July/August 2015

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A volatile mix: EM currencies

Recent volatility has presented treasurers with additional challenges when managing emerging market FX. With hedging sometimes difficult to achieve, or overly expensive, what is the best way to minimise the potential impact of such currency fluctuations?

The Corporate View

Rajan Gupta

Group Treasurer

HYVA

Cash Management

For treasurers in APAC, achieving the desired level of cash visibility is no easy task. Treasury Today Asia asks: is technology always the answer or is it time for a rethink?

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Keeping up with FTAs

Financing

M&As: on the rise

Know the Region

The potential of Oceania

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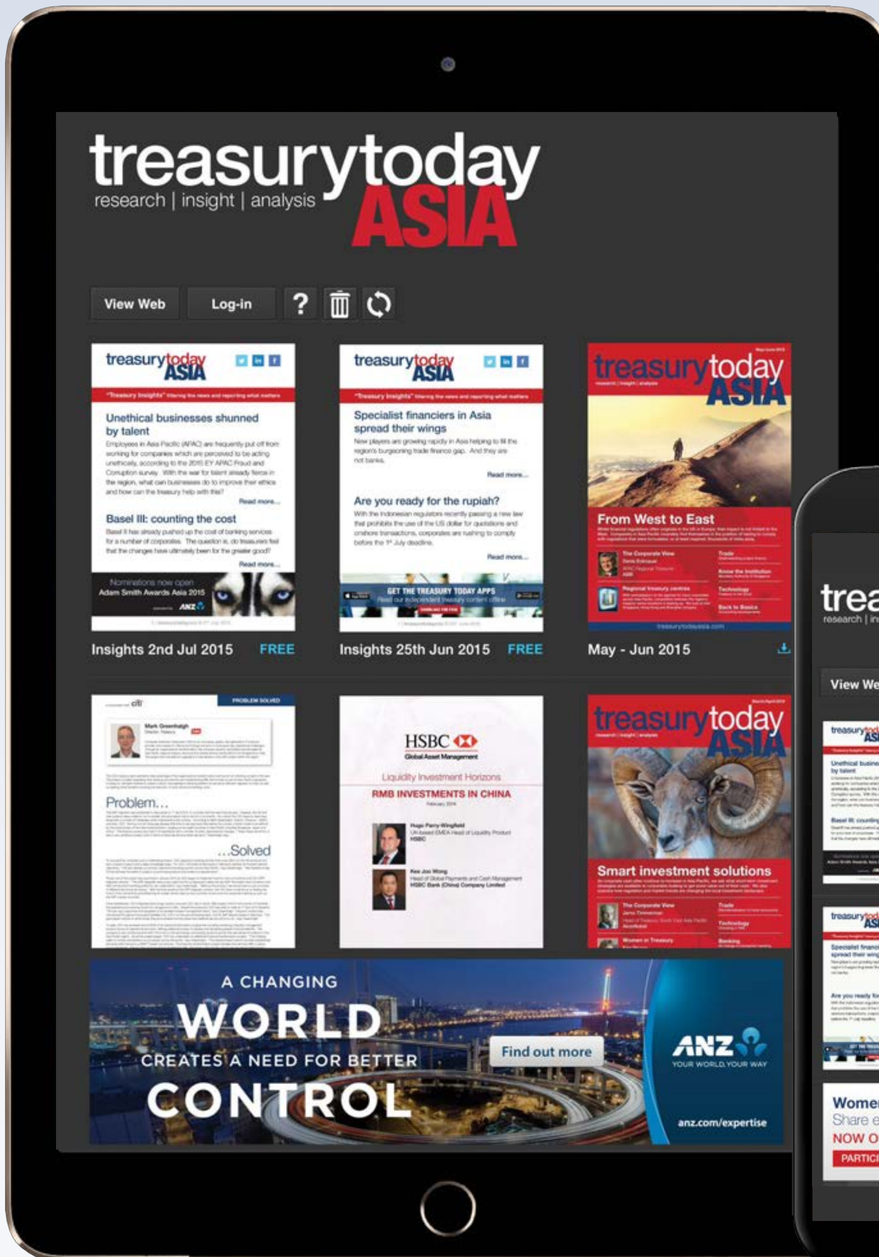
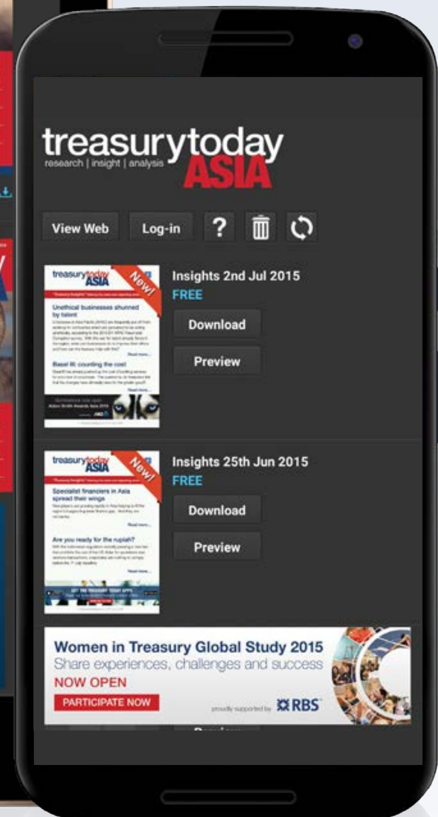
Exploring mobile solutions





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Volume 3 / Issue 4
July / August 2015

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Production	+44 (0)13 0462 9013
Fax	+44 (0)13 0462 9010

Annual Subscription Rate £285
subscriberservices@treasurytoday.com

© Treasury Today ISSN 2053-9398

Treasury Today Asia is published bi-monthly (6 issues) by Treasury Today Limited
Courtyard Offices • Harnet Street
Sandwich • CT13 9ES • UK

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Printed by: Buckland Media Group Ltd.

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

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

Periodicals postage paid at Jamaica NY 11431.

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

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

Air Business Ltd is acting as our mailing agent.

The paper used in the production of this magazine is sourced from protected forests and sustainable raw materials.

Stabilising China's stock markets

At the time of writing, investors across the globe are watching the Greek debt crisis unfold. Yet China is experiencing a crisis of its own, with the Shanghai and Shenzen Indices having lost almost a third of their value since the highs set on 12th June this year.

In order to help prevent the country's stock markets from plummeting further, and to prop up investor confidence, the Chinese authorities decided in early July to suspend initial public offerings (IPOs). This is not a new tactic from Chinese officials, as a similar move was seen in 2012, but this time around, the ban is expected to cover a far larger pipeline of deals. In fact, reports suggest that as many as 28 IPOs that were due to go ahead on the Shanghai and Shenzhen stock exchanges have now been (voluntarily) suspended.

The hope is obviously that such a move will help preserve liquidity, as well as stabilising the markets by encouraging investors to get behind stocks that are already listed. What is not yet clear is how long the IPO ban is set to last. Judging from past experience, it could remain in place for over a year, or as little as three months.

Alongside this IPO suspension, Chinese officials have also moved to create a so-called 'market stabilisation fund' – which is the first of its kind in the country's history. This will be funded in part by the top brokerages in China, who have reportedly pledged to buy at least RMB 120bn ($19.3bn) of shares between them. In a separate move, 25 Chinese mutual funds have also announced that they will invest a portion of their capital (amount not yet specified) into stocks in order to help reverse the downward trend.

Whilst the Chinese authorities appear to be doing all they can to help turn the situation around – these latest measures come in addition to an earlier interest rate cut, a relaxation of margin-lending rules and extra bank liquidity – many analysts believe the moves are too short term in their outlook and could seriously impact the long-term health of the country's stock markets. That said, Beijing is very much stuck between a rock and a hard place, needing to do whatever it takes to restore confidence before other parts of the Chinese economy are impacted.

As always, Treasury Today Asia will continue to monitor developments in this space and keep you updated. To make sure you get all the latest industry news and commentary, sign up to receive our complimentary weekly e-newsletter, Treasury Insights, by visiting ***treasurytoday.com/insights-sign-up.***

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A volatile mix: EM currencies

Various multinationals have bemoaned the bottom line impact of currency volatility since the start of this year. While currency risk comes with the territory of doing business in emerging markets, the heightened volatility at this time is creating additional challenges. What can treasurers do to minimise FX risk, especially in the emerging markets?

FINANCING 16

Safety in numbers

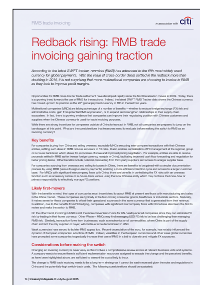
Mergers and acquisitions (M&A) are on the up, both globally and in Asia in particular. In fact, 2014 saw the region present the highest total value of deals on record. We examine the important legal, financial and organisational factors in making a deal and analyse what role the treasurer can play to ensure success.

TRADE 24

The trouble with preferential treatment

Not a week goes by, it seems, without two nations proposing or agreeing a new free trade agreement (FTA). Interestingly though, the utilisation rates of Asian FTAs are notably low. Why is this the case, are the benefits of these agreements not correctly communicated? Or perhaps FTAs are simply not all they are cracked up to be. Treasury Today Asia investigates.

RMB TRADE INVOICING 14



Redback rising: RMB trade invoicing gaining traction

SWIFT's recent RMB tracker showed that the currency is now the fifth most widely used for global payments. What this demonstrates is that the opportunities for corporates to use the currency are rising. The China series continues with Citi exploring the benefits of invoicing in RMB on profit margins and outlines what considerations corporates need to evaluate before making the switch to RMB.

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Germany: Europe's powerhouse

Germany is the largest economy in Europe and the fourth largest by nominal GDP in the world. Positive sentiment in Germany has been gaining momentum over the last year – and there is good reason to be optimistic. We look at the economic forces driving the country's growth, and outline Germany's suitability as a gateway to Europe for Asian businesses in search of expansion.

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Mobile treasury: just a corporate convenience?

There are now more connected mobile devices in the world than there are humans. The proliferation of mobile devices has changed both consumer and corporate behaviour and the expectation to have applications available anytime and anywhere is increasingly commonplace.

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Show me the money

Treasurers in APAC are all looking for a better view of their day-to-day cash balances across the business. Nevertheless, achieving the desired level of visibility is not an easy task. So, why are companies still finding it tricky to get proper visibility over their cash? Is technology always the answer or should treasurers be thinking about more fundamental changes?

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Rajan Gupta
Group Treasurer

Whether it is augmenting HYVA's working capital management, or navigating his company through one of the highest periods of FX volatility in decades, Rajan Gupta has long been comfortable with the heaviest of workloads. In this article, he tells us what initially attracted him to treasury and why the role continues to excite him to this day. He also explains how he managed to get on top of group liquidity management at a multinational that places a high value on local autonomy.

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Oceania: a sea of potential

Australia and New Zealand dominate Oceania with regard to economic power, land mass and population. How do the other nations in the region fit into this narrative? In this article, Treasury Today Asia explores how the geographical uniqueness of the region has posed some major economic development issues as well as tough challenges for businesses operating there.

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Recognising the best in corporate treasury

NOMINATIONS NOW OPEN

What are the Adam Smith Awards Asia?

As our Adam Smith Awards Asia programme enters into its second year, Treasury Today Asia has partnered 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 are now open and there are 17 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 has 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 are now open. 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, for example, implemented a solution that has delivered or leveraged any of the following:

- 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 are now open and and I invite you to rise to the challenge, submit your nomination and share your success story.

Carole Berndt
Head, Global Transaction Banking
ANZ

Adam Smith Awards Asia 2015

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Specialist financiers in Asia spread their wings

Much has been made in recent times of the rapid rise in alternative finance providers thanks to the post-crisis regulatory measures that have driven deposit-taking institutions to rein in their lending activities to SMEs. Less well documented, however, is the rise of 'specialist' financiers who have been expanding rapidly to fill the vacuum left as the international banking sector scales down trade finance activities.

A survey by the Asian Development Bank (ADB) published in December 2014, shed some light on the market opportunity for such lenders. Looking at countries like Vietnam, Cambodia, Bangladesh, Pakistan and India, preliminary estimates calculated using that survey data indicate an unmet demand for trade finance across the region now standing at around the $800bn mark.

The vacuum then, has become very significant indeed. That might partly explain why specialist financiers like The Falcon Group have seen such remarkable growth across Asia in recent years. Whilst the company is now over two decades old and one of the largest non-bank providers of trade finance, it is in the past six years (around the time, coincidentally or not, that the recent regulatory deluge began) that the company has really begun to spread its wings. During that time, the company's revenue has increased on average 25% per year – moving, for instance, from in excess of $3bn turnover in the last financial year to a projected $4bn this year.

Growth in Asia has been especially pronounced. "Mostly (the growth has been) in Asia during the past couple of years," says Will Nagle, CEO of the Falcon Group, a development he attributes to the region's corporate sector becoming conscious of opportunities outside the banking sector. "I think it is the general awareness that has made the difference, not just for Falcon but other specialist financiers too. There is appreciation across the region now of the availability of different financing structures and there isn't so much dependency on the banks to provide that," he says.

By taking a more 'transactional' approach, that is looking at each transaction and evaluating it on its merits, Falcon can reach areas that the banks cannot or do not wish to reach. "Would one of the major international banks want to finance say the importation of $1m over a six month period?" asks Nagle rhetorically. "Probably not – but we will do that."

Moreover, "clients like the way we work," says Nagle. "We try to keep things simple and avoid overcomplicating matters. A lot of it is about the service we provide and the speed and efficiency we can deliver." And that, understandably, is exactly what the company will be focusing on maintaining moving forward. "We are different," he adds. "It's a unique organisation which is why we are in the enviable position we are in today. But our objectives are to continue to grow and continue to stand apart."

Is the tide turning for the BPO?

It is fair to say that since the first BPO transaction took place between BP Aromatics and Oman-based Octal Petrochemicals in 2011, momentum behind the solution has been slow. However, in recent months a number of high profile transactions have pushed the solution into the spotlight again. "I think that the tide is beginning to turn in favour of the BPO," says Ashley Skaanild, Head of Trade Finance at essDOCS. "This is driven by the digitisation agenda that has gained a lot of momentum in recent years. Corporates are increasingly looking to digital solutions in order to automate and streamline their processes and this naturally leads to the BPO in the trade space."

BPO+

Interest in the BPO is also increasing because the solution itself is developing and offering more value to corporate users. Take, for instance, the recent BPO+ transaction, a deal involving BHP Billiton, Cargill, ANZ, Westpac and facilitated by electronic document provider essDOCS. This was billed as a 'major milestone for global trade finance and cross-border payments' because it was the first BPO transaction to utilise straight through electronic documentation end-to-end. "This is unique because until this transaction, paper has still dominated the BPO world, despite its billing as an electronic solution," says Skaanild. He explains that in previous transactions, the data that drives the BPO solution was provided on paper by the corporate to the bank. "The SWIFT TSU data matching software that sits at the heart of the BPO had to therefore be fed manually by the bank. This is not secure because the data can be changed, mistakes can be made, and it also takes time and is inefficient."

In addition to avoiding the rekeying of data, digitisation – in particular of the electronic bill of lading (eBL) – also solved another issue some corporates faced when conducting BPO transactions regarding timing. To solve this problem essDOCS holds the eBL in escrow, visible to all parties but unable to be touched, or traded on, until the BPO transaction is complete.

Challenges remain

Despite the apparent success of BPO+, there are still very few BPO transactions a year (around 600 in 2014 according to SWIFT data) and the majority of these involve very large companies and single large shipments of commodities. "The BPO+ model

works well for these types of transactions because the eBL gives control over the process," says Hari Janakiraman, Head – Global Core Trade Products at ANZ.

"But there are other types of trade and in many cases a number of different things need to align for this to happen. For example, in the majority of trade transactions there are lots of parties involved in the process, such as shipping companies and government agencies. All of these have their own documentary requirements so for the BPO to work all these parties in the process must move towards digital," says Janakiraman.

This trend has led some in the industry to form the opinion that the BPO is a solution for the big players. Yet, many involved with the BPO see this as being far from the truth and claim that it is actually a solution that can benefit companies of all shapes and sizes.

Rate liberalisation: a double-edged sword for China MMFs

Anybody who thought that the macroeconomic headwinds picking up in China of late might serve to divert the course of financial reform will surely be surprised to learn what the country's central bank has recently announced. It seems that rather than putting the brakes on the liberalisation project and focusing on growth, the Chinese authorities have instead opted to hit the accelerator as this decades-long journey nears its conclusion.

The People's Bank of China (PBoC) issued a regulation that will permit financial institutions in the country to issue large-denomination certificates of deposit (CDs). It is yet another sign that the PBoC is serious in its intent towards doing away with controls on interest rates, banks having just last month been given the authority to raise deposit rates to 1.5 times the benchmark rate set by the central bank. "These moves by the PBoC seem consistent with previous statements made by the PBoC's governor Zhou that interest rate liberalisation could be completed within 2015," says Jason Granet, Head of International Global Liquidity Portfolio Management, Goldman Sachs Asset Management. "However, we think that could face pressure from other government departments which might want to proceed with liberalisation gradually."

"The pace of liberalisation in the financial sector has definitely increased," concurs Aiden Shevlin, Managing Director, Head of Asia Pacific Liquidity Fund Management, J.P. Morgan Asset Management. Needless to say, this will all have profound implications for investors, including the treasurers of those multinationals who – despite the relaxation of FX controls – still hold substantial cash balances in RMB. The range of possibilities open to them in terms of how they invest all that liquidity are now broader than ever.

Historically, the investment options for corporates have been, shall we say, limited. "When I first arrived in China you could invest in time deposits, nothing else," says Shevlin. "Even just a year or two ago the choice was not much better. You could decide to put your money in low risk but low yielding time deposits, or you could put it into higher yielding but higher risk wealth management products."

Then came a fledgling money market fund (MMF) industry. In the past few years, MMFs in China have grown rapidly, accumulating assets as a result of investor desire for more market-driven (and higher) rates of return. Figures revealed in a special report by the ratings agency Fitch published this month indicate that overall assets under management now stands at a record high in China, reaching CNY 6.7trn by the end of 2014, 61% higher than where it was just one year ago. Within that, MMFs are expanding the fastest out of all the asset classes seeing AUM reach CNY 1.3trn.

Rival assets

Will China's MMFs continue to grow, now that CDs are out there competing with them for corporate cash? Shevlin believes they will, albeit now quite at the remarkable pace we have seen in the past twelve months. MMFs, he says, have long had an easy ride in China due to the absence of many alternatives. Now that investors will be able to buy a range of CDs with, potentially, very competitive yields that is evidently no longer the case. "At the end of the day, the overall market is still growing," he says. "So CDs will grow and, I think, MMFs will continue to grow too but at a slower pace because there are now other options."

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

Know your customer

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? We have heard talk of a growing trend around Know Your Customer's Customer – what impact will this have for corporates operating in Asia?

Paul Taylor
Director of Business Development, Compliance Services, SWIFT

Due diligence processes, and predictability around Know Your Customer (KYC) information requirements, have changed fundamentally since the latest financial crisis and the further globalisation of banking. This has led to escalating levels of regulation and enforcement where regulation is seen not to be met – meaning that banks and other financial institutions (FIs) have increased controls.

Today, to prove that they know their clients in depth, more stringent checks must be made and more documentation must be sourced. For corporates, this presents a few challenges and concerns. Some corporates have reported that collecting KYC data to open an account takes between an entire day to up to 30 weeks. There are also concerns about the security behind the exchange of such personal information such as passports and signatures.

The rise of the utility approach to KYC is aimed at addressing the concerns around this process. The utility approach will provide a secure method for the exchange of information, and will also remove the need to share the information each time an account is opened, removing the redundant duplication of effort.

The utilitisation of the KYC process would mean that corporates and treasurers only need to provide data once, to the secure system of choice, and then grant access to their different banking partners. This allows more time for treasurers to concentrate on other operational functions and areas of more complex risk. From a bank's perspective, they will receive the data in the format and detail expected, thus reducing the time to open accounts and to conduct ongoing due diligence.

For SWIFT's KYC Registry, SWIFT has defined a common, global baseline of data requirements. Banks contribute an agreed 'baseline' set of data and documentation for validation by SWIFT, which the contributors can then share with their counterparties. Each bank retains ownership of its own information, as well as control over which other institutions can view it. Banks are not charged for data contribution or for using the Registry to share their KYC information with other banks.

Moreover, industry leaders and regulators alike have highlighted the importance of knowing your customer's customer (KYCC). KYCC is a phrase increasingly used by regulatory bodies to reference the need for financial institutions to understand their clients to a deeper, more granular level of detail.

For correspondents, the focus would be more than simply understanding the relationship and risk of your immediate counterparty, but also to understand the greater systemic network risk. For corporates investing in assets or part of a wider correspondent/payment chain, they should be aware that they need to reference or identify their role as an actor in the transaction. It remains to be seen whether these increasingly-discussed requirements will add further complexity in terms of greater detail in the KYC data shared, as this is an evolving expectation.

Arin Ray
Analyst, Celent

Know Your Customer (KYC) is an essential part of banks' and other financial institutions' operations, particularly from a regulatory and compliance perspective. With increasing regulatory scrutiny and evolving regulations in recent years, banks are having to beef up their KYC and anti-money laundering (AML) policies and practices. This means banks' clients, including corporates, are having to provide more information, on a regular basis, to every bank they deal with. This raises the level of difficulty in the KYC process for corporate treasurers. However, some of the leading banks and service providers in the industry have come together to alleviate some of the operational challenges of their clients through the conception of utilities in KYC.

The current practices in KYC are complex, requiring every customer to exchange information with every financial institution (FI) they deal with. Providing the correct documentation, and receiving verification can take weeks and on-going updates are required for each FI. Multiple exchanges of documents result in duplication of efforts and higher costs. The utility model, on the other hand, gathers all customer information at a single place that can in turn be shared with FIs. Bank customers can provide, or upload, all required documents to a single utility provider where FIs can access all the necessary information from this utility.

In this model, the providers of information (investment managers, hedge funds, corporates) are typically not charged whereas FIs can access this information by paying a price to the utility provider. The provision of this service is typically made through

a web portal, requiring minimal effort from users in terms of technology and systems.

While ideally one would envision a single such utility catering to the whole industry, we have seen three or four utilities emerging in this area: these include utilities from Thomson Reuters, Genpact, Markit, DTCC and a group of six co-founding banks, and SWIFT (utility for correspondent banking). All of them are fairly new and currently cater to the developed markets, particularly the US and the UK. However, they all have plans to expand into emerging markets in the near future with particular focus on Asia. The utilities, once fully operational, have the potential to revolutionise the way KYC process is carried out in the industry.

By establishing a common standard and format, the utilities should minimise the need for operational changes for treasurers to submit and update information over time. Online portals can make the transmission and communication much simpler, especially compared to manual and paper based practices followed at many institutions at present. In addition to being free for corporates (and other bank clients), the utilities should free up time and resources of corporate treasurers allowing them to focus on their core business activities.

Neil Jeans

Head of Policy & Standards Org ID, Thomson Reuters

Raj Melvani

Market Development Manager, Thomson Reuters

In the current climate, it goes without saying that the banks are undertaking Know Your Customer (KYC) due diligence to meet legal and regulatory requirements in the jurisdictions in which their corporate clients hold bank accounts. For the treasury department, it is certainly difficult to quantify what value KYC processes provide. Rather than adding value per se, they can be seen as a giving corporates 'a ticket to the game'. In fact, KYC checks are now an intrinsic part of the business relationship between a financial institution and corporate client.

But it is the grey areas and duplication that make KYC seem so burdensome for everyone involved. In Asia, for instance, we see more de-risking happening in the banking industry – where entire portfolios, entire product lines or entire subsets of customers are de-risked by the banks because the associated risk is considered too great. As this risk-based approach starts to take hold in more jurisdictions, more people are pricing for risk to account for the reality that the cost of compliance, compared to the benefit of holding those accounts, doesn't necessarily stack up. Moreover, the risk-based approach has created a degree of interpretation within the financial institutions. Whilst there is a common set of recommendations from the Financial Action Task Force (FATF), and you have a standard legal framework and regulatory framework within a country, each bank is invited to interpret that as part of its risk-based approach and therefore put in place measures that they believe are appropriate for addressing their risks. This leads to a lack of consistency.

Against this backdrop, utilities can help improve the KYC environment by providing a degree of certainty about what level of due diligence is required. Utilities are driving consistency – they have the ability to achieve economies of scale through standardisation. They can also minimise duplication since the corporate only provides compliance information to the utility once, rather than providing it to multiple banks. This reduces the cost of KYC to both the financial institution and the end-client.

Moreover, the global regulatory environment is getting more complicated – in Singapore, for instance, changes were only made recently to the Monetary Authority Singapore (MAS) Regulation 626 in response to increasing international anti-money laundering (AML) due diligence standards predicated by the changes made by the FATF in 2012. What this is doing is placing increasing focus on the financial institutions to understand their corporates and understand who is behind the face of those corporate clients. After all, whilst there are many stable and low risk economies from a money laundering and criminal perspective in Asia, there are also economies that are less so.

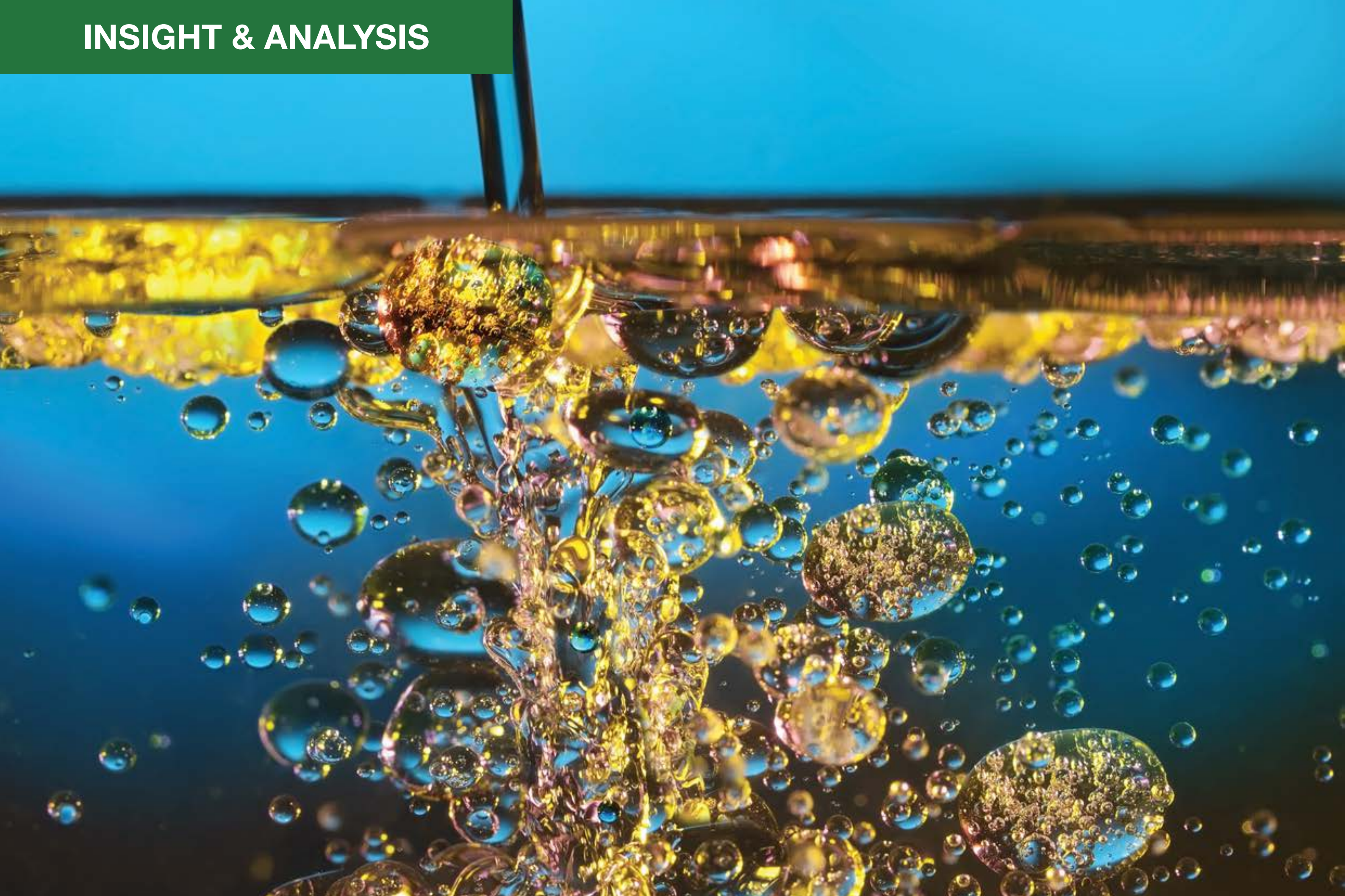
Banks, therefore, are concerned about 'contagion risk', enquiring about their customer's customer – where am I sending and receiving money on behalf of my customer and what trade finance transactions are occurring, for instance. And because we are seeing banks fined significantly for not managing these exposures, they will be less inclined to simply accept polite declines for information from their corporate clients. KYC and Know Your Customer's Customer (KYCC) processes are not only on the banks' agenda; it is our experience that, in a number of jurisdictions, they are on the political agenda too – not least because of tax transparency and corruption issues.

So, whilst we have painted a fairly challenging picture for corporates in Asia, there is also the value that co-operation is bringing as corporate treasurers and the customers of financial institutions start to have more of a voice in Asia. Policymakers are beginning to realise the impacts that some of these regulations are potentially having on the economic viability and health of particular industries. KYC could act as a catalyst for encouraging a co-operative effort to tackle some of the inefficiencies that the industry has had for many years. The benefits of which will be felt by corporates, financial institutions and the regulatory and political regimes in many countries alike. ■

The next question:

"The bank agnostic model is becoming ever more popular among large Western corporates – but how easily can this be achieved in Asia? Also, what technologies or developments in the region should corporate treasurers be looking out for as a means to foster a bank agnostic operating environment?"

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



A volatile mix: EM currencies

While currency risk comes with the territory of doing business in emerging markets, heightened volatility at this time is creating additional challenges. We ask several industry experts: what can treasurers do about it?

Various multinationals have bemoaned the bottom line impact of currency volatility since the start of this year. Diageo, for example, blamed it for a fall in revenues from Latin America and the Caribbean, while Volvo sought to minimise the impact of FX volatility by announcing plans to build a plant in the US.

On the other hand, Unilever's first quarter results were boosted by favourable currency movements and Danone also came out ahead. But the experiences of Unilever and Danone are untypical according to the latest FiREapps currency impact report, which found that North American and European corporates reported a combined negative currency impact of almost $40bn last year.

Corporates on the other side of the Atlantic were most affected – North American companies reported $27.1bn in total negative currency impact for 2014, a 53% increase since 2013. And the impact wasn't limited to a few big names either; in the final quarter of last year, 46% of North American and 51% of European companies had to report material currency-related impacts.

But what can treasurers do to minimise FX risk, especially in the emerging markets?

Tackling volatility

Andrew Gage, Global Head of Research at FiREapps, recommends that the approach to managing emerging market (EM) currency volatility should be the same as for developed markets. "Inter-company loans, hedging, option and natural hedges are all potential methods of countering risk – for companies with and without operations in emerging markets." Therefore, he concludes, "the best strategy you can employ is having complete data." He accepts that borrowing in local currency and managing working capital effectively can help reduce the impact of currency fluctuation,

but also refers to the importance of having a full understanding of exposures and flows.

Meanwhile, Sander van Tol, Partner at treasury consultancy Zanders has a slightly different view: it has always been important for corporate treasury to manage their exposures on EM FX, but higher volatility and increased exposure has made it even more important, he observes. Compared to developed countries, he sees some material differences in the management of these specific risks, which can be categorised as: the regulatory environment; a lack of liquidity; limited hedging products and higher hedging costs.

"The regulatory environment is a key driver in EMs. The majority of EM currencies are restricted and not freely convertible, but because some are linked or pegged to another currency or basket of currencies, a proxy hedge could be a solution." For instance, five out of the six currencies in the Gulf Cooperation Council (GCC) are pegged to the dollar, so a dollar hedge means a hedge in these five GCC currencies. Another example is the Chinese yuan, which is pegged to a basket of international currencies. The downside of such a proxy hedge is the uncertainty that a country can choose to unpeg its currency, which makes the hedge highly ineffective.

Local borrowing

Rando Bruns, Group Treasurer at Merck, observes that high interest rates in many EM countries make hedging expensive and economically uninteresting. Corporates will have to live with that risk and apply a long-term view, he adds. "Local borrowing can be an instrument to reduce exposure, although the high interest rates need to be weighed against this exposure."

Borrowing in local currencies is one of the traditional techniques used for FX exposure management. To the extent that timing differences between revenues and expenses can be managed, FX exposures can be managed at a lower cost and at a lower volatility to the financial statements explains Patrick Trozzo, Vice President for Reval. "However, many companies are also employing technology and more advanced strategies by automating the process of gathering FX exposures across multiple entities and efficiently netting them to optimise the execution of FX derivatives and reduce transaction fees."

According to Ronald Leven, FX pre-trade Strategist at Thomson Reuters, the impact of currency fluctuations is largely a by-product of mismatched exposure profile for assets and liabilities. "Hence, local borrowing (when possible) can be a very effective tool for buffering a firm from currency fluctuations."

Avoiding volatility

Another technique for reducing the impact of EM currency movements, says Lauren Goodwin, an Associate Practice Leader Global Analytics at Frontier Strategy Group, is for corporates to consider country-specific factors since these can provide meaningful information as to where currency volatility may be most rampant. She suggests the questions corporates could ask include the following:

- Where are central banks most likely to be controlled by political factors (rather than economic logic), thus, leaving them more susceptible to volatility?
- Which countries have meaningful FX reserves that can be used to protect the currency in the event of a global macroeconomic shock?
- Would multilateral or local banks be willing to lend to the government (buy bonds) in the event of trouble?
- Is liquidity a serious risk?

In terms of what treasurers can do to manage EM volatility, she says clients should consider 'operational' hedging, which can buffer the treasury against large currency movements. "At the higher-risk end of the spectrum, corporates could complete a strategic acquisition to lessen the impact of currency on sourcing and production."

Moving money

The ability to move money out of certain countries is usually investigated carefully before a corporate invests in a country in the first place, explains Brian Welch, Director UserCare Treasury Consultancy. "Sometimes companies will invest in a particular country because of its economic potential, but if there are potential problems about paying dividends out of those countries the initial investment may be made with loans rather than equity, as the loans are sometimes more easily repaid. Similarly, finance from within those countries might be possible and preferable, so that any balance sheet exposure can be offset by local loans in the same currency."

In the latter case, a counterparty risk will arise with a domestic bank or other financial institution. Although the local investment legislation might require the corporate to use a local bank – in which case the corporate will aim to use the best rated bank in that country. "There is less risk borrowing from a local bank than investing local cash with the same bank," says Welch. "There is also the possibility of one of the global banks providing some kind of service." Many EM countries maintain exchange control regulations to prevent the unlimited transfer of funds out of the country – but the existence of those regulations usually also means that there is an official route by which funds can be transferred out.

In general, the more volatile and free a currency is, the more flexibility corporates have to move money out of the country, says Bruns. "The best example of this is Venezuela, which has a highly regulated FX rate and restrictions on moving money out of the country. Counterparty risk goes along with this." He also refers to the impact of political stability on a corporate's ability to move cash as well as on FX rates.

The typical treasury team, according to Gage, often has a blindspot into its EM finances due to a pattern of opaqueness created by how businesses in emerging markets are acquired/integrated. "Legacy systems and processes often create areas that the team cannot see into, create a lag in the system or are not consistent with company-wide processes. These nuances often make it hard, if not impossible, to manage the risk associated with these markets."

The extent to which the typical corporate treasury team has sufficient resources to effectively manage emerging market currency exposure depends on the size of the organisation, says Bruns. "Having said that, I believe it is good to be rather close to those currencies." Improvements in the process of moving money in and out of EMs, according to Trozzo, have somewhat cushioned the impact of emerging market currency volatility on corporates. He goes on to explain that there are

fewer cases of rigid currency conversion restrictions, which had been driven previously by frequent periods of hyper-inflation.

Additional considerations

Factors such as banking infrastructure and political stability are taken into account when assessing risk in an EM, although Trozzo observes that such issues are of less concern than they were in the 1990s. Globalisation and investment in technology have upgraded banking infrastructures worldwide and many EM countries have established local financial markets that connect to global financial markets.

David Blair, an independent Treasury Consultant based in Singapore, observes that currency volatility is not limited to EMs, though the EM volatility has been exaggerated by dollar strengthening. According to Blair, EM currency volatility has yet to directly impact on exchange controls, while borrowing in local currency and managing working capital effectively can help reduce the impact of fluctuation. "Hedging is possible in most Asian EMs, both onshore and offshore via non-deliverable forwards and many treasurers are actively hedging. The typical multinational company will also have local currency receivable and hard currency payable for sales and the reverse for production.

"Funding local sales operations in local currency reduces risk, as does producing and selling in-country. Long day sales outstanding (DSO) in local currency add to risk; efficient working capital management, therefore, is vital." Blair also warns that many corporate treasury teams lack the manpower to effectively manage EM currency exposure. "Most treasuries are under-resourced and multinationals that have centralised globally for cost reasons are left with no or limited EM expertise."

According to Leven, recent earnings releases would suggest that the strong dollar has been a much bigger issue for corporates than volatility, causing potential credit problems for a lot of EM companies that are dollar-funded. Since most corporate exposure to EMs has a long time horizon, political stability is probably the number one issue, he continues. Banking infrastructure may also be a factor in determining whether to hedge on- or off-shore.

Risk appetite

Market makers' reduced appetite for risk, general uncertainty in the commodities market, increased regulation and continued uncertainty over Greece's future as a member of the Eurozone have all contributed to volatility, explains Jon Dovener, Head of Emerging Markets, Lloyds Bank Commercial Banking. His colleague, James Buckle, Director of Industrials, says treasurers will usually try and use a well-established bank with a local presence and understanding, which can give them a real-time assessment of the local risks. "Alternatively, they may be inclined to use the local market's leading bank. Any treasurer will value a local presence in a region deemed to have certain socio economic and political risks."

Resources could be a factor – but approach and governance are more important according to Peter Wong, Associate Director, PwC Corporate Treasury Consulting in Hong Kong/China and Founding Chairman of the International Association of CFOs and Corporate Treasurers (IACCT) China. "A recent PwC corporate treasury survey found FX risk was the number one risk exposure, yet only 8% of treasurers adopted an active or dynamic approach that took into account business strategies and activities (including physical supply chain) with the goal of maximising market opportunities and profitability and cash flow."

While accepting that borrowing in local currency and managing working capital effectively can reduce the impact of currency fluctuation, Buckle adds that certain larger corporates have a preference to fund centrally for a number of reasons (including cost), so may elect to utilise synthetic funding options such as a cross currency swap as opposed to borrowing locally.

"We see several differences in EM FX hedging strategies," says van Tol. "The first is that exposure is managed from a portfolio perspective in which the imperfect correlations between the different currencies lower the exposure and hence hedging costs. Furthermore, corporates apply a shorter hedging duration in order to decrease costs of carry. Thirdly, more option structures are used to protect the corporate against specific event risks of a very material depreciation of the currency. The final difference is that macro-economic outlooks are used to determine a risk map or consensus on currencies to be used as guidance on hedge ratios.

"In order to reduce transaction risk, corporates can either change to invoicing in hard currencies or use FX adjustment clauses in their sales contracts. Whether this is possible depends very much on the market and sector you are operating in." Van Tol believes that treasurers need to change their approach, strategy and hedging instruments: investing in specialised exposure quantification and dynamic hedging strategies pays off but normally, as he explains, that is only perceived as such after the occurrence of an event risk – the depreciation of the Russian ruble or the peso crisis, for instance.

Goodwin observes that any increase in global risk or major tightening by central banks (particularly by the US Federal Reserve, likely in Q4 2015) will lead to a reduction in EM flows and amplified currency volatility. "Currency volatility itself doesn't make counterparty or credit risk more likely, but the causes of currency volatility do. The impending US interest rate hike is increasing volatility and makes countries with high proportions of corporate and sovereign dollar-denominated debt (much of Latin America, Angola, Kazakhstan) vulnerable to currency volatility while increasing the likelihood of capital controls."

External pressures

Welch acknowledges that the decision to expand operations into a new EM will come from the sales or manufacturing parts of a company and such momentum is often difficult to stop with treasury concerns about banking infrastructure or political stability. Companies with EM operations are likely to be supported by a reasonably sized treasury team, but EMs are often challenging, he concludes.

"External advice from the local offices of the major accounting firms is usually essential, together with advice from the global or local banks. There will also be a need for local financial staff and expertise, although they may not be officially part of treasury.

"The local banking facilities may be quite different from European banking, possibly with a higher usage of cash and cheques and less secure methods of collection and delivery. Practical local treasury management issues are possibly more time consuming than EM currency exposure management," he concludes. ■

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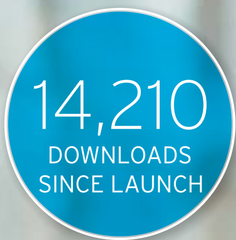

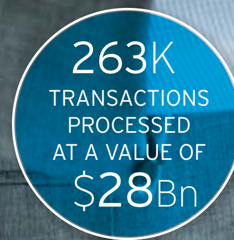

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Redback rising: RMB trade invoicing gaining traction

According to the latest SWIFT tracker, renminbi (RMB) has advanced to the fifth most widely used currency for global payments. With the value of cross-border deals settled in the redback more than doubling in 2014, it is not surprising that more multinational companies are choosing to invoice in RMB as they look to improve profit margins.

Opportunities for RMB cross-border trade settlement have developed rapidly since the first liberalisation moves in 2009. Today, there is a growing trend towards the use of RMB for transactions. Indeed, the latest SWIFT RMB Tracker data shows the Chinese currency has moved up from its position as the 20th global payment currency to fifth in the last two years.

Multinational companies (MNCs) are taking advantage of a number of benefits – whether to reduce foreign exchange (FX) risk and administrative costs, gain from potential RMB appreciation, or to expand and strengthen relationships in their supply chain ecosystem. In fact, there is growing evidence that companies can improve their negotiating position with Chinese customers and suppliers when the Chinese currency is used for trade invoicing purposes.

While there are strong incentives for companies outside of China to transact in RMB, not all companies are prepared to jump on the bandwagon at this point. What are the considerations that treasurers need to evaluate before making the switch to RMB as an invoicing currency?

Key benefits

For companies buying from China and selling overseas, especially MNCs executing inter-company transactions with their Chinese entities, settling such deals in RMB reduces exposure to FX risks. It also enables centralisation of FX management at the regional, group or in-house bank level, which allows for economies of scale and improved pricing negotiation. For example, entities are able to receive proceeds settled in RMB earlier (versus foreign currency receipts in China), facilitating improved cash flow forecasting and negotiation for better pricing terms. Other benefits include potential discounting from third-party suppliers and access to a larger supplier base.

For companies sourcing from overseas and selling to buyers in China, there are benefits to be gained with a simpler documentation process by using RMB (versus foreign currency payments) enabling a more efficient collection cycle and access to a larger customer base. For MNCs with significant intercompany flows with China, there are benefits in centralising the FX risks with an overseas function such as a treasury centre or in-house-bank versus using the local Chinese entity which may not have the know-how or primary responsibility to effectively manage FX positions.

Likely first-movers

With the benefits in mind, the types of companies most incentivised to adopt RMB at present are those with manufacturing and sales in the China market. These companies are typically in the fast-moving consumer goods, healthcare or industrials sectors. Naturally, it makes sense for these companies to offset their operational expenses in the same currency that is generated from their revenue. In addition, due to the benefits from FX hedging, companies with significant intercompany flows with China have also been the first to review and make the switch to RMB.

On the other hand, invoicing in USD is still the more convenient choice for US-headquartered companies since they can eliminate FX risk by trading in their home currency. Other Western MNCs may find managing USD FX risk to be less challenging than managing RMB risk. Similarly, transaction flows from businesses, such as electronics or oil commodities, where China is part of the supply chain and not the only supplier or buyer, will continue to be denominated in USD.

Weak currencies have served to bolster RMB appeal too. Recent depreciation of the euro, for example, has notably influenced the dynamic of European companies' adoption of RMB. Indeed, volatilities in the European currencies and other weak global currencies have prompted some companies to gradually increase their use of RMB in a bid to diversify and mitigate FX exposures.

Considerations before making the switch

Changing an invoicing currency is never easy as this involves a comprehensive review across all relevant business units and systems. A company needs to ensure there is sufficient implementation resources assigned to execute the change and the perceived benefits, as have been highlighted above, are sufficient to warrant the costs likely to incur.

The change to RMB trade invoicing needs to be a long-term strategy as it cannot be easily reversed given the rules and regulations in China and the potentially high switch-back costs. The following considerations should be evaluated:

1. Introduction of a new currency code – CNH

With the existence of two currency codes for RMB, namely onshore CNY and offshore CNH, companies will need to ensure that their treasury and dealing systems allow for trading in CNH as a new currency. In addition, any incremental risks, tenor availability and instruments available in accessing the CNH market needs to be considered in foreign exchange policies. It is the case too that the trade settlement currency for RMB remains as CNY and therefore may create currency/system conflicts which need to be reviewed.

2. Changes to trade documentation

While the RMB internationalisation initiative has simplified processing, there are still cross-border controls in place and nuances which companies must understand for effective implementation. Supporting documentation will need to be amended accordingly to ensure proper validation can be conducted by the relevant authorities in China. The list includes the intercompany trade agreement, purchase order, place of acceptance authority document and the invoice (the *fapiao* which is an official invoice registered at the local tax bureau and is used as a form of proof of purchase).

3. Understanding the nuances of RMB settlement

We have seen significant progress over the past few years, however compared to USD, RMB settlement is still very much in its infancy and there are several considerations that a corporate should be aware of in ensuring that their payment obligations continue to be fulfilled on a timely basis.

Additional information required for RMB payments with China

- CNAPS bank code.
- Detailed transaction details for reporting (RCPMIS/BOP).
- Accurate beneficiary name (in English).

Other considerations

- Different clearing and settlement systems can result in varying payment cut-off times and holiday handling schedules.
- Beneficiaries can access the funds once they are received by the bank in China.

4. Benefiting from the different programmes in China

Moving on from simplifying processes for current account activities, the country has seen the introduction of payment programmes stemming from the Shanghai Free Trade Zone (SFTZ) and nationwide initiatives allowing payments to be performed on a net basis or on-behalf-of. These programmes allow companies to conduct payments with China on a more streamlined basis, as they do in other more developed countries.

The RMB journey continues

Without doubt, RMB internationalisation will accelerate. Over time, this will introduce incremental changes and flexibility offered by way of pilot programmes such as other Free Trade Zones, as well as improvements to cross-border controls and processes.

There will be potential tipping points for increased RMB invoicing going forward, and Citi continues to lead the way in helping clients to evaluate the opportunities created from ongoing regulatory reforms. At the right time, and specific to a company's needs, RMB invoicing can certainly open new doors for companies – whether by negotiating cost savings or pursuing attractive new trading relationships with buyers or suppliers only willing to trade in RMB.

The key for treasurers is to start preparing their companies to make the timely switch when the opportunity arises.

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Safety in numbers

M&A deals are on the up globally and in Asia in particular; 2014 saw the region present the highest total value of deals on record. What are the important legal, financial and organisational factors in making a deal and what role can the treasury play to ensure success?

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

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

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

One of the causes of the breakdown of outward bound deals is the failure of companies to fully understand the cultural, legal and political environment of their foreign target businesses. Of the 120 failed outbound Chinese deals between 2005 and 2014, CDN claimed that about a quarter were due to political reasons. The China Centre for

International Economic Exchanges cites a "lack of talent familiar with international practices" as being a "major shortcoming" for Chinese companies in overseas markets. This signals the need for qualified input from a range of functions.

A legal perspective

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

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

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

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

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

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

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

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

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

How can the banks help?

In terms of preparation for a deal on the finance side, there are many different dynamics to consider, explains Alexandre Huet, Global Head of Strategic and Acquisition Finance, Société Générale. As a banker, he naturally considers it more provident for buyers to prepare well in advance wherever

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

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

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

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

The treasurer's role

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

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

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

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

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

Communication is the key

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

Jeanette Chang

Treasurer, Asia Pacific

Founded in 1911, IBM is a multinational technology services and consulting company with global headquarters in Armonk, New York. IBM manufactures and markets hardware and software, and offers infrastructure, hosting and consulting services in areas ranging from mainframe computers through to nanotechnology.

Problem…

Like many companies operating in China, IBM historically had restrictions with moving cash in and out of the country. Traditional structures to fund working capital either created entrustment loans which are inefficient, or required onshore bank financing which was more expensive than using internal sources of cash. As a result, IBM experienced an increased cost of doing business in China. Each local entity conducted their business directly with offshore IBM entities and vendors which generated high volumes of two-way, cross-border, foreign currency payments with associated compliance requirements. The model was decentralised with foreign exchange (FX) conducted at the entity level with limited opportunities for consolidation.

…Solved

The regulatory changes introduced in the first half of 2014 by the State Administration of Foreign Exchange (SAFE) provided an opportunity for IBM to implement a more efficient and effective cash management solution in China. IBM could now centralise working capital funding and FX management to drive down costs whilst also integrating China into the group's global in-house bank. Working with Citi, IBM received approval from SAFE under the Foreign Currency (FCY) Centralised Management Programme in November 2014 to implement a new solution under the FCY Pilot Programme. SAFE allowed IBM to utilise its entity registered in the Shanghai Free Trade Zone (SFTZ) to roll out a number of solutions including: an automated FCY cross border pool between the SFTZ and London, a FCY intercompany netting solution, and a FCY payment on behalf of/receipt on behalf of (POBO/ROBO) solution to streamline 3rd party transactions.

Citi was selected to work on the project after IBM conducted a thorough RFP process. "The FCY Pilot Programme has helped solve many of the challenges that we faced in China," says Chang. "We are now able to bring cash in and out of the country thanks to the cross-border pooling structure and this offers much greater flexibility in funding." Although there are still limits to the amount of cash that IBM can move in and out of the country, the automated nature of the solution means that IBM can keep within the SAFE borrowing/lending quotas whilst minimising the actual amount of foreign debt quota leveraged. "The fact that the limit applies to the whole group and not each individual entity also gives us the flexibility to make sure that the correct entity receives funding at the right time," adds Chang.

The unique approval from SAFE allowed all FCY intercompany netting settlements to be settled in RMB which, aligned with an automated domestic RMB cash pool, meant that IBM was able to eliminate all but one of their FCY accounts in China and could move working capital funding more efficiently to their China entities. Citi's solution has streamlined payment supporting documentation, significantly reduced the number of cross-border payments, reduced transaction costs and centralised FX to save on FX margins. The solution has also allowed IBM to centralise and standardise treasury processes in China to be the same as their global in-house bank. Significant operational, administrative and funding efficiencies have been generated. "Combined these benefits have brought numerous cost savings and allowed us to leverage economies of scale to obtain the best deals reducing the cost of doing business in China," says Chang.

The structure that IBM has implemented demonstrates how SAFE has made China a more business-friendly environment in which to operate. "If you compare what we can do now, with what we were able to do a few years ago, it is a remarkable change and most, if not all, of the roadblocks that previously prevented a treasury efficiently operating in the country have now been removed," says Chang. "This is something that we greatly appreciate and I am sure that going forward many more companies will be able to reap numerous benefits from these changes." ■

Yigen Pei, Country Head, China, Treasury and Trade Solutions at Citi comments: "Citi's innovative solution for IBM demonstrates the benefit of combining excellent local regulator relationships with an integrated cash management platform. We are helping clients across all industries leverage the latest regulatory developments that enable China to be included into global treasury processes which drive significant cost savings and operational efficiencies such as those achieved by IBM."

Doing the heavy lifting

Rajan Gupta
Group Treasurer

Whether it is augmenting HYVA's working capital management, or navigating his company through one of the highest periods of FX volatility in decades, Rajan Gupta, Group Treasurer has long been comfortable with the heaviest of workloads. In this article, he tells us what attracted him initially to treasury and why the role continues to excite him to this day. He also explains how he managed to get on top of group liquidity management at a Dutch multinational that places a high value on local autonomy.

HYVA (HYVA Group BV) is a global multinational company based in the Netherlands, with a treasury centre in Hong Kong which co-ordinates cash management and funding for the group across 43 subsidiaries worldwide. The company is committed to the development, production, marketing and distribution of components for the commercial vehicle industry, and is one of the world's biggest brands for hoist cylinders and container handling equipment.

Early on in his career, at a time when he was still working in the Home Finance division of Deutsche Post Bank, Rajan Gupta was invited to give a speech to the 'who's who' of Indian finance about the mortgage backed securitisation products (MBS) he had helped to roll out for the first time in India. "After that I was known as a securitisation expert," he recalls.

That Gupta was once known as an expert in the field of securitisation reveals a lot about both his personal character, and approach to his job as treasurer for a large multinational company. Securitised products are, of course, infamous for their complexity. Even the former Chairman of the US Federal Reserve, Alan Greenspan, who is renowned for his sharply analytical mind and aptitude for quantitative problem solving,

admitted once to finding such products baffling, describing them as being "beyond human understanding." That Gupta does indeed understand securitised assets and, moreover, can boast a level of expertise in these notoriously opaque products reflects just how adept he is at making sense of highly complex financial issues. It is a skill which, as we will see, has since served him very well in his career as a corporate treasurer.

A vital role

At a renowned Indian university, Gupta had originally studied law. Yet by the time he began working towards his MBA in Finance at the Institute of Management Technology in Ghaziabad, an earlier ambition to join the bar faded as he became captivated by financial matters. Treasury had a particular appeal as it resides right at the core of corporate finance. "That excites me," he says. "It is the degree to which treasury impacts on all aspects of the company. I always wanted to be involved in the active part of finance, and that is how I ended up in treasury."

Naturally, there were several career defining moments along the way. The first of these came when he received his initial induction into the world of treasury after being hired in 1999 by Korean conglomerate Daewoo Motors, then one of the largest companies in the world. At that time, Daewoo was attempting to establish a factory in India from which it would export to Europe and the Americas. The projected cost was $1bn, meaning the business had to leverage itself considerably to finance the venture. It was, says Gupta, the perfect induction to the work of a treasurer.

"That is where you get tremendous exposure. Any financial instrument you can think of – it was all there. In that first role I was exposed to so many different instruments and practices in the treasury; it was a conduit for innovation and work satisfaction as well."

The second career defining moment came later on, after he had left Daewoo to take up a role as a senior manager in the Deutsche Post Bank, working specifically in the area of home finance. Here he played an integral role in the launch of the first MBS products in India. "For the first time, my company actually endorsed my initiative, and I worked closely with a subsidiary of India's central bank in the roll-out of the product." When he was invited to a conference to explain the structure of the product to some of the most eminent names in Indian finance, he realised he was building quite a reputation for himself. "That helped me to define my career and, ultimately, opened the door for me to move to a bigger role."

Another career defining moment was joining Nortel Networks of Canada, at one time was one of the most renowned telecom companies of the world, "which opened doors for me to the international treasury and with a special focus on APAC treasury."

The Dutch way

After a brief spell working in the Hong Kong treasury of Australian telecommunications giant Telstra International, Gupta finally walked through that door, taking up the role of Group Treasurer at HYVA. The first thing that Gupta noticed when he arrived at HYVA was the company set-up being very different from that of most other multinational companies. In Holland, where the company is headquartered, there has long existed an entrepreneurial culture that attaches great value to local autonomy, he explains.

But how does this Dutch business trait shape the decision-making process on treasury matters? "Here all the entities are responsible for their own matters," he says. "In recent years, we have put strong focus on centralising various process and procedures while maintaining a level of local autonomy and we were quite successful in doing so." Gupta, as Group Treasurer, will propose the strategy and, once approved at board level, he will talk to the local finance managers responsible for executing what has been decided and keep a track of the progress, in coordination with local management. "Each country where we operate has its own finance manager. These local finance managers are my eyes and ears on the ground, and they are the ones responsible for executing the strategy that we decide upon," he says.

Overhauling working capital

Local autonomy is indeed a deeply embedded value at HYVA. However, that definitely does not mean that the various entities are permitted to use inconsistent, erratic processes. Especially on working capital front, to support working capital optimisation, Gupta developed internal policy on Accounts Receivable (AR) and Accounts Payable (AP) management, which helped the company to further streamline working capital management.

"We put together a policy on how debtors should be managed and in this policy we have defined processes and procedures – how and when we should chase them, how and when we should follow counterparty credit limits and so on, including covering the risk using credit insurance products."

> "These local finance managers are my eyes and ears on the ground, and they are the ones responsible for executing the strategy that we decide upon."

In the post-crisis environment, where liquidity is still drying up and nearly every company is looking nervously at the Days Sales Outstanding (DSO) metrics, optimising the collection process has proved quite challenging, notes Gupta. Yet HYVA has seen significant improvements in this area in recent years. It is nearly all down to the adoption of a two-pronged approach to debtor management, he explains.

The policy was not especially radical, but it sure was effective. In order to further optimise working capital as a next step HYVA is trying to set up receivables discounting programme for some entities, wherein invoices are automatically discounted on the first day and we get the money into the our bank account. "These measures actually help a lot in terms of working capital and also on the debtor risk management perspective," he notes.

Managing uncertainty

It is in times when the economic climate turns gloomy that measures to optimise working capital management, such as what HYVA introduced, really begin to show their value. The recent market turmoil in Europe, reignited by the election in January of the anti-austerity party Syriza in Greece, has created precisely that kind of environment for many global

businesses, HYVA included. The euro, already down on the ECB's announcement of a new programme of quantitative easing, has taken a mauling against other G10 currencies this year, particularly the US dollar. That working capital management is now performing more efficiently, therefore, is probably just as well as Gupta is now heavily occupied in keeping an eye on the group's multiple currency exposures.

> "In my opinion, hedging should be balanced. It should never just be fixing the whole lot, because then your upside is gone."

Why has the euro's recent plunge against the US dollar proved such a headache for Gupta and his team? After all, HYVA are domiciled in the Netherlands and use the euro as their transaction currency in Europe. The explanation, says Gupta, is that with a dollar denominated bond listed on SGX worth $375m, HYVA is a US dollar function globally, and movements in the euro impact the company both in terms of transaction and more importantly translation risk and such significant EUR movements will become more and more a matter of concern.

Of course, the euro may be the biggest but it is far from being the only FX concern for the companies at this moment in time. Latin American currencies have suffered from rampant inflation and geopolitical tensions and the falling oil price precipitated a collapse in the Russian rouble on a magnitude beyond anybody's imagination only a year ago. All in all, FX volatility has now reached its highest non-crisis level in two-decades, according to recent research by Bank of America Merrill Lynch (BofA Merrill).

When deciding upon the FX risk management policies to be executed across the group's various subsidiaries, Gupta is eager not to be overly aggressive. "First of all, I'm not in favour of hedging everything," he explains. "In my opinion hedging should be balanced. It should never just be fixing the whole lot, because then your upside is gone." Wherever possible, Gupta prefers to find a natural hedge. On the transaction side, for example, HYVA is managing its Russian rouble risk, not with the help of derivative products, but by funding the contract of the customer in euros or in hard currency US dollar which lessens, considerably, the impact of the currency's current volatility.

Regarding translation risk, HYVA has to date not put a policy in place to actively hedge their exposure, like a majority of multinationals. The sheer scale of the recent market volatility means this strategy is far from being set in stone, however. "I think translation hedging may be necessary, given how markets are performing at the moment," he says. "If you have a very big exposure in a BRICS market and that market is in trouble then however well you perform there, the balance sheet will probably not reflect the same. It can be a big risk, especially on your financials. So I am in favour of hedging translation risk, although not in favour of hedging everything."

That HYVA is not hedging every exposure across its 40 global entities is probably just as well for Gupta. Since hedges are decided and executed centrally, FX risk management is, as he says, already a very big job. "That's taking up an awful amount of my time," he says. "It involves looking at the way transactions flow in certain countries, the inter-company relationships, flows of goods and invoices, transaction currencies and finally ways to reduce FX exposure or establish natural hedges at first place before using external instruments to hedge the FX risk."

And that doesn't look like it is going to change anytime soon. On the contrary, Gupta is likely to be spending more time in the weeks and months going forward working out whether the company's strategy needs to change in order to account for the extraordinary volatility we are currently seeing. "We will be looking at how we can best manage the volatility, especially on the translation side to address the volatility ensure we don't take hits from month to month on our balance sheet."

Scaling the refinancing wall

That pressing task, along with HYVA's ongoing efforts to optimise its use of liquidity, means that there will be plenty of challenges for Gupta to get his teeth into over the course of the coming year. And that's even before taking into account of the refinancing of the biggest financial instrument on the company's balance sheet, the $375m bond due to mature in March next year (the year that many ratings agencies and other commentators, such as auditors KPMG, believe will mark the summit of the next refinancing wall).

In current times, companies are generally looking all the possible refinancing options and not sticking a single source of funding. Generally yields are at peak level in the Asian bond market and therefore bonds are not so attractive source of funding, as it used to be few years back. The syndicated loan market globally has been quite active and many companies have managed to fund themselves.

Gupta is confident that for a business of its type and size, HYVA is well positioned, and he will be putting in the hours in the coming months to lock in new funding at an appropriate rate. "There is a lot of work around making sure we have refinancing in time, at the right price and in the proper condition. That is one of the biggest current projects we have and it is certainly keeping me occupied," he says.

An expanding role?

It's a heavy workload, unquestionably, but that's just how Gupta likes it. In fact, that, along with his love for numbers and mathematical problem solving, is one of the principle reasons why he sees himself staying in treasury for a very long time. Like most treasurers, he would one day like to reach the level of CFO, but that is not an ambition he is set upon realising in the immediate future. There are simply so many exciting things going on in treasury at HYVA at the present time, testing daily his analytical talents, to allow him to ponder such possibilities for too long.

"I like challenges, and deadlines," he says. "So I think I'll stay on the treasury side for some time." Ever keen to broaden his skill-set, however, he does admit he hopes to have the opportunity to delve into new areas around the periphery of treasury – such as accounts, budgeting or tax – in the coming years. Since these are areas that require a high level of specialist knowledge and expertise, they are not usually seen as the domain of the corporate treasurer. But for an individual once recognised by his peers as an expert in securitisation, one wouldn't bet against Gupta quickly becoming an authority on these matters too in the coming years. ■

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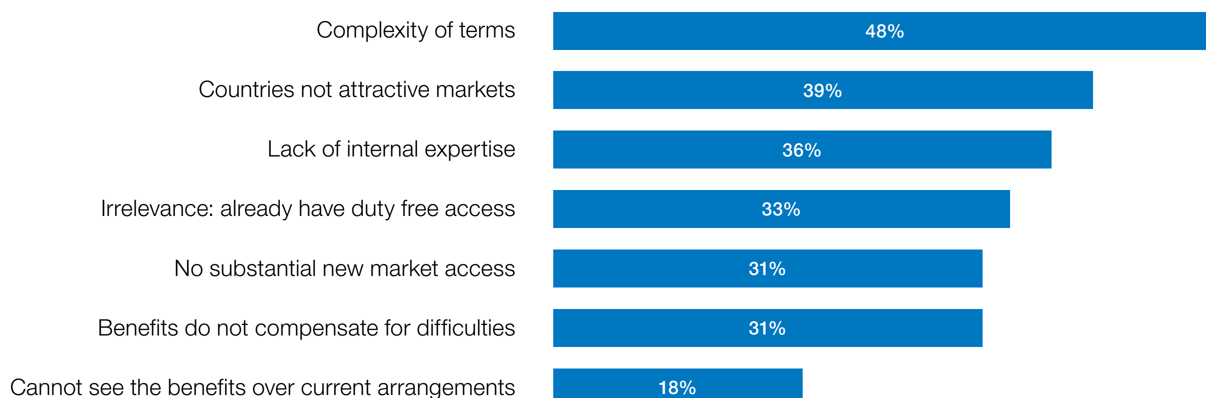
The trouble with preferential treatment

While free trade agreements continue to proliferate at a remarkable pace in Asia, the utilisation rates are on the whole negligible. Is this because governments have not effectively communicated the benefits? Or are FTAs simply not all they are cracked up to be?

A well-known economic priority for many governments in Asia of late – and indeed in much of the Western world – has been to encourage companies to pursue a global strategy. Globalisation and technology have made the world a much smaller place and the companies today that don't explore growth opportunities beyond their own shores are likely to drown in a sea of competition.

That makes sense. Ever since the economist David Ricardo observed that countries do well when they focus on what they are relatively good at producing, the benefits of free trade have never really been in doubt. However, governments should bear in mind that, counterintuitive as it sounds, the benefits of Free Trade Agreements (FTAs), which in Asia have been the dominant channel through which governments have sought to foster greater cross-border business, are not quite so evident.

Just look at the figures. While Asia has seen an enormous proliferation of FTAs across Asia in recent years – both bilateral and regional – utilisation rates of Asian FTAs are notably low. Usually uptake by businesses ranges between a mere 10% and 20%, according to Asia Development Bank (ADB) figures. Often the fact that few businesses seem to be taking advantage of FTAs open to them is blamed on poor communication. There is a common line of argument that says FTAs would see much greater uptake if only governments did more to publicise their existence to



Source: Economist Intelligence Unit

treasurers, Chief Procurement Officers (CPOs) and other key corporate decision makers.

Last year a HSBC sponsored study by the Economist Intelligence Unit argued this exact point. The survey revealed that of the 800 businesses – large and small – that were surveyed across a total of eight different jurisdictions, only 26% are using the FTAs that have been established. If you dig down a little further into the data, only 19% were taking advantage of bilateral FTAs, the agreements that have been most common across the continent. Does this apparent lack of enthusiasm for FTAs from the region's exporters reflect the fact that exporters see no value in the agreements? Other findings suggest that this is not the case. Of the 26% who use FTAs, 86% reported that their exports had seen an increase as a consequence of trading under the terms of the agreement. An additional 24% told the researchers that they their exports had increased significantly as a result of their participation.

Legal minefield

Not everybody is convinced this is always the reason, however. One alternative explanation is that companies are by and large aware of FTAs negotiated between countries where they do business; but they simply do not have the time, expertise and resources to make sense of what they need to do to take advantage of them. Usually certain complex criteria must be met in order for goods to be exempted from import duty or qualify for lower rates. And when you think about the number of FTAs in place across the Asia region, each containing perhaps hundreds of pages of dense legal text it is not difficult to imagine some companies reasoning that utilisation is not worth the hassle.

"Currently, the Rules of Origin differ in each FTA negotiated and it is not easy for laymen to comprehend the legal text of the concluded FTA," says Angelia Chew, Partner, Trade & Customs, Indirect Tax at KPMG in Singapore. "Although the benefits of FTAs are clear, the cost of not meeting these criteria is hefty. Customs authorities in the region are aggressively conducting FTA audits. Any non-compliance will result in penalties and interest payable on top of the duty shortfall. Many companies – including multinationals and small-medium enterprises – give up on applying for FTAs as they do not have sufficient resources to fully understand the rules in the agreements and are unable to manage compliance concerns."

Can anything be done to resolve this issue? Well, as often is the case when complexity is the challenge, technology is one possible solution (for those that the initial outlay is not prohibitively expensive, of course). There are on the market a whole range of automation models that can integrate FTA functionality with company Enterprise Resource Management (ERP) systems and leverage the capability of similarly integrated Global Trade Management (GTM) systems.

Solutions like these work by allowing companies to solicit and store origin data from suppliers, and calculate the origin for manufactured products. In addition, they can also make it easier to generate and track origin requests. All in all such tools such as these can provide companies with a structured, controlled process through which to calculate preferential origin and, importantly, eliminating the fear of non-compliance by ensuring everything is in place ahead of customs audits.

There is also another, third perspective on the issue. "I don't think it is about information," says Jayant Menon, Lead Economist, Economic Research and Regional Cooperation Department, ADB. Analyse the detail of the vast majority of FTAs and the rationale of those companies choosing not to utilise an FTA soon becomes apparent. "In a lot of these agreements, the difference between the preferential rate provided by the FTA and the normal Most Favoured Nation (MFN) rate, the difference is quite small or even zero.
For some tariff lines, where there are much larger preference margins, utilisation might be higher and could be increased by more information. But by and large the problem is that the margins are simply not there to worry about using them."

The fourth explanation relates to Asia's distinctive trade relationships. As a recent ADB Working Paper on the matter points out, about two-thirds of intra-regional exports consists of intermediate goods (eg parts and components) and much, if not all, of this trade already travels duty-free, or at very low rates.

There are several reasons. First, a significant proportion of the parts and components being traded are electronics exempt from tariffs under World Trade Organisation's Information Technology Agreement. Second, many of these intermediate goods may also be subject to duty-drawback schemes under which tariffs can be waived. Then the last point to make, which is applicable to final as well as intermediate goods, is that tariffs have been in any case been declining in the region in recent years irrespective of any FTAs.

Too many FTAs

Governments in Asia should take note. There are currently more than 100 FTAs in place over the region, and many more still being negotiated. With the negotiation of each of these agreements using up considerable time and administrative resources, one would think it sensible to at least consider whether there might be more effective means by which greater intra-regional trade can be facilitated. FTAs, remember, are but one way to encourage trade and, in fact, can sometimes encourage the wrong kind of trade ie trade diversion.

That quickly becomes a vicious circle. Non-signatory countries, not wishing to lose market position, will endeavour to negotiate their own agreements. "They feel forced to come into the game and sign FTAs with others," says Carlos Kuriyama, Senior Analyst at the APEC Policy Support Unit, Asia Pacific Economic Cooperation (APEC). "Everyone then wants to have preferential treatment over others and it creates distortions." No wonder we've seen such a proliferation in bilateral and regional agreements in Asia-Pacific over the past ten years. FTAs, it seems, beget more FTAs.

> "My view is that we've got to the point where there are so many FTAs, that they are becoming a burden rather than a benefit."
>
> Jayant Menon, Lead Economist, Economic Research and Regional Cooperation Department, ADB

"My view is that we've got to the point where there are so many FTAs, that they are becoming a burden rather than a benefit," says Menon. Radical though it may sound, instead of wasting yet more time and energy negotiating yet more agreements with one another why don't policy-makers, Menon asks, focus on harmonising what is already in place and offer the accords to everyone on a non-discriminatory basis? This would be advantageous in two respects. "If you offer it to everyone, you would have lowered your barriers to trade and you've reduced your cost of administering multiple FTAs and multiple rules of origin. It would encourage greater trade and, ultimately, isn't that the real objective of an FTA?"

That would appear to be the kind of thinking that has informed the Beijing-backed plans to establish a vast, Free Trade Area of Asia Pacific (FTAAP). At the APEC summit held in late 2014, the Chinese President Xi Jinping announced that the bloc had "approved the roadmap for APEC to promote and realise the FTAAP." It was a 'historic' step, he added, and one which reflected the "confidence and commitment of the APEC members to promote the integration of the regional economy."

> "Companies should start seriously considering how they can best use FTAs to reap the benefits of duty savings as soon as possible."
>
> Angelia Chew, Partner, Trade & Customs, Indirect Tax, KPMG, Singapore

Despite China's apparent optimism there is no doubting that the diversity of markets in Asia will pose a big obstacle that will need to be overcome if this objective is to be realised. After all, one of the reasons that FTAs are so popular is that in most cases they involve fewer countries and so differences are easier to iron out. "It is possible for the Asia Pacific free trade area to become a reality in the next ten years but the biggest challenge lies in harmonising the rules of all the various FTAs signed," says KPMG's Chew. "While this will take some time, companies should start seriously considering how they can best use FTAs to reap the benefits of duty savings as soon as possible."

If negotiations over the so-called 'mega-regionals' – the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (R-CEP) have become protracted, how long will it take to reach consensus between every economy in the region? If those can be concluded though it might just pave the way for something bigger. "Right now there are some big regional agreements being negotiated and if these don't see the light of day it's going to be hard for a free trade area across the Asia-Pacific to become a reality," cautions APEC's Kuriyama. "But I think those regional agreements, if they can be established, could serve as a stepping stone to something like the FTAAP."

What now then? As negotiations over the so-called 'mega-regionals' – the contentious TPP and R-CEP – roll on, Menon's observations raise the question of whether such agreements are worth pursuing at all. What precisely would be gained by those deals, even in the best-case-scenario? "We will end up with a fragmented world trade system carved up into different trading blocks," he says. "This will not be good for members, or for non-members."

Indeed, neither, perhaps, is that the type of distortion-free trading paradigm that David Ricardo had in mind when he articulated his theory of comparative advantage. To rework an old saying of the great Chinese philosopher Confucius, one might say that trade is actually really simple – it's just that the governments of countries sometimes insist on making it complex. ■

Mobile treasury: just a corporate convenience?

If you take a quick look around you, it is likely that a smartphone or tablet computer won't be far away. The evolving habits of today's consumers and corporates mean that expectations for mobile applications to be available anytime and anywhere are increasingly commonplace. But how comfortable are treasurers with mobile channels and how committed are their banks to investment in mobile technologies?

Developments that offer great potential to increase the productivity and improve the flexibility of the treasury function are normally welcomed with open arms. And mobile technology should be no exception, especially in this day and age. "With increased travel commitments and the need to fulfil multiple roles, the ability to manage their company's transactions – amongst other functions – on a mobile device is going to be invaluable to corporate treasurers," explains Marie-Caroline Domingo, Head of Client Access for Global Transaction Banking in Asia Pacific, Deutsche Bank.

But mobile technology has thus far had somewhat of a mixed reception from treasurers, which many put down to its novelty and intangibility. Completing banking transactions and associated activities on mobile devices in the corporate world is "a relatively new phenomenon for treasurers," explains Ankit Goel, Treasury Manager at Bharti Airtel.

This is in stark contrast to the general consumer uptake for mobile banking – which has been impressive, with solutions on offer from all of the major retail banks. These are typically used to complete payments and authorise transfers of small amounts.

In the business world, however, "corporates are dealing with transactions of significant value so a lot of reassurances with respect to security are required," Goel explains. The result: developments aimed at corporates are inevitably, albeit appropriately, slower.

Smart choice

The relatively slow adoption of mobile services in the treasury function has not been helped by the lack of available services from banks. Aite Group reported in September 2014 that 63% of global banks are yet to offer corporate mobile banking. "Traditionally, corporate banks have underinvested in digital technology," says Thomas Zink, Research Manager for IDC Financial Insights. But now that is starting to change.

Deutsche's Domingo explains how her team have taken time to gather feedback from clients which has been vital in shaping the bank's mobile developments. "We have adopted a relatively conservative stance in rolling out mobile services because we wanted to ensure, from direct feedback, that any development addressed a problem for our corporate clients and created real efficiency for them."

Emerging considerations

Unlike desktop computers, mobile devices can bridge a gap created when access to fixed infrastructure is not possible – which is not an uncommon challenge among Asia's emerging economies. Thankfully, the processing power of tablet computers and smartphones is further increasing and high-speed internet connections continue to improve across Asia. The benefits of which, according to Nidugondi, can be of assistance to consumers at either end of the development spectrum experienced in Asia.

For example, when traditional bricks and mortar banks aren't financially feasible, how do you reach potential clients that require access to the organised banking services? "For the unbanked or underbanked in emerging markets, you can use innovative mobile methods to reach isolated areas and address the needs of this segment." Bank representatives from Bank of South Pacific are using tablets to sign up consumers and businesses to financial services in rural areas of Papua New Guinea, for example. Users can then transfer funds and make payments using their mobile phones.

However, as frequently seen in the region, the great disparity between individual nations is problematic for mobile innovation. For instance, Bharti Group's Goel explains that "Indian banking is highly regulated by Reserve Bank of India; hence major banks are still to come up with mobile banking solutions. It is the MNCs and private Indian banks that have started to offer solutions."

Based on the different infrastructure and maturity levels of each market, solutions can take different forms but, regardless of the target end-user, "the reality is that, in addition to electronic banking regulation, there are also local outsourcing and local data privacy requirements to comply with," explains Tony McLauglin, Regional Cash Product Head for Asia Pacific at Citi. Going live with a mobile solution is dependent on compliance and "it's something we go through market by market."

Similarly, Arafat Sheik Jabbar, Head of CitiDirect Asia Pacific at Citi, explains that by continuously gathering user feedback, Citi has been able to optimise the intuitiveness of their corporate mobile solutions. And, the smart choice in taking time to advance is paying off. According to Srinivas Nidugondi, Head of Mobile Financial Solutions for Mahindra Comviva, "mindsets are changing and corporates are quite excited. Aside from mobile payment solutions being a 'current' thing to talk about, a lot of them are beginning to see benefits in this overall way of doing transactions as well." Sheik Jabbar cites the delivery of time-critical information – such as access to balance information, status updates and alerts – remotely and on demand as an example of how mobile solutions are helping treasurers make informed decisions whilst on-the-go. "Additionally, treasurers are able to translate financial data into global business intelligence with just few taps on their tablet, viewing data globally, by region or country and filter by currency, amount, country in map or chart views."

Initially, corporate mobile applications were largely informative, providing notifications for the end-user but newer solutions are becoming more interactive and action-orientated. "In Asia, we have seen an increase of functionality being added to the mobile platform," says Citi's McLauglin.

Solutions on the move

As corporate treasurers grow more comfortable with mobile channels, and the services on offer undergo development, the desire to perform more sophisticated treasury-related tasks via the medium of mobile is increasing. For example, Aite Group's survey of 45 corporate treasurers in May 2014 revealed that 51% of respondents ranked approving wire payments as 'important/critical' and 46% believed initiating wire payments would be 'nice to have'. According to Zink, "changing corporate client preferences – looking for fast fully-integrated solutions, lean processes, 24/7 access via the web and mobile devices – goes hand in hand with the evolving role of treasurers in modern enterprises." Treasurers are more accountable for the regulatory compliance and cash positions of their organisations and management ultimately relies on their insights to make the right decisions at the right times.

The treasurer's traditional role also requires more effective payments mechanisms and accurate cash flow forecasting. This translates into a need for an accurate, real-time and comprehensive view of the liquidity position of an organisation – increasingly on the go, Zink explains. Moreover, further "technological advances like integration with ERP, elimination of hard token login requirement, user friendly applications in a complex multi-entity and multiple accounts banking structure, productivity will definitely improve," says Goel.

But is such productivity for everybody? For Damian Glendinning, Treasurer at Lenovo, some responsibilities certainly shouldn't be mobile-based: "Typically, we tend to be formal about the payment approval process. Mobile suggests the tendency to do things on the move – if you're on the tube home or waiting in a queue – and in my view, that's not the appropriate environment.

"Payment enablement, however, is very different from passive consultation of bank accounts. If you're waiting for confirmation of payment, for example, then this can be done

in a less formal environment." KyongSun Kong, Analyst for Asian Financial Services at Celent explains that corporates sometimes prefer face-to-face and formal interactions due to more intricate requirements.

There is some disparity in opinions but certainly, for Zink, greater data analytics and business intelligence capabilities are playing a crucial role in allowing banks to mine large amounts of data increasingly near real-time, while data visualisation and dashboarding makes data more actionable and easier to digest – particularly on mobile devices. Celent's 2014 survey Mobile Banking in Asia indicated that growth in transaction volume is the top driver encouraging banks to enhance their corporate mobile banking capability.

Evolved security

Perhaps the largest barrier to adoption remains concerns over security. There is a degree of resistance towards the idea of allowing corporates access to networks over mobile devices. However, the perception that mobile technology is inferior regarding security is reducing as users become better informed. "The same security that exists in the desktop world also exists in the mobile and tablet world," explains McLauglin. Information is carried using the same bandwidth and, with the exception that a mobile device does not have a fixed IP address, security measures are applied in largely the same way.

> As corporate treasurers grow more comfortable with mobile channels, and the services on offer undergo development, the desire to perform more sophisticated treasury-related tasks via the medium of mobile is increasing.

There is an aspect of joint responsibility where, as Goel explains, "it is important that banks create awareness among the corporates about the security features, data transmission capabilities and authentication mechanisms" but mobile security also depends on the user being receptive to education on safe computing and internet practices. For Nidugondi, "users need to be careful: the weakest link is usually the human. It is a case of educating the user – this is where I believe the adoption curve has been a little slow."

Mobile dashboard

Against this backdrop, creating a suitable mobile treasury dashboard or application for corporates inevitably involves a balance between convenience and security. The most frequent solution to achieving this balance is ensuring the levels of security change depending on what the user wants to do. "For example, the user could view a report without a process of authentication but to view balances one level of authentication would be required. To complete a transaction, identification via a touch ID or transaction pin would be necessary," explains Nidugondi.

In Domingo's experience, corporate clients generally understand the security mechanisms that have to be in place, accepting the trade-off in terms of what security procedures are required for certain activities. But security should not compromise the user experience. Indeed, collaborative efforts between corporates and solution providers are increasingly commonplace in creating user-friendly yet secure applications. "The key driver behind corporate mobile banking services is the client. Certainly market requirements are putting pressure on banks to deliver increasingly innovative solutions as well but the client's user-experience is driving developments," says Domingo.

"You can have all the bells and whistles but if the user experience is bad, then it's not going to work," says Nidugondi when describing his own frustration as a user filling in a mobile app registration that required his country code once, only to be asked for the same information again at a later stage. After all, treasury departments are staffed by consumers, and their experience of technology in their personal lives can influence the technology they do or do not introduce into the corporate treasury.

At Deutsche Bank, Domingo explains, they benchmark themselves against what their clients perceive to be a good user experience. "What we know is that client preferences are becoming more and more influenced by the use of online tools outside of the banking industry – social media applications or search engines – and clients are expecting the same ease of use and convenience for their banking applications."

Tapping into success

Despite certain barriers to the adoption of mobile technology, most believe "the future of mobile banking is bright and strong," explains Goel.

However, it remains uncertain whether everyone will be willing to adjust their working habits in accordance with mobile developments. The convenience factor, for Glendinning, is limited to general office expenses (such as ordering pizzas to a meeting or arranging for flowers to be delivered) where mobile-enabled credit card accounts are encouraged.

Simply judging by the percentage of corporates still relying solely on desktop methods, persuading them to become avid mobile users could take longer than the banks expect. However, adoption of mobile treasury is predicted to "increase and intensify", says Zink but "corporate mobile banking is rather characterised by slow evolution than by revolution."

Arguably, the APAC region is progressively digital, gradually adopting mobile solutions for ubiquitous access to treasury tools. And as technology matures, processing power increases, and data integration deepens, the value for corporates will increase. The true added-value, however, will always come from the skilled corporate treasurer. Ultimately, it is up to them to decide whether and how mobile channels will influence their strategic decision-making going forward. ■

Key facts

Geography and society

Population: 81 million (2014 estimate)

Population growth rate: -0.18% (2014 estimate)

Capital city: Berlin

Time zone: CET

Land boundaries: Austria, Belgium, Czech Republic, Denmark, France, Luxembourg, The Netherlands, Poland, Switzerland

Coastline: 2,389km

Economy and business sector

Currency: euro

Financial capital: Frankfurt

GDP annual growth: 0.1% (2013), 1.6% (2014)

GDP per capita: $44,700 (2014 estimate)

Ease of Doing Business rank: 14th (2015)

Index of Economic Freedom: 16th (2015)

Politics

Government type: federal republic

President: Joachim Gauck

Chancellor: Angela Merkel

Trading partners

Top import partners: Netherlands, France, Belgium, China, Italy, UK, Austria, Russia, Poland, Switzerland, Czech Republic

Top export destinations: France, Netherlands, US, Austria, China, Italy, Switzerland, Poland, Belgium

Country credit rating

AAA

Germany: Europe's powerhouse

Positive sentiment in Germany has been gaining momentum over the last year – and there is good reason to be optimistic. Treasury Today Asia examines the economic forces driving the country's growth, and outlines Germany's suitability as a gateway to Europe for Asian businesses in search of expansion.

Germany is the largest economy in Europe and the fourth largest by nominal GDP in the world. At the start of 2015, despite the turbulence being experienced across the rest of the Eurozone, Germany's economics ministry increased the country's growth forecasts from 1.3% to 1.5%. Moreover, 2015 GDP growth forecasts of 2.2% from EY and 1.6% from HSBC research cement the country's return from a mid-2014 slump.

Lower oil prices, currency depreciation and a robust labour market have acted as a stimulus for better-than-expected domestic consumption. In fact, consumer confidence in the country is at its highest in 13.5 years according to a recent poll by market research company, GfK. And whilst growth isn't immune from risks such as the challenging market conditions in the single currency zone, analysts expect that the German economy will be propped up by strong consumer demand throughout 2015 and beyond.

Maintaining good form

Although its advantages have been widely debated, the German economy is also benefiting from the European Central Bank's (ECB) €1.1trn quantitative-easing (QE) programme. In April this year – as QE pushed yields on German bonds with a maturity of as long as nine years below zero – the DAX Index closed at a record high.

And investors are in a buying mood for good reason. In 2015, the country achieved its highest ever score from The Heritage Foundation Index of Economic Freedom, making its economy the 16th freest globally. Improvements cited by a corresponding report include marked advances in labour freedom and in policy areas related to market openness. These developments to economic freedom – openness to global trade, freedom from corruption and reliable business environments, for instance – are beneficial to overseas investors. "There is an open and welcoming foreign investment regime in Germany," says Stephen Price, Country Head of Commercial Banking for HSBC Germany.

In addition, "Germany is in the centre and the heart of Europe, from there you can reach both the eastern and western parts of Europe quite easily," explains Gabriele Schnell, Head of Payments and Cash Management for HSBC Germany. Its optimal location has traditionally led to Germany being leveraged as a hub for investments and trade logistics. Moreover, its infrastructure, according to Schnell, is "well-developed" and received recognition in IMB World Competitiveness Yearbook 2015, ranking 9th globally.

International presence

As such, it is unsurprising then that Germany is a major export country. In fact, as Carola von Schmettow, CEO of HSBC Germany, explains, "Germany is one of the

in association with HSBC

Top tips from Testo AG

Case study

Matthias Wehrle
Head of Accounting

Testo AG, headquartered in Lenzkirch in Germany's Black Forest, is a world market leader in the field of portable and stationary measurement technology. Testo AG has a presence on every continent with 30 subsidiaries and more than 80 trade partners.

Matthias Wehrle, the company's Head of Accounting gives his top tips for doing business in Germany – and some considerations for German-based corporates looking to Asia for expansion:

- As in most countries, you have different local regulations and laws. So, before you set up a business overseas, it is important to clarify your company's needs and be aware of new business procedures. That said, setting up a successful enterprise in Germany is relatively straightforward.
- It is important, especially when considering Asian markets, to find a good banking partner who can inform you about local nuances and keep you updated on regulatory changes. The HSBC team in China keeps Testo AG up-to-date and is well-placed to help with the company's liquidity needs at both a domestic and international level.
- For German corporates doing business in China, it is also essential to keep up-to-date with China's State Administration of Foreign Exchange (SAFE). It is the most important regulatory department in China for corporates and is responsible for the management and monitoring of cross-border trade and FX. Corporates will need to ask about every regulation in every Chinese province separately, however.
- To keep up to date in Germany, Asian corporates can ask the International German Chamber of Commerce for the latest information, as well as relying on their chosen bank partner for regular updates.

top export nations in the world." However, she continues, "Germany is highly dependent on the global trade environment. The economic challenges in the Eurozone are weighing strongly on exports." How then has the country kept its position as a leading exporter?

Deutsche Bundesbank, Germany's central bank, reported in December 2014 that, as the economy remains in remarkably good shape, German corporates are able to seize opportunities in foreign markets. The country's Mittelstand (mid-market segment) has looked towards faster growing markets, where average growth rates far exceed those of the Eurozone, explains von Schmettow. For instance, China is now one of the country's biggest trading partners and, "in order to ensure companies get the best possible payment conditions, many corporates have started to look at using the renminbi (RMB) as an invoicing currency to source goods. According to HSBC's latest RMB internationalisation survey, they are also willing to sell goods and invoice in RMB to make their goods more attractive," says Schnell.

HSBC was the first bank to offer two-way cross-border sweeping between China and Germany. According to a 2015 survey that HSBC conducted, the awareness and discussion of RMB usage had reached the CFO and board levels internationally. Given that the study found 60% of German companies expected their cross-border trade with China to increase in the next 12 months, it is unsurprising that German senior management teams were recognised as those discussing the RMB as a business enabler.

Asian attraction

But the country's relationship with Asia hasn't only been one-way. Germany also offers an attractive prospect for Asian corporates looking to expand into Europe. Deloitte reported in 2014 that "Germany attracts Chinese investors in specialised deals that are more technology-driven, to look for technology upgrades, mostly in the sector of machinery building and automotive car parts," for instance. Within the first five months of 2014, both the number of deals and value of Chinese M&A transactions in Germany showed an increase compared to the previous year. In fact, 2014 marked the fifth consecutive year where the number of M&A transactions by Chinese firms into Germany increased. And due to increasing volumes of mutual trade between the two countries, in March 2014,

the German central bank and the People's Bank of China agreed to co-operate in the clearing and settling of the Chinese currency, RMB, in Frankfurt.

According to Matthias Wehrle, Head of Accounting, for Testo AG the world market leader for measuring solutions and instruments, with its headquarters in Germany and subsidiaries in Asia, "when exploring setting up business in Europe, I think, you first look at Germany."

"There is a strong interest in the technology knowledge and the research capabilities in Germany as well as the infrastructure and generally reliable, transparent processes," adds HSBC's Schnell. All of which, she notes, is appealing to an increasing number of Asian corporates. Moreover, SEPA has been a major step in the direction of standardisation as "you only need one account in, for instance, Germany in order to settle your transactions across all of the euro countries." This is yet another attraction for Asian corporates thinking about European expansion.

And, by choosing Germany, overseas corporates are offered "a highly developed legal and political framework that provides a good deal of security," says Price. The country is arguably a representation of stability in an otherwise volatile environment. Not only does it offer a resilient economy that represents relatively low risk with low inflation and low unemployment, from a workforce point of view, Price adds that Germany's working population is highly trained, well-educated and committed to IT developments.

Legal considerations

For any business entity wanting to conduct operations in the country, decisions will need to be made under which form they want to do business. Generally, foreign investors will function through a subsidiary or branch – that is, an overseas company can set up a German branch as a place of business without necessarily forming a subsidiary. The registration of a foreign company branch must be made electronically with the Commercial Register at the given location of that branch; application content will vary depending on the legal form of the overseas company. But, in general, registration must include: approvals by the Germany state (if required), the company's foreign legal registration, the legal form of the company, persons with power of agency and applicable laws.

> In order to facilitate both inward and outward business for multinational corporates, HSBC operates for instance a German desk in China and a China desk in Germany where the relevant relationship bankers can provide corporates with "direct on-the-ground support in key markets."
>
> Stephen Price, Head of Commercial Banking Germany (Member of the Management Board), HSBC Germany

Should a foreign investor wish to set up a separate subsidiary, their organisation would complete a Private Limited Liability Company (GmbHs – 'Gesellschaften mit beschränkter Haftung') form, have the respective Articles of Association signed by shareholders, file these documents with the Commercial Register and make this available for public inspection. Since the shareholders of a GmbH can control and instruct the management directly (which the shareholders of a Public Limited Liability Company – AG 'Aktiengesellschaft' cannot), foreign investors generally prefer to establish a subsidiary in the form of a GmbH.

Banking sector

Although there has been significant consolidation in Germany's banking sector over the past decade, there are still a high number of banks operating in the country, including 168 domestic commercial banks, 36 foreign-owned banks and 109 foreign bank branches. As expected, these include most of the large international cash management banks, which offer full services. "It is a very competitive market and to that extent banks have to be very innovative in the payments and cash management space," says Schnell.

Moreover, funding conditions are favourable, despite German banks having to contend with a number of measures the ECB has out in place. Compelled by the recent phase of stress testing, banks have had to readjust their balance sheets to meet capital ratios set by regulations. All 24 German banks that took part completed the tests successfully.

Elsewhere, the new bank tax introduced in January 2011 by the German government expects banks to inject up to €1.2bn every year into a reserve fund to finance any future bank bailouts. This all points to a stable banking sector that is doing all it can to safeguard against external shocks.

Bank supervision in Germany is carried out by the German Financial Supervisory Authority – known as BaFin – and the central bank, Deutsche Bundesbank, in accordance with the Banking Act. The Bundesbank is a member of the European System of Central Banks (ESCB).

Payment instruments

- **Cheques** are declining in use in Germany due to the preference for electronic payments for both high-value and low-value transactions.
- **Payment cards.** All payment cards issued in Germany are SEPA-compliant.

- **Cash** is still popular in Germany. In fact, the country remains one of the most cash-intensive advanced economies globally.
- **Direct debits** are available and typically used for low-value recurring payments. In February 2014, SEPA direct debits were introduced to replace Germany's pre-authorised direct debit scheme until February 2016.
- **Credit transfers.** Although credit transfers can be paper-based or automated, all paper-based ones are truncated into electronic items. They are used for both high-value corporate and low-value retail payment transactions.
- **Electronic banking** is commonplace – all of the country's leading banks offer e-banking solutions.

Asian support

Against this backdrop, how can Asian corporates successfully establish operations in the country? Choosing a banking partner with global reach and local knowledge is a good starting point, says Price. For instance, HSBC offers country desks and dedicated members from their International Subsidiary Banking (ISB) team. In order to facilitate both inward and outward business for multinational corporates, HSBC operates for instance a German desk in China and a China desk in Germany where the relevant relationship bankers can provide corporates with "direct on-the-ground support in key markets," explains Price. Additionally, from an Asian point of view, HSBC also sits experienced bankers at both ends of the trade and investment flows.

"Entering a new geography is often a challenging and, at times, a worrying occupation for corporates," says Price. But, considering the international footprint of HSBC, the bank is well positioned to support companies in overcoming cultural issues and issues of communication and connectivity as well as a bank's bread and butter role of support with issues of funding and FX. "The ISB team ensures the required level of understanding of how to operate in Germany is consistently provided, minimising the chance of unforeseen surprises for the corporate," continues Price.

This particular approach to relationship management offers Asian corporates ease of access into a country whose advantages – including reliability, transparency and a competitive edge – place it on a strong footing and, as von Schmettow concludes, "make Germany the ideal starting point for multinationals wanting to do business in Europe."

Useful websites

Supervisory authority: www.bafin.de
Central bank: www.bundesbank.de
Stock exchange: www.deutsche-boerse.com
Ministry of Finance: www.bundesfinanzministerium.de
Association of German banks: www.germanbanks.org
Association of Corporate Treasurers: www.vdtev.de
Association of Chief Financial Officers: www.gefiu.de
Germany Trade and Invest: www.gtai.com
Chambers of Industry and Commerce: www.dihk.de
Central credit committee: www.zentraler-kreditausschuss.de

Gräfin Carola von Schmettow
CEO of HSBC Germany and Chair of the Management Board

Stephen Price
Head of Commercial Banking Germany (Member of the Management Board), HSBC Germany

Gabriele A. Schnell
Head of Payments and Cash Management HSBC Germany

HSBC

Show me the money

In recent years, survey after survey has shown 'improvements to cash visibility' to be near the top of the corporate treasurer's wish list. Achieving that desired level of visibility, however, seems always just out of reach. Why are companies still finding it tricky to get proper visibility over their cash? Is technology always the answer or should treasurers be thinking about more fundamental changes? In this article, industry experts give us their take on this perennially thorny issue.

Treasurers in the Asia Pacific region have one overriding strategic priority at the moment. Put simply, it is to get a better view of their day-to-day cash balances across the business.

In the second edition of Bank of America's (BofA Merrill) Asia Pacific Treasury Barometer Survey, published in late May, improving visibility of balances and cash forecasting was the most cited (21%) priority of treasurers in the region for the year ahead. This may not be so surprising to many in the industry. Cash visibility, if not number one, usually comes near the top whenever treasurers are asked about what they are focusing most on improving. And rightly so. Failure to achieve sufficient visibility over the company's cash carries significant risk. In fact, without clear visibility, companies cannot adequately control group cash. In turn, this means they cannot use that cash at optimum efficiency, or maximise investment opportunities for it. Reducing borrowing costs and improving foreign exchange (FX) risk management will also be extremely challenging without full visibility and control.

Why the increased focus of late though? Perhaps, ponders Glen Giffen, Director of Sales at Visual Risk, it has something to do with recent corporate balance sheet trends. As we are reminded by industry study after study, corporate balance sheets have ballooned across the globe since the 2008 global financial crisis, especially in the Asia Pacific region. Recent figures reveal that non-financial companies in APAC are sitting on more idle cash – an average of $4.2bn each – than firms from any other region listed in the S&P Global 1200. In South Korea, companies have around $270bn idle on the balance sheet, while in China, the largest 500 companies have

Source: Bank of America Merrill Lynch Treasury Management Barometer Survey 2015

$405bn. Japanese companies are the most cash rich of all, meanwhile, with a stockpile close to $3trn.

"There is a lot of cash on corporate balance sheets," says Giffen. "Treasurers are naturally focusing more of their efforts on managing that excess cash than they have had in the past. And if managing surplus liquidity is a much bigger feature of your day-to-day job, then cash visibility is obviously going to come into much greater focus than perhaps it has in the past. Moreover, credit and counterparty concentration risk becomes a huge concern so understanding and managing this effectively becomes a big part of the cash visibility story. For example, what is the impact on cash and investment holdings if the credit quality of a counterparty deteriorates?"

Cutting through the fog

What corporate treasurers want, at the base level, is to be able to get a snapshot of all the cash across the organisation, together with the details of any transactions that forecast to be made throughout the day; and they want to be able to obtain all of this information in an efficient manner. That way, when they arrive at their desks in the morning they are able to anticipate whether the company will have, come the end of the day, a surplus of cash that will require investing or a shortfall that will necessitate some form of borrowing.

Yet the fact that improving cash visibility is still listed by so many treasurers as a top priority would suggest that, despite the apparent simplicity of what they want, initiatives designed to provide them with it have so far only seen mixed success. Why does the optimal level of visibility seem, for so many, still out of reach?

Industry commentators each have their own take on why this might be. "The treasurers that we talk to are typically under-resourced and frequently wrestle with the challenge of accessing data in a timeframe that allows them to make informed decisions," says Alastair McGill, Managing Director, Global Business at Cashfac. The issue stems from the fact that despite the increasing sophistication one sees in the sorts of technologies implemented by multinationals at the top end, for the vast majority of companies these activities remain heavily reliant on manual input. In Asia, this can be especially troublesome given the geographic regional spread, the multiple currencies, multiple time zones and the multiple banking relationships companies typically maintain.

"For the treasury function, identifying real-time balances of cash across these dispersed operations and across different bank relationships remains a considerable challenge," says McGill. Indeed, the Cashfac Operational Cash Index, which recently surveyed corporate treasurers in Asia Pacific reveals that almost two-thirds of corporates in the region do not have access to a real time view of their transactions and cash. "This is a worrying statistic," he adds.

Thomas Knudsen, Senior Manager in the Treasury team at PwC believes that, fundamentally, the issue comes down to the structure of corporate banking relationships. "Often it depends on which banks a company uses," he says. "In some developing markets you find that your core relationships bank might not be able to support you for the local services that you need. So while you can get reasonably good visibility with an international bank, you might still need to use other, smaller and less capable banks, some of which might not be connected to a banking network like SWIFT."

In fact, some banks in some countries won't even provide you with an electronic banking platform of any sort, adds David Stebbings, Head of Treasury Advisory at PwC. "That means, in some instances, you have to be more manual," he explains. "You have tiers of standards around how you do these things depending on what country you are in. That is why there is no one-size-fits-all solution. There are different ways of addressing the issue and what you do will depend on your cost benefit analysis and the banking infrastructure in that part of the world."

What is clear though is that centralised treasuries with fewer bank accounts have a distinct advantage over those with more

decentralised structures when it comes to the issue of cash visibility. Getting that visibility over banking infrastructures – and in efficient manner – is never easy for those that must wrestle with a multitude of security tokens, logging into multiple banking interfaces and extracting the required data manually. In fact, as McGill explains, even having done this many times, treasurers will still not have the full picture "as the bank account data showing balances and historic transactions makes no allowance for the imminent expected receipts and payments, or those that should have been credited or debited but for whatever reason failed to materialise."

The results of the Cashfac Operational Cash Index supported this notion showing that among those corporates with a real-time view, on average less than 60 per cent of their total cash and ongoing transactions was visible in real time. That leaves the remaining balance being consolidated manually in order to achieve a complete view of their positions. As such, it's rare for most firms to have complete real-time cash visibility at an operational level that allows treasurers to effectively maximise the treasury tools at their disposal; sweeping and pooling strategies, for example, could all be enhanced if the real-time view of cash was better understood.

One way in which firms can gain better visibility of operational cash is to exploit Client Managed Accounts where the bank account infrastructure remains bank-connected but resides under the corporate's control; either deployed as an in-house system or as a bank-provided service. Client Managed Accounts are simply an evolution of the virtual account model, where corporates have the scope to determine their account structures; mapping them to their business requirements and establishing the rules that determine their behaviour. The way in which money is routed when it hits the main account can be predetermined and automated. Expectations of payments and receipts can be pre-populated against individual accounts so when money movements occur they are automatically reconciled against the expectations and an accurate real-time view maintained.

Where companies are multi-banked the same principles can apply, connecting multiple banks to a single set of Client Managed Accounts is less of a challenge than most assume. Either via direct connectivity channels or through industry initiatives led by organisations like SWIFT, there are plenty of options that can be deployed to make life simpler and accelerate the aggregation of balance and transaction data.

Forecasting inaccuracies

Visual Risk's Giffen believes there may be another factor preventing treasurers from attaining that desired level of visibility: the accuracy of cash flow forecasting. Corporate cash balances, it probably goes without saying, are never static. Throughout the day, money will flow in and out of a business altering each time the company's cash positon. For treasurers then, it is simply not enough to have visibility over cash at certain intervals. They need to be able to see what is coming down the line.

This is where analytical software comes into play. Solutions like these can help the treasurer to identify the key risks that might lead an organisation to deviate from a forecast. This allows a stress test to be performed where the treasurer can analyse how a particular market risk – currency or energy price volatility, for example – might impact cash flow projections.

The degree of sensitivity to such market risks will vary between companies, for reasons that are not difficult to understand. A manufacturing company that is exporting 100% of the goods it makes will, naturally, have a much higher sensitivity to movements in the currency markets than another manufacturer that only exports, say, 5% of its goods. Similarly, a soft drinks company is going to find its cash flows to be highly sensitive to the price of sugar, especially if it is unable to alter the price of its products. "What if there is a product issue that means not all of the investments the treasurer holds can be liquidated at current market rates?" says Giffen. "What if a particular currency or central bank interest rate moves in an adverse way? Visual Risk has always been very strong in sensitivity analysis."

> "I think a move to systems-based solutions is really the first step. Because at this point in time a lot of the cash processes we see out there are incredibly inefficient. It can take an inordinate amount of time just to arrive at a simple end of day cash position."
>
> Glen Giffen, Director of Sales, Visual Risk

Technology quite evidently has a significant role to play for treasuries determined to optimise the visibility they have over their cash. The greatest advantage of systems-based solutions offer is the time saved, adds Giffen: "I think a move to systems-based solutions is really the first step. Because at this point in time a lot of the cash processes we see out there are incredibly inefficient. It can take an inordinate amount of time just to arrive at a simple end of day cash position."

In Asia, where a lot of companies are still some way behind their European or US counterparts in terms of technological sophistication, investing in such solutions could bring some significant efficiency gains in performance of cash management. Are companies now finally beginning to hear that message? "We are starting to see it but it is a long process," says Giffen. "Obviously in jurisdictions with a relatively high cost of labour like Australia, Singapore then technology offers a clear cost benefit. However, if it is Indonesia or Vietnam, for example, where the cost of labour is lower, you might not want to make that investment."

Still top priority

As we have seen, the issue of cash visibility is inextricably linked to two perennial pursuits for the treasurer, centralisation and the quest for process efficiencies through the harnessing of technology. Experts seem to agree, however, that while structural or organisational solutions are certainly helpful, there is nothing quite like the power of technology when it comes to improving cash visibility.

And now, with an ever-growing range of sophisticated and – thanks to the cloud, increasingly affordable – technologies on the market, those treasurers who say improving cash visibility is their top priority for the year ahead should have the means at their disposal to help realise that objective. ■

Oceania: a sea of potential

Made up of thousands of islands, Oceania is a region many would consider to be a veritable paradise. But, as many countries within Oceania have never been connected to a continent by land, economic development faces some tough challenges – as do businesses operating there.

With the exception of Australia and New Zealand, Oceania is ranked by the UN as a developing region. Of course, discussion of Oceania would not be complete without mention of the region's only developed countries, but this article endeavours to focus on the local highlights and Australia and New Zealand's business connections with the rest of the region.

The collection of island countries has experienced diverse economic development paths. For many of these developing nations, agriculture, fishing and tourism are key industries. Eighty percent of Vanuatu's population and 70% of Fiji's works in agriculture, for instance, and canned tuna accounts for 93% of exports in American Samoa. Other major exports from the region include coconut oil, palm oil, coco and sugar, but natural resources of lead, zinc, nickel and gold are also mined on some islands.

There have been some rather interesting exports over the years too. Tuvalu, for instance, hit the international news in 1998 when the country sold its internet suffix (.tv) to a Californian company for an advanced payment of $50m (£33m). As more than half the country's GDP at the time and with the promise of more revenue to follow, the ten-square-mile island made quite a

Countries comprising Oceania

Australia, New Zealand and Norfolk Island

Melanesia – Fiji, New Caledonia, Papua New Guinea (PNG), Solomon Islands, Vanuatu

Micronesia – Guam, Kiribati, Marshall Islands, Micronesia (Federated States of), Nauru, Northern Mariana Islands, Palau

Polynesia – American Samoa, Cook Islands, French Polynesia, Niue, Pitcairn, Samoa, Tokelau, Tonga, Tuvalu, Wallis and Futuna Islands

splash at the start of the internet boom. Such opportunities are not regular for these isolated islands, however.

Indeed, many countries lean on the region's front-runners Australia and New Zealand – among other donor nations and organisations – for foreign aid. Australia and New Zealand often have arrangements together (in the Cook Islands, Niue and Tokelau, for example) and are typically the largest aid donors. But the political landscape is changing slightly, notes Deva De Silva, Senior Country Officer for IFC in East Asia and the Pacific. "China is also now an important donor and development partner for some of these countries."

Regional patchwork

The economic landscape of Oceania exhibits not only variation between the region's developing and developed countries but variation between the island nations themselves. Nauru, for instance, has been forecast impressive growth rates of 10% and 8% for 2014 and 2015 respectively. Although the smallest island country in the world (with a population of approximately 10,086), it is now on the global radar because of infrastructure developments. The Regional Processing Centre (RPC), originally reopened in 2012 for asylum seekers looking for refugee status in Australia currently employs around 200 Nauruans and is set for expansion. Thus, a boost to consumption, expenditure and growth is predicted.

With one of the largest populations in Oceania, PNG is also one of the fastest growing economies in the world with predicted growth rates of 6% for 2014 and 21% for 2015. The bright future for the country's economy is driven by liquefied natural gas (LNG) exports to Asia. A $19bn LNG plant in PNG's highlands began production in April last year and is expected to produce 6.9m tons of LNG per feed. With two more gas projects being developed, PNG could become a crucial energy producer for Asia.

> "It's a tough region as the countries are small and all far from global markets. Isolation makes the economies quite weak and poor infrastructure often gets highlighted as the key limitation for private sector growth."
>
> Deva De Silva, Senior Country Officer, IFC in East Asia and the Pacific

Across the rest of the region, other instances of growth include tourism for the Cook Islands where economic growth has been linked to a 11.2% increase in visitor arrivals between 2011 and 2013. Similarly, Fiji – the only country amongst the pacific island nations not included in the World Bank's International Development Association (IDA) aiming to help the world's poorest countries – beat expected number of arrivals in 2012 by over double, with around 600,000 tourists visiting. In fact, Fiji acts as a regional hub and is a focal point for business activity in the Pacific region. Fiji's international airline, Fiji Airways, operates 400 flights a week throughout the Pacific. The country also offers international shipping services and three international submarine cables land in Fiji.

However, evident of the disparity between island countries, other countries struggle to optimise their potential. Tonga, for instance, is a relatively poor nation with a narrow industry base focused around farming of a limited range of crops and Kiribati experiences problems transporting goods due to its 33 islands being spread over a vast distance.

Developing economies: the challenges

As such, growth for the majority of these developing Pacific countries is no easy task. De Silva explains that "it's a tough region as the countries are small and all far from global markets. Isolation makes the economies quite weak and poor infrastructure often gets highlighted as the key limitation for private sector growth." Economic stability is also vulnerable to external shocks – largely due to the nations' limited resources.

> Opportunities for growth are set to expand as more companies and investors see the region's potential.

One example of this vulnerability is the natural disaster which recently struck Vanuatu. "There was a category five cyclone there in March this year – which is both a tragedy and a logistic challenge for businesses," explains Michael Murphy, CEO for mobile communications provider, Digicel Pacific. "We managed to get our mobile network back up within five days but I think a lot of people forget that in this region we have very different terrains. Building locations and connectivity into these markets is very challenging and will remain so until the infrastructure starts to improve over a longer period."

Moreover, ANZ notes several challenges associated with doing business in Oceania's developing countries: the limited avaliability for overseas businesses to own land in Samoa; the 820 indigenous languages spoken across PNG and the corrupton that can exist within parts of the public service, as well as in PNG's business environment; and stringent controls over cross-border payments from Fiji are but a few examples.

What needs to done?

Nevertheless, opportunities for growth are set to expand as more companies and investors see the region's potential. As De Silva explains: "Although they are not always seen as strategic countries, there are donors from across the globe investing in Pacific island countries. It is amazing that some of these countries – even the smallest with only 30-50,000 people – will have up to 40 active donor partners."

In addition, privatisation of public utilities by many of the governments in Oceania is opening up opportunities for forward thinking companies. Digicel Pacific, for example, has taken on the challenge of establishing operations in the region (described by Murphy as "up mountains and down rivers"), and, according to De Silva, "has absolutely changed the landscape in terms of telephone usage, the efficiencies of telephone usage, the cost of usage and its reach." The telecoms company now boasts expansion over six pacific countries (Vanuatu, Samoa, PNG, Tonga, Fiji and Nauru), including 4G in two markets.

Before Digicel, each of these six countries had government-owned single monopoly telephone operators which were

inefficient, costly and limited to urban areas. Certainly, the dialogue around private sector investment in such areas is increasing and De Silva predicts in the next few years that "we will see the Pacific governments pursuing private sector investment as a priority for economic sustainability and growth."

A helping hand

South Pacific Business Development (SPBD) is one example of an organisation assisting companies in the region with the identification of opportunity and provision of financial support at the other end of the scale of opportunity. Inspired by the pioneering organisation in microfinance, Grameen Bank, SPBD targets the base of the economic pyramid in four pacific island countries: Samoa, Tonga, Fiji and the Solomon Islands. "The top 20% of the population in the South Pacific have most of the wealth, education and business connections meaning a lot of the existing financial services and development is channelled through them. But if you are going to achieve improvements to the quality of life for the masses, then you need to do it through a vehicle like us," explains Greg Casagrande, Founder and President of SPBD.

"Due to the small-sized nature of Oceania's developing economies, there are very few formal waged employment opportunities. SPBD enables individuals to be self-employed, invest in capital equipment and increase their productivity to enhance their income." By providing training on loan applications, granting those loans without the requirement of collateral and maintaining ongoing business guidance, SPBD "empowers people at the grass roots level through getting them established privately." That, according to Casagrande, "is what's sustainable and scale-able." Indeed, such opportunities help leverage a business environment where the private sector can flourish.

Doing business in Oceania

Problematic for both corporates and entrepreneurs alike, however, is the limited access to finance in Oceania. With the exception of Fiji, in the majority of countries, less than 20% of the population have access to finance. "The banking sector faces the same challenges that a corporate would because of limited access to actual infrastructure," explains Murphy. Moreover, "traditional banks that demand collateral or formal wages end up excluding 80% of the population from any sort of financing," says Casagrande.

Reliance on cash is particularly problematic for entrepreneurs as they have to travel long distances to deposit money at distant bank branches. But a new trend has been emerging where banking services can be available at their fingertips using technology. Several initiatives have launched where payments and transfers can be completed using mobile phones – so although consumers and businesses may be geographically remote, they can be connected to their banking provider. Money can then be withdrawn from electronic funds transfer machines or at local shops operating as agents for the banks. Currently, BSP, ANZ and Westpac are all implementing electronic and/or mobile banking platforms.

For larger corporates, research must be undertaken into which banks can support their local needs. ANZ, for example, has a regional operations hub in Fiji's capital city, Suva, and operates branches with corporate services in many of the island countries.

Looking ahead

The reliance on external support and investment, as discussed earlier in this article, is recognition of the tough conditions that economic and social development face in the small island countries of Oceania going forward. Although the majority of Oceania's nations are likely to remain aid-dependent for some time, the nature of dependency has the potential to reach a point at which financial assistance could support budget implementation by governments, rather than dominating it.

The reason – change is beginning to occur: "A while back, the governments in the region seemed happy enough to receive aid and manage bilateral relations. In the last five years, however, we have seen a marked improvement in the way governments are engaging with the importance of the private sector," explains IFC's De Silva. Pacific governments seek (increasingly so) to build a greater capability to respond to operational and business challenges, attracting investor attention along the way. ■

Top tips for Oceania's future

In order to increase the region's appeal, Casagrande has the following recommendations (or rather, wish list):

- **Maintaining security.** Ensuring there is peace on the islands is extremely important to their future economic well-being.
- **Increasing skill levels.** Trying to further enhance educational opportunities for everybody would increase the notably low skill levels in the Pacific Islands.
- **Further disseminate laws.** Promoting transparency and the effective function of the central banks would improve the attractiveness of the business environment.
- **Investment-friendly tax systems.** Amongst the pacific island countries, there are some high withholding taxes that can go up to 35%. Building a more attractive tax regime would incentivise investment.
- **Changing property rights.** Currently, it is difficult to get clean title as a lot of land is communally held. This is a concept many overseas investors find challenging.
- **Improving air connections.** There is a surprising lack of direct flight connections between the islands. In fact, Tokelau is only accessible by boat twice a month from Samoa and travellers face a 26 hour journey – even in good weather!

Closing the gap: treasury models

Centralisation, automation and cost reduction remain the major trends when it comes to structuring the treasury function. With many companies intensifying efforts towards all of the above, it is pertinent to reacquaint ourselves with the basics of treasury models, asking the question 'does full centralisation really suit every business'?

It is no secret that since the financial crisis, treasurers increasingly want to know where the company's cash is and how quickly they can access it. Treasury Today's Asia Pacific Corporate Treasury Benchmarking Study 2014 found that cash management and cash pooling structures are within the top three priorities for corporate treasurers. Moreover, addressing cash flow forecasting and improving visibility over the company's cash comprised two of the top technology issues – the study concluded that on these points, there is still room to improve.

But what impact do these concerns have on treasury models? Certainly, emphasis on visibility and control is considered one of the drivers behind intensifying interest in centralisation. Moreover, technological advances have made it easier and cheaper to centralise. Technology is no longer the preserve of large corporates.

Operating a centralised structure is not always straightforward however and, as every business has individual requirements, it is important to determine (and periodically re-evaluate) the degree to which centralisation is beneficial and practical from a specific company's perspective.

Levels of centralisation

Broadly speaking, there are three levels of treasury structure: decentralised, partially centralised and fully centralised. Although full centralisation may be the ultimate goal for most multinational corporations, many companies end up with a partial or decentralised structure simply because it is too impractical for them to operate in any other way. It is to these two that we first turn:

- **Decentralised.** Treasury policy-making, decisions and activities are conducted by individual subsidiaries. Typically, only a small team is retained at group level to provide advice and support. Subsidiaries may have their own local banking arrangements, will organise their own funding and handle cash management (including short-term borrowing and investments) locally. Payments to and from the parent company will still occur.

  Decentralised structures work well when the subsidiaries are independent and autonomous units with limited complimentary needs. Local treasury units' enhanced local operational knowledge and risk awareness is advantageous – especially when the business needs to adapt to unexpected events. However, they face issues with limited automation (no central processes), and potentially lack the leverage or ability to offset surplus cash positions against borrowings elsewhere, among other potential problems of multiplying, rather than minimising, efforts.

- **Partially centralised.** Arguably a 'best of both worlds' approach, a partially centralised model usually involves individual subsidiaries following the treasury policy as outlined by group treasury – often they will also receive advice or instruction. Individual subsidiaries, however, will be responsible for executing deals themselves via their local banking partners. Back office operations may be undertaken at a local level or they may be centralised. Partial centralisation delivers more control while enabling subsidiaries to maintain a degree of autonomy within the front office function. It can also help to increase uniformity in treasury policies and procedures across the group and allows key decisions to be made at a global level with a comprehensive view of cash flow – whilst also retaining local expertise.

  A common approach to partial centralisation is the regional model. With treasurers rethinking their approach to banking and funding since the financial crisis, the one-bank approach is no longer seen as a viable option. So, with treasurers giving more consideration to regional banking relationships, a regional treasury model is also being mooted as an equally prudent option.

- **Fully centralised.** With a fully centralised structure, a global treasury centre or regional centres (on behalf of subsidiaries across a specific region or across the group) will undertake policy-making decisions and most, if not all, banking and financial activities. These centres may offer 24-hour services to ensure round-the-clock coverage for all subsidiaries. The organisation of centralised treasury is increasingly built around two objectives – debt capital and risk management – with the aim to source and secure a strong cash flow by placing key decisions at the centre.

  Centralisation ensures group treasury has standardised operations, greater control across the company with streamlined bank accounts and improved transparency of cash flow. The natural hedge created by matching of financial positions can also result in better margins.

Moreover, the concentration of knowledge and experience typically leads to improved results with fewer people and a reduced risk of error.

Costs are also likely to reduce – if basic processes of payments and collections are centralised, the cost of those processes decreases: it is a simple economy of scale. Centralisation can, however, lead to a lack of local banking expertise and a loss of responsibility may lead to either (or both) a lack of interest and resistance at the local level.

Centralisation developments

Technological advances have been making it easier to centralise treasury operations, lifting both practical and financial barriers. Technology has come to be seen as a key enabler in the implementation of treasury centres and integrating company platforms with those provided by the company's banking partners, therefore, a key success factor. Furthermore, some regulatory initiatives favour the adoption of centralised treasury structures. The persistence of general economic and geopolitical uncertainty means more corporates with global operations are looking at streamlining their treasury management into full centralisation.

The advent of cloud computing is also opening up new possibilities for treasury centre locations. Access to data sources and solutions in the cloud means that it increasingly doesn't matter where the treasury centre is situated. This development means that labour costs have emerged as one of the primary factors in determining location.

Of course, labour costs shouldn't be treated as the sole arbiter of location. Technology and communications infrastructure, time zone considerations, political stability and the local regulatory environment, should all be considered as part of the selection process.

Issues for consideration

However, it certainly isn't a case of one size fits all. Some responsibilities of the treasury department can benefit more obviously from centralisation – increased visibility of information, for example. Centralised information enables a business to 'think globally and act locally' ensuring sound management and the ability to prevent problems from a comprehensive group view – without having to compromise people on the ground managing both local risks and local opportunities.

Whilst other areas of focus consistently offer savings when centralised (for example payment processes), in some instances companies must question whether the process involved would be handled better locally. Certain commodities hedging or transactions requiring reporting to central banks provide two examples.

When deciding on a treasury model to operate, the following points outline some issues to consider:

- **Cost and cost saving.** The financial implications of initial expenditure and ongoing costs must be weighed against the benefits and potential savings for each model.
- **Group-wide support.** The chosen model must gain full support at management and board level; the understanding from employees at both group and subsidiary levels is also required.
- **Legal, regulatory and tax implications.** The significance of changing structures and establishing centres in different regional locations (with potentially different tax, regulatory and legal requirements) should be investigated.
- **External relationships.** Relationships with any banks and vendors impacted by any changes should be managed well – this involves negotiating advantageous terms and handling the declaration of any loss of business appropriately.
- **Technology.** What steps are required to progress to the desired system infrastructure? Of consideration here is whether legacy systems are able to migrate or integrate – this could have an impact on costs.
- **Operational aspects.** Any transition procedures, project management and staffing issues should be addressed with minimal adverse impact on daily treasury activities.

The treasury centre

Where a centralised structure is chosen, a treasury centre will be encountered. These are centralised treasury management functions, legally structured as a separate group entity or branch. Treasury centres are normally located in a tax-efficient environment, reducing the bill on transactions and profits associated with the entity. Also of importance is the location's possession of highly developed banking infrastructure and a wealth of financial services expertise. Moreover, technology and communications infrastructure, time zones, political stability and local regulatory environments should all be considered when choosing where to locate a treasury centre.

A treasury centre will provide financial management and transactions services for the other group entities including, but not limited to:

- Internal and external payment services.
- Cash pooling.
- Asset management services.
- Financial markets research.
- Monitoring and financing capital requirements of group companies.
- Risk management analysis and monitoring.

It is important to be aware that the capabilities and activities of a treasury centre are defined by each individual case. In some instances, responsibilities may be best managed locally as not all countries where group companies are located will necessarily permit the concentration of all treasury centre activities.

Nevertheless, operating with a centralised treasury can lead to numerous improvements, including: governance improvements (co-ordinated and central database, group-wide reporting, standardised procedures), cost reductions (higher volumes and fewer transactions, reduced financing requirements) and efficient tax management (optimising global tax position).

The organisational structure of a treasury centre

Depending on the group's management philosophy, the treasury centre has a choice of two models to adopt:

Finding the right spot: treasury centres in Asia

As more and more corporates centralise their operations and look to establish a treasury centre in Asia, the big question is which location is best? For many corporates the choice is between the region's two key finance centres: Singapore and Hong Kong.

Singapore is currently the dominant treasury centre location in the region. The country offers a business-friendly environment, deep and well-educated talent pool, and best-in-class infrastructure which has seen it become the regional hub for many multinationals. In addition to this Singapore has 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.

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. Qualifying corporates receive a concessionary tax rate of 10% on all fee income received from treasury activities and an exemption from withholding tax on interest payments.

Hong Kong, the regions second key treasury centre location, is popular with companies that have a significant presence in China. On the whole it offers a similar proposition to Singapore with a business-friendly environment, legal system based on English common law, liberal and well-developed regulatory framework, deep, well-educated, international talent pool and excellent infrastructure. Corporates in Hong Kong also have access to a wide range of banking services and a well-developed RMB market.

One area where Hong Kong has lagged behind Singapore is in its tax incentive programme. But recent developments have looked to change this and address the tax imbalance which put some corporates off operating in the territory. The Hong Kong Monetary Authority have proposed that tax payments on intercompany loans will no longer be larger than profit earned – thus bringing the territory's incentive package in line with Singapore.

Although Singapore and Hong Kong are currently dominant, there are other locations in the region such as Shanghai, Malaysia and Thailand which are all also looking to get a slice of the treasury centre pie. Currently, Shanghai is offering the strongest proposition and its attractiveness is growing as China further liberalises and the country becomes more critical to businesses. But, it remains to be seen if these locations will attract enough corporates to challenge Hong Kong and especially Singapore as the region's dominant locations.

1. The treasury centre acts as central agent, operating all financial transactions for the group companies in their name, compensated on a cost plus basis.
2. The treasury centre acts as the group's central in-house clearing bank, either on a shared service centre basis (which means that the group entities have direct relations with the treasury centre) or in competition with third-party banks.

Both models centralise the treasury know-how of the group. In addition, the in-house bank (IHB) operates the group's financial management as its own business. Cost savings, as well as additional income earned, arise at treasury centre level.

If a treasury centre is organised according to an IHB model and is competing with other third-party banks, it will usually operate as a profit centre. The group companies' financial needs are met on a price level applicable to a third party.

The question of whether a treasury centre operates as a cost, service or profit centre has a direct impact on where the treasury centre is located. Indeed, a treasury centre acting as a profit centre has a clear advantage if operating in a low tax jurisdiction.

In-house banking structures

IHB structures are typically established by medium-sized businesses upwards. An IHB acts as the main provider of bank services to all group subsidiaries. This may be established on a global scale or on a regional basis. Instead of using local external bank partners, each subsidiary channels its cash flows through bank accounts held at the IHB. The bank then nets out the resultant debit and credit balances across the group. The IHB may also use a netting process for foreign exchange (FX), as well as for the payable and receivable amounts owed between the subsidiaries.

It can be noted too that the IHB may organise inter-subsidiary lending. When all the internal transactions have taken place, any remaining investment, financing and hedging needs are fulfilled by external banks chosen by the IHB from its preferred group of relationships. Some multinationals have restructured their inter-company loans to repatriate cash and achieve tax efficiency. In the US, for example, there are strict 'arms-length' rules on interest charges which, according to Ernst & Young (E&Y), "should reflect the interest rates on loans between unrelated parties with similar terms, including duration and credit standing of the borrower."

However, as an example of what can be achieved through such a structure and practice, Toyota Financial Services (TFS), the finance and insurance brand for Toyota in the US, built an inter-company lending facility for global affiliates and achieved a $25m saving through reduced interest expense alone.

Centralised treasuries may operate an IHB within their overall model. However, an IHB can also be used to enhance operations whilst keeping a decentralised structure. ■

Averting the next crash

As a follow up to his article in the last edition of Treasury Today Asia, our treasury insider looks at four potential ways to strengthen the current fragile banking system, and considers their likely effectiveness.

The current regulatory approach is one in which I have little faith as a means to mend or even really change the financial system. So, what are the alternatives? Well, whilst there are doubtless other possible solutions, there are four interesting alternative views (spurred on by last issue's article) that I'd like to explore here. Namely: Fintech will save the day; separate credit from money; revive Glass-Steagall and rolling sub debt.

Does Fintech hold the answer?

Clearly technology is having massive impacts on finance. From algorithmic and high speed trading to electronic and mobile payments; social investment, peer-to-peer lending and trading; private currencies; and more. Many of these technologies are impressive and appear to have the potential to disrupt banks and drive radical change. Peer-to-peer lending, for instance, shows great promise, as reflected in soaring IPOs of some firms. By cutting out the middle men (traditionally banks), they promise lower fees. By harnessing big data, they promise better credit assessment.

Three big questions remain: firstly, how will they survive the next downturn? Lenders are likely to lose their appetite when defaults mount. Secondly, how will they scale? Will these lenders be able to step in to replace conventional credit markets? And if so will they provide healthy liquidity? Finally, when they hit credit losses at scale, will they need to be bailed out like banks? If that happens, then we have just created new high tech banks with the same fragility that we face now.

These platforms currently appear to meet the criteria that both risks and rewards are private. Banks under the current moral hazard regime have private profits and social (eg tax payer) losses. If the new platforms become too big to fail, then we have not achieved sustainable finance. Similar problems face peer-to-peer trading – both retail and institutional. Traditional markets provided liquidity; this is already drying up under current regulations. Fintech platforms struggle even more without market makers. In many cases, Fintech is not really disrupting finance but simply building new channels to traditional markets. And it may not have the advantages that it boasts.

Separate credit from money?

Here, it's important to explore the distinction between banks and banking. We have seen low tech shadow banking can quickly reach levels requiring government bailout. It is likely that Fintech will not just reach – but actively target – too big to fail. What business would forego privatised profits and socialised losses? One would be a fool to refuse a free lunch! The question though is not Fintech vs banks. The question is what to do about banking (whether performed by Wall Street, Silicon Valley, or any other player) which conflates money and credit to disastrous effect – driving leverage and moral hazard? New regulations will just push the banks themselves and their various non-bank competitors to find creative ways to build leverage again, to game the system, to force the next crisis and the next round of bailouts. What some industry commentators suggest is to separate money from credit. Money would remain government issued and controlled as a medium of exchange. Credit would be restricted by revising accounting rules.

As the authors of the book 'The end of banking – money, credit and the digital revolution' say: "The total value of financial assets of a company has to be less than or equal to the value of its equity. They explain that this reading highlights that companies have to back assets that are someone else's liability with their own funds, that is, equity. Companies cannot finance credit with someone else's credit."

This would indeed solve the problem. It would also create wrenching change and radically reduce credit availability. Since we seem to be hooked on credit driven growth as a replacement for productivity driven growth, this could make the solution politically and socially unworkable.

"Clearly technology is having massive impacts on finance. From algorithmic and high speed trading to electronic and mobile payments; social investment, peer-to-peer lending and trading; private currencies; and more. Many of these technologies are impressive and appear to have the potential to disrupt banks and drive radical change."

Revive Glass-Steagall?

Separating investment banking from commercial banking has been much discussed. Partial steps in this direction have been legislated – for instance the Volker rule in the US and ring-fencing in UK. The idea is to create 'safe banks' which would have deposit insurance and separate them from investment banks which would do the dangerous stuff without government support. The difficulty is in keeping safe banks safe. Safe banks used to pour deposits funds into housing. But the term 'safe as houses' seems laughable after the last crisis, which was largely one of housing leverage.

With all the technology available to banks now, keeping the separation intact will be difficult. So, as described above, the issue is probably more with banking than with specific banks. Separating money from credit (for all businesses whether they call themselves banks or not) is probably more robust than trying to segregate different types of banks. In any case, full reinstatement of Glass-Steagall would be a wrenching change for the economy and might be politically unworkable.

Rolling sub debt?

As described in my previous article, central bankers and others have proposed that banks be forced to issue substantial amounts of ten year rolling subordinated debt as a solution to financial fragility. The need to sell a material chunk of sub debt every year would focus management's minds on their risk profile, and continuous market pricing of sub debt would provide a market view of the institution's riskiness.

Of course, buyers of such rolling sub debt would want to understand the issuer's business and risks. This would likely drive simplification, which is likely to take the form of downsizing (since size increases complexity) and specialisation (since universal banking is harder to understand). This might also provide economics for independent risk assessment, rather than the crazy conflict of interest built into today's rating process.

Investors will demand reliable reporting from sub debt issuers, so this might provide impetus to clean up the current accounting standards mess which seems only to enrich advisors and confuse everyone else. Since transparency will equate with lower pricing, issuers have a strong incentive to be clear about their businesses.

As discussed previously, simple economics imply that banks will outspend and therefore out manoeuvre regulators. The beauty of the rolling sub debt concept is that it unleashes the markets to regulate the banks. Sub debt investors will be able to pay to keep on top of bank obfuscation, and thus to keep the banks honest. Dodgy banks will have a very high cost of capital. Markets are out of favour these days, but they are the most efficient method of capital allocation unless incentives are distortive. Pre-crisis politicians wanted more home ownership – markets delivered brilliantly.

The other advantage of rolling sub debt is that it allows the banks and the markets to figure by supply and demand how fast to adapt and in what direction. It is likely to be better to let banking evolve under market discipline rather than to ask regulators to decide what banking should look like. And since the markets will be left to determine how to reduce financial fragility (by deciding how to optimise risk and reward), the regulators will be freed to do a much simpler job – ensure honest reporting (and hopefully jail and bankrupt offenders).

Since it is not prescriptive on how, the rolling sub debt solution subsumes some of the others that I looked at above. We will find out from sub debt pricing whether investors prefer higher or lower tech banks, specialised investment banks separate from commercial banks, and so on. We may find some of the more inscrutable branches of finance go back to being partnerships, as was the norm in the past for investment private banking, because it is too hard to explain the business to investors. We might even end up in a situation from which the separation of credit from money becomes less jarring.

Conclusion

There are many potential ways to reduce financial fragility. Since banks have more resources than regulators, regulation is unlikely to succeed because the banks will just find new ways to game the system. For now, of the options discussed in this article, forcing banks to issue material rolling ten year subordinated debt still looks like the most workable current alternative. It is a clean yet strong mechanism that imposes strict discipline on risk in banking without regulating micro behaviour. It allows the markets to find optimal solutions to this worrying financial fragility. ■

David Blair, Managing Director

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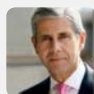
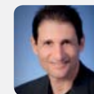


Lord Rose, Chairman, Ocado & former Chief Executive & Chairman, Marks & Spencer

Jogi Rippel, CEO & Founder, Tignum

Zanny Minton Beddoes, Editor in Chief, The Economist

Michael E. Raynor, Author of 'The Three Rules: How Exceptional Companies Think'



Dr Erez Morag, CEO & Founder, Acceler8 Performance

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