation gives bankers a massive playground of obfuscation in which they can confuse customers and shareholders alike to maximise their rents.

Given the plethora of data I have referenced above, I doubt the bankers' claims that universal banking brings scale economies that benefit the real economy. My personal experience has been that Fixed Income Clearing Corporation (FICC) and commercial bankers barely talk to each other within the same institution. That inclines me to believe that "too big to fail" is more like "too big to manage," as concluded by the St Louis Fed and more recently by HSBC's CEO.

Still, we have to assume – either because size brings benefits we have failed to discern or simply because of the depth of regulatory capture – that banks will not be broken up.

Market discipline

An intriguing idea surfaced in the immediate aftermath of the crisis. It was proposed mainly by central bankers, and I waited eagerly for the ensuing media discussion (it never happened).

The common theme was to let the markets police the banks. Hedge funds and investment houses have the budget to hire bankers and physicists to keep up with the banks. So force banks to issue some fairly unpalatable funding, and the pricing of that will enforce market discipline on them.

William Poole (ex-President of the St Louis Fed) made a very clean suggestion in the FT in 2009: force banks, as a condition of their licence, to issue ten-year rolling subordinated debt amounting to 10% of their assets. The ten-year rolling part ensures continuity of assessment. The subordinated part ensures that investors will have serious skin in the bank game. And the 10% of assets keeps it material. Incidentally, Julie Dickson (Canada's superintendent of financial institutions) also suggested sub debt and using market discipline to police the banks in the FT in 2010.

Corporate treasurers are often cited as a strong use case for global banks. But the truth is that no bank really spans the globe, so we have to multi-bank already. And megabanks are not as seamlessly integrated as their marketing departments would have us believe. As such, using a number of smaller banks is not so scary for corporates.

Although William Poole was structurally astute in his suggestion, he definitely got the regulatory psychology wrong when he concluded his letter with this optimism: "A return to the status quo ante, with banks enjoying the benefits of 'too big to fail', does not seem likely. Regulators will not dare risk a repeat performance. Bankers who think that their political influence will control the regulatory process are in for a rude surprise."

I fear the bankers got the last laugh – at least for this cycle. Obviously, transparency is a prerequisite for market discipline. The markets cannot police the banks if the banks are not transparent. Bankers, whose primary profit centre is customer ignorance, detest transparency, and are endlessly creative about the benefits of opacity.

So, strict enforcement of accounting clarity (which I realise is not easy) will be needed. This will be coupled with pressure that will come from investors to disclose meaningful information about derivative and cash exposures, so that they can assess the risks. In the end, investors will not buy sub debt of a bank they cannot understand. So market discipline will likely succeed in shrinking and simplifying the banks where regulation has failed.

According to the St Louis Fed, "Most, if not all, of the megabanks would have failed without government support during the financial crisis. In other words, in a truly free market, most or all of those banks would have exited."

What does this mean for treasurers?

Corporate treasurers are often cited as a strong use case for global banks. But the truth is that no bank really spans the globe, so we have to multi-bank already. And megabanks are not as seamlessly integrated as their marketing departments would have us believe. As such, using a number of smaller banks is not so scary for corporates. SWIFT and other providers can connect us to multiple banks.

Ripple provides an exciting model for even more seamless finance in the future. And we would benefit from banks collaborating more rather than aiming for world domination. So, for those treasurers with the bandwidth to look beyond the current regulatory tsunami and the possibility that it could trigger the next banking crisis, planning for a more heterogeneous banking ecosystem might be one for the to-do list. ■

David Blair, Managing Director

Twenty five years of management and treasury experience in global companies. David Blair was formerly Vice-President Treasury at Huawei where he drove a treasury transformation for this fast-growing Chinese infocomm equipment supplier. Before that Blair was Group Treasurer of Nokia, where he built one of the most respected treasury organisations in the world. He has previous experience with ABB, PriceWaterhouse and Cargill. Blair has extensive experience managing global and diverse treasury teams, as well as playing a leading role in e-commerce standard development and in professional associations. He has counselled corporations and banks as well as governments. He trains treasury teams around the world and serves as a preferred tutor to the EuroFinance treasury and risk management training curriculum.

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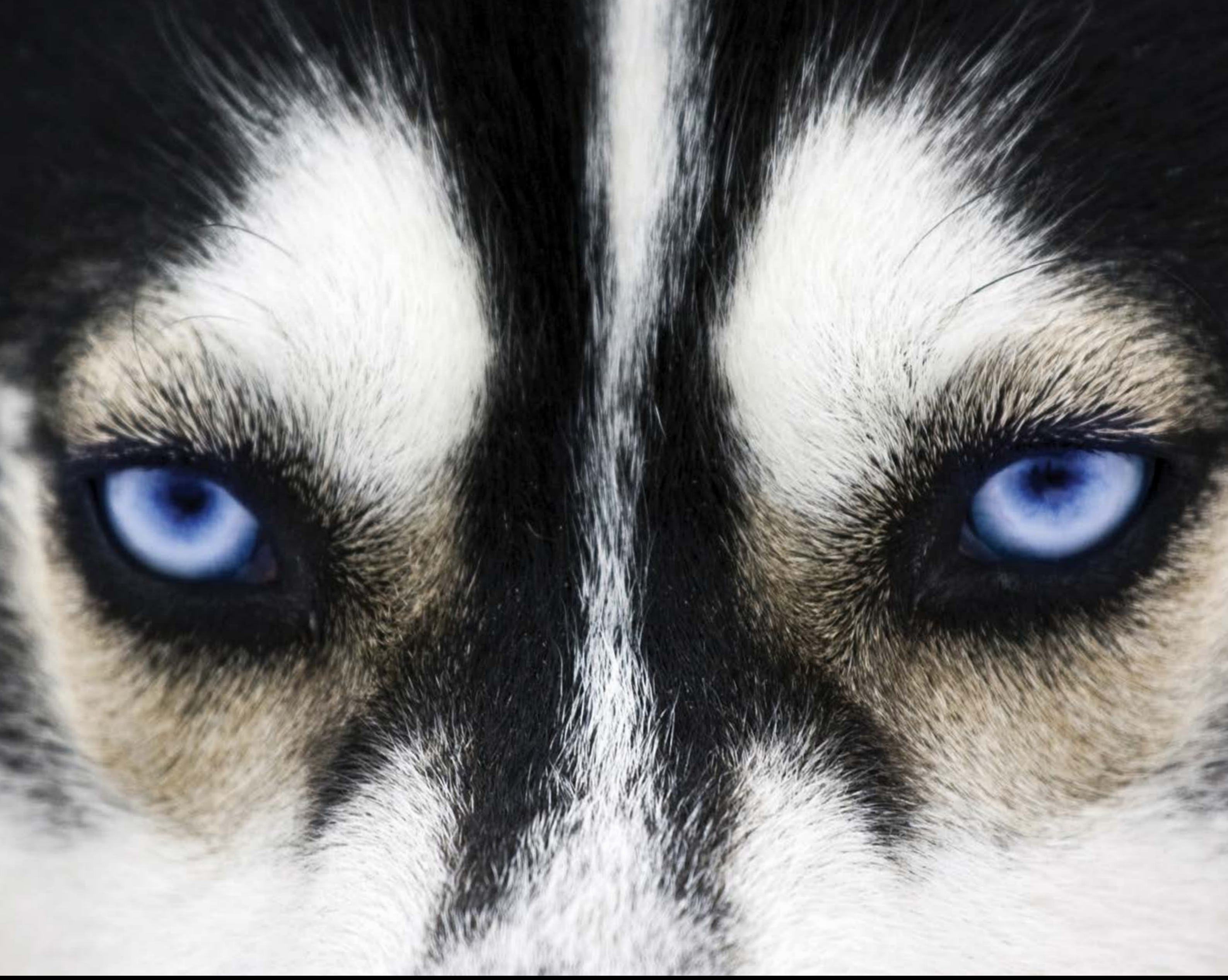

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