March/April 2016

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Treasury with foresight

Sustainable and responsible business practices are in the spotlight. What do corporate treasurers need to know and what can they do to ensure their business makes a positive impact on the world without having a negative impact on profits?

The Corporate View

Pratibha Advani

Chief Financial Officer
TATA Communications

China: approaching the last mile

As China continues on its journey towards economic reform and market liberalisation, the road may become increasingly bumpy. We ask what this means for China and for corporates operating in the country.

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Managing commodities risk

Back to Basics

In-house banks

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Diversity in the spotlight

As our industry moves towards a more diverse and inclusive future, our Women in Treasury initiative becomes ever more important.

On 14th April at the South Beach in Singapore we will host our third Women in Treasury Asia Forum. Designed to discuss gender equality within corporate treasury, we welcome women and men to attend and to continue to develop this discussion around diversity and inclusion on a broader level within this field.

Hear the latest insights from senior industry panellists including: **Vivian Peng**, Asia Treasurer & VP of Treasury, Flex Group (Vivian is also our Adam Smith Awards Asia 2015 Woman of the Year); **Pratibha Advani**, CFO, Tata Communications; **Lillian Sim**, Head of MNC Regional Coverage & Sales, Singapore & Hong Kong, Global Corporate Bank, J.P. Morgan; and **Deepali Pendse**, Head of Corporate Treasury Sales, Southeast Asia, Bank of America Merrill Lynch. Learn about the career paths these women have taken, the challenges they have overcome and galvanise your professional energy.

Each panellist will focus on a broad topic highlighted as being particularly pertinent in our 2015 Women in Treasury Study and you will have an opportunity to put your own questions to the panellists, as well as joining in the wider discussion and networking with your peers.

We look forward to seeing you there.

Enquire about attending

If you or a colleague would like to attend the Women in Treasury Asia Forum, to be held at The South Beach, Singapore on 14th April, please contact our Global Head of Events, **lisa.bigley@treasurytoday.com**, for further information.

Alternatively visit, **treasurytoday.com/women-in-treasury/events/asia**

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IN THIS ISSUE

Treasury with foresight

There is little doubt that recent examples of bad practices have placed the spotlight on sustainable and responsible business more than ever before. However, a green strategy is sometimes difficult to relate to in the treasury department. In this article, we explore what corporate treasurers need to know and what they can do to ensure their business makes a positive impact on the world.

China's credit challenge

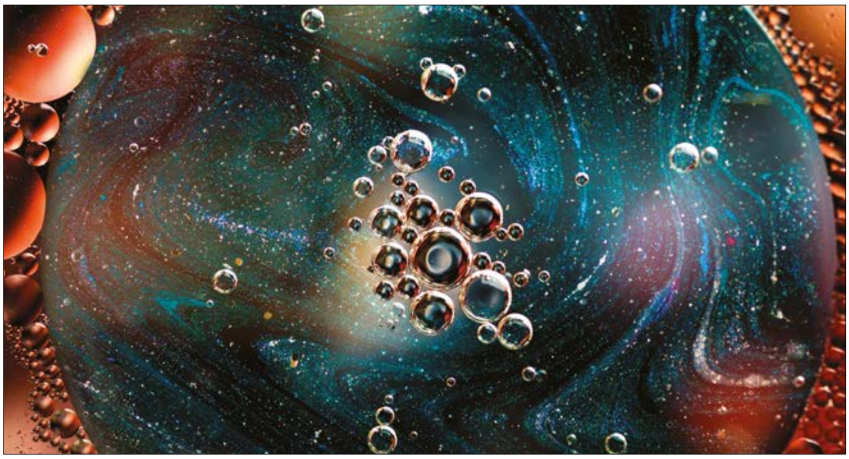
Following the global financial crisis, China was one of the few countries where syndicated lending continued to grow, playing a critical role in fuelling the nation's recent growth story. But, as China changes, so does its loan market. We ask if the strong demand for loans seen in recent years will continue, and if it does, will the banks be in a strong enough position to meet it?


Unlocking the strategic potential of SSCs

Standard Chartered

Unlocking the true value

The value of establishing a shared service centre (SSC) has been known for some time now. However, companies today are exploring ways to unlock additional benefits from the SSC model. In this article, Standard Chartered offers their insights into the challenging area of collections and how these can be managed by the SSC.



A matter of policy

Against a backdrop of market volatility, struggling interest rates and various regulatory reforms, Treasury Today Asia looks at the processes involved in establishing a best in class investment policy that is fit for purpose.

China: approaching the last mile

Over the last few decades China has become the world's second largest economy, a manufacturing hub, a mega trader, and overall a country with substantial economic and political might. But China is changing. What therefore does the future hold for the country, both on a macro-level, and also in terms of corporate treasury operations?

Managing commodities risk

In recent months the commodities market, both hard and soft, has been extremely volatile, creating a host of challenges for corporates and their bottom line. Here we explore the various risks associated with commodities, and ask why these materialise, and how they can best be mitigated?

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Pratibha Advani
Chief Financial Officer
TATA COMMUNICATIONS

The common acronym for Chief Financial Officer is CFO, but for Pratibha Advani, CFO at one of the world's largest communications groups, a more suitable definition may be Chief Facilitation Officer. In her role, Advani applies her creative impulses to their fullest extent, acting as a catalyst, promoting new ideas, sowing the seeds of innovation and improvisation, and driving productivity and efficiency within the organisation while also pursuing growth within a highly regulated environment.

A valuable proposition

Working capital optimisation, bank fee reduction and returns on idle cash are some of the many benefits corporates can expect from an in-house bank. But what is best practice when implementing such a structure, and what should be considered when choosing a location? Going back to basics, this article answers these questions and more.

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

FX risk: taking a new look at hedging

In 2015, volatility returned to the global currency markets – evidenced by numerous events including the Swiss de-pegging the Swiss franc from the euro and China's depreciating the RMB – and there is reason to believe that FX markets will remain highly volatile in 2016. At a time when companies of all shapes and sizes, but particularly SMEs and mid-market corporates, are striving to tap into international markets in order to find new growth opportunities and counter sluggish domestic demand. It is, therefore, unfortunate to realise afterwards that the return on an investment or a transaction can often be neutralised by a negative exchange rate variation.

Indeed, all importing and exporting companies will face FX exposure at some point. And these exposures can be classified in three ways. Transaction exposure arises when a company with import/export activities has committed cash flows to be paid to buyers, or to be received from suppliers in a foreign currency. "If the transaction is not hedged, it will de facto generate an open FX position subject to the exchange rate fluctuations between the sale and the payment of funds," explains Jean-Philippe Godard, Manager at DPC Asia Ltd. Hong Kong. "The risk stems from the exchange value of the foreign payment when it is exchanged for home currency terms, which could result in a loss or a gain for the company."

On the other hand, translation exposure arises when a company with operations overseas translates the balance sheet and income statement items of its foreign subsidiaries into its home currency. "The translation process can result in unfavourable consolidated financial statements, providing misleading information to management regarding actual overseas operations performance," says Godard. The third risk is economic exposure caused by the direct macroeconomic impact of sharp FX swings on a company's competitive position in a given market compared to its foreign competitors. The company's transaction volume in this market would be structurally impacted. For example, a Malaysian latex glove manufacturer will be subjected to economic exposure if the Malaysian ringgit appreciates against the Thai baht, since it will result in the local gloves being more expensive than their Thai competitors.

Integrating FX

Given that FX risk is one of the main concerns among treasurers and CFOs, it makes sense to integrate this into the company's strategy, and there should be a clear competitive advantage in addressing the risk. According to Godard, the implementation of an effective FX hedging strategy can offer many benefits for companies active in international markets. These include allowing the company to reduce income variability in case of exchange rate swings and mitigate the long-term strategic effects by buying some time to adapt its strategy in case of large structural shifts, while less prepared competitors are weakened. "Improvements can also be made in accountability and internal communication by the implementation of standard procedures and workflows that can be shared at different company levels," he adds. "The cost of capital can also be reduced and the valuation of the company can be increased by enhancing the predictability of its results. But ultimately, the main benefit is that it allows the company to focus on what it does best: its core business."

New rules for China's budding MMFs

After a year of rip-roaring growth, change will soon be afoot in China's nascent money market fund (MMF) industry as new rules are introduced that promise to bring the regulation of MMFs closer in line with international standards. Since February 2016, Chinese MMFs have been subject to a package of new requirements that should go some way to addressing concerns about risks that have been developing in the industry in the wake of the recent inflows. That regulation around Chinese MMFs is now moving closer to intentional standards is timely, given how important the funds have become to institutional investors – including international companies – in China of late. The past year has seen exponential growth in investment. Assets Under Management (AUM) for Chinese MMFs more than doubled in 2015, and while a lot of the growth has been driven by the arrival of online funds for retail investors, the trend in AUM is also a reflection of what a growing number of treasurers are doing with those big cash balances that have built up onshore over recent years.

"Last year we saw a huge growth in MMF investment in China, partly driven by institutional investors," says KL Cheah, Head of Global Liquidity Sales, Greater China, J.P. Morgan Chase Bank (China). "We are seeing a growing popularity in MMFs across the board as retail clients gain easier access to these investments, increasing popularity in MNCs using it as a cash management option and institutional funds flowing more readily into the product as well. This is happening at a time when we have regulatory development of the overall MMF industry in China that make it more investable and more comparable to the AAA rated funds market." Other industry experts agree on this assessment of the market. "We are seeing that more and more corporates that traditionally would have put their money in the bank are now beginning to accept MMFs as one of their investment options," says Li Huang Associate Director, Fund and Asset Manager Group, Fitch Ratings.

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

Funding strategies in Asia

Since the financial crisis, corporates in emerging markets (EMs) have been able to borrow increasingly cheaply in foreign currencies, leading to record dollar denominated bond issuance in Asia. Where should EM corporates focus their funding strategies following the rate lift-off recently embarked upon by the Federal Reserve?

Thiam Hee Ng
Principal Economist
Asian Development Bank

With the Federal Reserve raising its interest rate, US dollar funding will become more expensive for the region's corporates looking to issue US dollar bonds. At the same time, the more volatile economic environment and increased risk perception of emerging markets will likely further push up the cost of borrowing in US dollars.

Corporates that have borrowed in US dollars are facing higher debt servicing cost now with most of the region's currencies having depreciated against the US dollar. In some cases, the increased debt servicing cost from depreciation has far exceeded the savings from lower interest rates from issuing dollar denominated bonds. This highlights the risk of borrowing in US dollars for corporates especially if the borrowing is unhedged or if the corporates do not have substantial US dollar revenue which can help serve as a natural hedge.

One alternative would be to explore funding in other currencies. The cost of borrowing in euro and Japanese yen remains low. However, going down that route would mean corporates would be exposing themselves to exchange rate risk. Also the offshore bond markets in these two currencies are smaller and less liquid.

Going forward, Asian corporates should look more towards using the domestic bond markets to satisfy their funding needs. For domestic oriented firms borrowing in local currency, this will help mitigate the exchange rate risk. This is especially true if they expect the US dollar to appreciate further.

There has been considerable growth in Asia's local currency bond markets since the 1997/98 Asian financial crisis. Following the crisis, the region's governments started the Asian Bond Market Initiative to promote the development of local currency bond markets to avoid the problems of currency and maturity mismatches. Since then, the local currency bond market has grown by leaps and bounds. The total outstanding amount of local currency bonds in emerging East Asia reached almost US $9trn as of the end of September 2015. Early on in their development, the corporate bond markets tended to be much less developed than the government bond markets. But the gap has narrowed considerably. This means that the local currency bond market is now a viable option for meeting corporate funding needs. Efforts are also underway to make it easier for corporates to tap the regional local currency markets by streamlining the processes and procedures. This should further facilitate corporate funding through local currency bond markets.

Jan Bellens
Asia Pacific Banking & Capital Markets Leader and Global Emerging Markets Leader
Ernst & Young

Given current regional economic uncertainty and exchange rate volatility, yet interest rates rising following a prolonged low cost period, corporate treasurers in emerging Asia Pacific (APAC) are increasingly challenged in servicing and refinancing their USD-denominated debt. Effectively, higher real rates and lower capital availability are spurring them to revisit funding options to optimise on capital efficiencies.

For now, we expect bank financing to remain the dominant source of funding for regional corporates, with these loans proving to be most cost effective especially for seasoned organisations with good track records. Bank financing continues to account for approximately 50% of corporate borrowing in EMs as compared to below 25% for peers in developed markets. As such, despite the region's slowdown raising risk premiums for EM borrowers (particularly for industries such as energy and power, materials and real estate that are at higher default risk due to weaker demand from core markets like China), banks are still competing to capture big ticket lending opportunities and jostling to offer more attractive loan pricing to the blue-chip clientele.

Nonetheless, with steadily increasing USD-denominated rates as the Federal Reserve tightens policy, corporates in EMs that depended heavily on foreign currency loans for inexpensive financing while generating cash flow domestically could consider less-volatile local currency alternatives. Those that rely largely on shorter tenured loans are also exposing their organisation to rising rates and should lock in borrowing costs over longer repayment periods in advance of further expected rate increments.

Besides financing corporate activities via loans, bonds offer further funding diversification for EM corporates. While issuance has tapered drastically since H215 (with investment banking fees from bond issuance for the full year declining 18% globally), bonds remain a popular funding choice for EM corporates. However, credit quality has been deteriorating over the last three years with defaults for speculative grade corporates likely to increase. While EY is taking a sanguine view on the corporate debt market, banks are raising yields in response to growing corporate risk (perceived or otherwise) and bonds will become an increasingly expensive form of funding in the mid term. But despite a less robust debt market, bonds will remain a viable fund-raising option primarily for well-established corporates, though fund raising will be tougher for sectors struggling with the current downturn.

For EM corporates with USD and other foreign currency denominated bonds, those that lack natural hedges and sufficiently sophisticated currency risk hedging mechanisms are likely to face currency mismatch challenges and increased credit and refinancing risk. This would encourage the development of more robust in-house treasury departments, as well as spur the respective local currency bond markets to enhance services to corporates seeking more efficient onshore replacement funding and protection from forex volatility. This obviously does not happen by chance and would need support from EM governments to raise market efficiencies, transparencies, and foster higher issuer and investor participations.

Meanwhile, fund raising via follow up equity offerings and new public listings will remain lacklustre until turbulence in global markets eases and investor confidence returns. Investment bankers already felt the pinch in 2015, with a 13% year-on-year fall in global fees from equity products. Waning risk appetites will continue to dampen corporate's enthusiasm to list their shares until the markets turn calmer.

All in, despite the current market volatility, investment grade corporates continue to benefit from a reasonable selection of funding options. It is the smaller, newer organisations that lack established track-records we see struggling to realign their funding strategies following the recent rate increases. With bank financing getting increasingly scarce for this demographic, there is a massive white space for alternative lenders such as peer-to-peer and debt and equity crowdsourcing platforms to expand rapidly into the EM regions with alternative, more accessible funding options.

Ranu Dayal

Senior Partner &
Managing Director

The Boston Consulting Group

Before addressing current funding strategies, it is important to understand the situation in years prior. If you go back a few years, the APAC markets had high growth rates. It was a time when the prospects looked desirable: the appreciation of exchange rates and low interest rates in OECD markets, for instance. There was the view that it was a great opportunity to raise capital and the ability to pay down debt was seen as good. Now, with the US interest rates starting to rise and EM currencies declining, the attractiveness of foreign debt and the ability to service that foreign debt from domestic earnings is a difficult issue.

In terms of the right cost of capital, even sophisticated treasuries are not very consistent in their approaches. There are a variety of ways in which corporates have thought about, and are thinking about, their cross border funding and capital raising. In addition to the moving parts of exchange rate changes and interest rate changes, the fundamental growth drivers in EMs have been changing – all of which results in differences in terms of funding approaches corporates in Asia are adopting today versus five years ago.

With the Federal Reserve announcing higher rates, the strength of the US dollar resulted in a reduction in how much funding corporates wanted to do in USD. Now the Fed is being encouraged to slow down the rate of interest, or the timing of the rate increases. The inflationary pressures that were beginning to appear in the US are abating – for instance, if the price of oil stays put, then it reduces the likelihood that US rates will increase. In some ways, this is a counterbalance to the fact that US funding will appear less attractive than it was some time ago.

This uncertainty points to the need for corporates to undertake scenario-based assessments of the alternatives available. They need to model what the company's cash flows will be given different situations. If, for example, they are orientating debt in renminbi, corporates should question whether the currency is likely to appreciate or depreciate, what the ability is to pay down current debt, how much of it would be serviced by revenues from where the company is operating in renminbi and where it will need to be serviced from revenues in other parts of the world. It is about knowing what kind of cash flow stress each scenario would create on the different parts of the business that have different underlying currency and interest rate dimensions. Corporates should be using a structured set of analytic techniques, not relying on their conviction or a single point estimate, in order to lead a more comfortable position from which to service the debt.

Where home market weakness may diminish the capacity to service foreign currency denominated debt, detailed cash-flow modelling and liability matching is even more critical when assessing options. However, for some of the leading EM corporates, foreign currency financing for acquisitions abroad may make sense if focused on foreign revenue-generating options. All in all, assessing the impact of the large number of moving macro parts – some of which are outlined above – requires: sound analytical framework, development of different business scenarios and active dialogue with lenders to fully appreciate the range of options available.

The next question:

"Unethical business is increasingly in the spotlight. How can treasury help improve their company's ethics?"

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

Treasury with foresight

There's little doubt that efforts to engage in sustainable and responsible business are in the spotlight more than ever before; Volkswagen's share prices plummeting amidst last year's emissions scandal, the public reaction to Amazon's treatment of employees and the outrage that China burns much more coal than it claims – the list could go on. But what do corporate treasurers need to know and what can they do to ensure their business makes a positive impact on the world without having a negative impact on profits?

When China's President, Xi Jinping, visited the UK late last year – the first state visit from a Chinese president since 2005 – it marked an important moment between the two countries. The trip, however, was somewhat tainted by China's poor history with human rights; numerous reports narrowed in on the fact that the country's record has been distant from international standards until recently. The Telegraph questioned whether Jinping deserved the UK's "red carpet" treatment, for instance. The general air of malaise was one indication, amongst many, of a mind-set that is focused on a responsible future more than ever before.

And it isn't only the treatment of people that is receiving precedence; engaging in business that has a positive environmental, social and governance (ESG) impact has been in the spotlight for some time. "The train has truly left the station," says Gavin Power, Deputy Executive Director for the UN Global Compact, a key sustainability initiative. "Sustainability is a global agenda here to stay."

Since it is sometimes disregarded as a buzzword in the corporate arena, it is apt to provide a definition of sustainability. The UN Global Compact felt the need to put a stake in the ground and defined sustainability as the delivery of long-term value towards environmental, economic, social and ethical concerns. There remain some obvious hurdles, including the disparity in what embracing sustainability means for different businesses and the sceptics who believe that, in current economic circumstances, sustainability is unaffordable. But momentum is gaining ground.

What do companies owe society?

Bill Gates, however, probably wasn't alone in his belief when he claimed last year that the private sector is too selfish to produce effective energy alternatives to fossil fuels. "There's no fortune to be made," he told The Atlantic. For many, it isn't unreasonable to question the extent to which sustainability is an obligation for business – their allegiance, after all, is primarily to growth and profit generation. Axel Boye-Moller Head of Global Transactional Services, Asia, at Westpac, clarifies that this is an issue to overcome. "A sustainable approach to doing business makes sense for all stakeholders, including shareholders, and there are significant opportunities for businesses that get this right. However, in the short term, there are challenges. For example, producing sustainable agricultural commodities can be more expensive in the short term. There is a lot of discussion around who is going to wear that cost and how it will play out – however it is important to maintain focus on longer-term value, in line with shifting expectations."

But, Power argues, there is a fiduciary duty to answer these questions. "For large companies and investors, there is a legal responsibility to ensure their organisations are managing critical sustainability issues." Why? "Because they are risk issues." According to a recent report from the UN Global Compact, 'Fiduciary Duty in the 21st Century', in addition to the ethic argument of meeting the needs of today without compromising future generations' ability to do the same, there is a legal case for sustainability.

In terms of investment, ESG factors are certainly viewed as risk factors. Loic Dujardin, Director, Research at Sustainalytics, a leading global provider of ESG and corporate governance research, ratings and analytics, explains that the research they conduct enables investors to identify ESG risks that could have an impact on the bottom line of companies. "A typical example would be investigating the potential water scarcity for a mining or power generation company. Without water, they are not going to be able to operate the mines or power generation plants." The risk management performance of companies, he says, is something asset managers and asset owners, who have a long-term investment perspective, should pay attention to. In the words of Mark Carney, Governor of the Bank of England and Chairman of the G20's Financial Stability Board: "The more we invest with foresight; the less we will regret in hindsight." At the end of the day, ESG factors – such as climate change – are systemic risks to the economy, says Dujardin. "And for investors in Europe and North America, integrating ESG factors into investment decisions has become mainstream."

In Asia, the story is slightly different. Although the sustainability landscape is rapidly changing, it is still a relatively new idea in the region. Broader recognition means unlocking the corporate leverage necessary to accelerate sustainable progress. This requires a new business mind-set – one which, according to Power, necessitates "an imperative on culture change top to bottom". This includes the sustainability of a company's own operations; the sustainability of its products and supply chain; and the encouragement of sustainability within the end customers' lifestyles, and of all key business partners – suppliers or banks, for instance. It is about building resilience within company operations, as well as in the communities in which they operate. "At the very heart of that, it is about winning the hearts and minds of customers," adds Boye-Moller.

If further motivation is needed, however, Sustainalytics offer a benchmarking service for corporates "so within a specific industry, a company can find out how they perform compared to peers", says Dujardin.

Times are changing, however: the options available to corporates, the economic drivers encouraging sustainable business and actions many country leaders are taking towards this topic are on the rise. "Five or ten years ago,

Circular supply chains

A change from engrained business models, advocates of the circular economy argue that products should be designed to maintain their quality and continue to be useful to the economy beyond their typical shelf life. "In a circular economy, products and materials flow in loops, maximising asset utilisation and minimising waste by design. It avoids the economic losses along the value chain and negative externalities inherent to the traditional linear model of production and consumption," say Jocelyn Blériot, Executive Officer and Ian Banks, Editor, both from the Ellen MacArthur Foundation, a charity with a mission to accelerate the transition to a circular economy. Working with businesses, governments and academia, the Foundation seeks to set out the economic opportunities provided by the restorative and regenerative activities needed in such an economy.

Blériot and Banks provide the following two examples of circular economy business models being used on the ground. One hundered La Place restaurants in the Netherlands provide 2.5 tonnes a week of waste coffee grounds to GRO-Holland, a company that uses them as a growth substrate for oyster mushrooms. The mushrooms are then sold back to the same restaurants to be used as ingredients. The supply chain is therefore made circular by turning one player's by-products into feedstock for the other.

As an example of a pay-per-use business model, in addition to selling lightbulbs, Philips now also signs contracts to provide light, by the lux. The company keeps ownership of the lighting system, taking care of maintenance and remanufacture during the contract. Such a model can be both more profitable than traditional products sales for the manufacturer and cheaper for the user. It also promotes increased customer interactions – and, potentially, increased customer loyalty.

non-business organisations and spheres of influence were unclear about the best modes of engagement with the business community. Fast-forwarding to now, we are at an inflection point in the sustainability movement; multilateral organisations, governments, civil society, investors and corporates are aligning in some exciting ways," says Power. The Sustainable Development Goals (SDGs), for instance are one example of this increasing alignment.

The tide is turning

For corporates, despite slow economic growth and lingering volatility, investing in sustainable business practices is becoming an attractive prospect – one that can add value, people are beginning to realise, rather than adding just another cost to the business. Companies are reporting substantial savings as a result of their efforts to reduce energy use and waste, for instance. "It makes business sense to embrace sustainability," says Catherine Bremner, Global Head of Sustainable Finance Solutions, ANZ. "Yes, there are challenges in terms of the change, innovation and technology necessary but there are massive opportunities for businesses." Her colleague at ANZ, Christina Tonkin, Managing Director – Global Loans & Advisory, adds: "Corporates want to be operating for the long term and those that boast robust processes around their impact on the environment and society are the ones that will be in for the long haul. It is as simple as that."

For example, businesses are demonstrating compassion for current environmental concerns. In October last year, 38 firms in Singapore pledged that their products were free of raw materials from companies being investigated for forest fires in Indonesia – an environmental disaster caused by forest clearance known as 'slash and burn', where land is set on fire as a cheap way of clearing it for new planting. The cost of this activity as of November 2015 was estimated – by the Indonesia government – at $47bn worth of financial damage to the region's economy, illustrating the damage not only to the environment, but companies who are reliant on its health.

Corporates in Singapore aren't the only ones adopting environmentally considerate initiatives. More of the success stories include: L'Oréal announcing its plan to become "free from deforestation" in the production of all its products by 2020 at the latest and Unilever supporting the most progressive suppliers which can guarantee key criteria, including compliance with the laws in the country on cultivation; informed consent from indigenous people and local communities; conservation and restoration of forests; and a pledge not to clear peat for new plantations.

Banks too are leading the charge against unsustainable primary goods. Westpac, for instance, recently launched a sustainable shipment letter of credit (LC) as part of the Banking Environmental Initiative to transform supply chain practices. By doing so, corporates can access commodities with a recognised stamp of approval to certify that they are produced sustainably. "We are now working with The Banking Environment Initiative to expand similar principles into more commodities and other trade finance instruments," says Siobhan Toohill, Group Head of Sustainability and Community, Westpac.

As the range of sustainable financial products on offer expands, companies seeking out, or actively demanding, such solutions are leading 'the new norm'. And the number of corporates taking sustainability matters into their own hands and looking for support is on the rise too, according to Power. The UN Global Compact is joined voluntarily, to publically commit to a universal language on corporate responsibility with the provision of learning materials and ongoing support. "We've passed a really important hurdle globally," says Power. "When the Global Compact started in 2000, we had to coax companies to join but it's now aligned with societal trends – graduates, for instance, look to join working environments which actively engage in the subject – and the membership of several large companies has encouraged others to join." The initiative now has 8,000 companies and 4,000 non-business participants based in over 160 countries committed. Joining primarily involves company alignment with The Ten Principles, focused on human rights, labour, environmental and anti-corruption priorities.

Although it is a leadership agenda, the principles need to be cascaded throughout the organisation. Companies are provided entry level management resources to ensure they meet the expectations of how to implement the principles. The Global Compact also continually challenges companies to do more and produced a blueprint as a high-level aspirational model a few years ago. As Power says: "Sustainability needs to be a progressive agenda."

Commitment also includes the mandatory requirement for corporates to submit Communication on Progress (COP) reports annually. Not only does this afford transparency, the UN now boasts the largest repository of these public sustainability reports. They can serve as learning resources, but have also generated numerous partnerships for companies who perhaps had never thought about sharing and inviting other partners. "I get calls and enquires from NGOs and UN agencies who, after reading reports, want to work with some of the companies on projects that they had heard about for the first time in a COP," says Power. The Global Compact also has an interactive Business Action Hub to encourage similar engagement.

The banks' role in championing change

Banks, of course, play a huge part in ensuring sustainable business practices come to the fore. "Five years ago, the first things banks thought of were immediate footprint actions – such as conserving electricity or reducing paper use – which are important but don't get to financial institutions (FIs) central role in the global economy, finance," says Power. More recently, banks in Asia Pacific (APAC) have been taking some impressive steps, however.

Westpac received recognition as the industry leader for banks in the 2015 Dow Jones Sustainability Index. "Sustainability is fundamental for the bank, it is embedded into all processes – our lending criteria for clients, for instance," says Toohill. "We look at sustainability at a country and sector level, at a customer level and at a transactional level." If a client's sustainability policies aren't up to scratch, banks will work with them to create alignment. When it comes to sensitive sectors, such as agribusiness, because there are a range of potential environmental and social impacts, specific mission statements and strategies exist.

In terms of guidelines on an individual transactional level – project financing, for instance – both ANZ and Westpac are signatories of the Equator Principles which sets a framework on risk management for projects. Banks often also commission separate research as part of that assessment. Trade finance, on the other hand, is short tenor and there may be transactions that need a decision intra-day "so we've got tools, frameworks and checklists in place to assess risks at that level quickly", says Toohill.

In recognition that sustainability should be progressive agenda, banks keep their offerings up-to-date. "We need to have the finance available for corporates so they can grow their businesses in a sustainable way," says ANZ's Bremner. For instance, originally in Australia a lot of focus was on renewable energy, mainly wind power, but the bank is seeing mounting interest in rooftop solar. "Therefore, finance solutions are tailored in a way to suit individual client needs." One of the largest targets of its type to date, an AUD 10bn commitment to support customers' transition to a low carbon economy by 2020, will help meet this developing need.

Additionally, when Westpac exceeded its goal of AUD 6bn of funding for the CleanTech and renewable energy sector by 2017, it set a whole new benchmark in terms of what classifies as sustainable and warrants the allocation of funds, rather than resetting a new end objective. For example, a higher threshold for green buildings within the portfolio. "All of these movements are of interest to corporates across Asia," says Boye-Moller. "I recently participated in a seminar in China, organised by The Banking Environment Initiative, alongside other banks, regulators, academics and some of the largest Chinese commodities importers. They were incredibly interested in what the banking sector is doing in the sustainability space."

Indeed, according to Tonkin, "there are few institutions that will touch customers' right across the globe and across all different sectors in the way FIs do. I welcome the increasing involvement of FIs into the sustainable finance space as the pivotal role banks play will benefit corporates and society going forward." Providing their experience, driving advocacy through the standards set in lending practices and underlying policies, banks can raise the bar. For the treasurer, it is about selecting banking partners that can support their company's transition to sustainability. The product suite, funding and attitude towards supporting ongoing sustainability are of consideration. Watch out however, as Power believes some are behind the times in terms of ESG concerns.

Taking the lead

In the near future, ANZ's Tonkin and Bremner believe there will be an increased interest in company resilience – whether existing infrastructure is up to the task of withstanding increasingly severe weather, for instance. "Part of the challenge will be funding over the long-term," she says. When US President Barack Obama delivered a call to action to some of the world's biggest companies at the Asia Pacific Economic Cooperation forum in Manila in November last year, he raised the issue that "few regions have more at stake in meeting this challenge" than APAC. Aptly, as Tonkin says: "We are seeing sustainability embraced more as part of the DNA of business. It's part of the conversation on a daily basis, elevated in the thinking of corporates across APAC beyond what was once a fringe subject."

Investment opportunities, as well as funding opportunities, are on the rise. "We see good momentum in three markets predominantly: Japan, Singapore and Hong Kong," says Dujardin. "Drivers include reforms and initiatives from regulators, governments, banks and other financial intermediaries. Investors too are concerned about the disruptive effects climate change could have on the stability of their portfolios." Therefore, it is in the best interest of all that businesses align with climate and societal objectives. This could mean capital reallocation strategies for investors or for treasurers, investing capital in projects that will deliver sustainable returns, ensuring they are resilient to shocks that may come, and avoiding feeding into negative concerns through careful selection of business partners.

The risk of ignoring ESG priorities is becoming clear for the corporate world and, as a result, action is occurring – in supply chain management, for instance (see box opposite). But there remain aspects somewhat out of a treasurer's control. More than anything, though, as Boye-Moller says: "In Asia Pacific, we need to get to a point, as you see in many more developed markets, where you have a large groundswell of consumer sentiment. People who are demanding, and are prepared to pay more for products that are produced sustainably. That's where the region is still on a journey and each market is slightly different." With the economic climate becoming more volatile and risks on the rise, perhaps this is an agenda item businesses in APAC should be looking to take the lead on.

China's credit challenge

The syndicated loan has proved a useful product in supporting China's recent growth. But will the strong demand for loans seen in recent years continue? And if it does, will the banks be in a strong enough position to meet it? We take a look at some of the key challenges now facing the markets fuelling China's growth engine.

In much of Asia, the global financial crisis brought about a sharp decline in syndicated lending. But that didn't happen in China. On the contrary, China was one of the few countries where syndicated lending continued to grow through the crisis. Syndicated lending volumes have continued to grow steadily over recent years as well, to the point where the product is now one of the most popular sources of finance for businesses in China.

The credit financed through the syndicated lending channel has therefore played a critical role in fuelling the nation's recent growth story. But will it continue to in the years ahead?

The outlook is mixed. Despite the talk of a 'hard landing', China's official growth rate in 2015 was 6.9%. Slowing – but still robust – growth figures, should mean that demand is still there (especially while M&A continues to surge and more corporates look to refinance the foreign currency loans weighing on the balance sheet). The real question, then, is around supply and, in particular, if the ability of banks to lend might be restricted by the non-performing loans (NPLs) now accumulating on their balance sheets.

But there is also another, perhaps bigger, story to tell here. The history of China's loan market very much mirrors the country's economic development, more specifically the transition from a centrally planned economy to a market-based one. Consequently, syndicated lending in particular has been subject to tremendous changes in recent years and with the economy continuing to open itself up to market forces, there is very likely more still to come.

The journey so far

In the not too distant past, syndicated lending in China was the near exclusive domain of Chinese banks, the so-called 'Big Five' in particular. In 2006, this began to change following reforms that allowed more foreign participants to commence lending in renminbi onshore and in foreign currency offshore, often collaborating with domestic banks to take advantage of their superior origination and distribution networks. Much of the liquidity supplied through the expanding loan market went into infrastructure financing, where syndicated loans became the preferred vehicle for extending the credit since it reduced the risk of default caused by a single bad project. Since large amounts could be arranged relatively quickly compared with the other available channels, they also became popular with borrowers. Before too long syndicated lending began to dwarf other financing channels in China.

Today China dominates the syndicated lending market in Asia, with volumes of $100bn recorded in H215, accounting for around 31% of all lending in Asia, excluding Japan. Chinese banks remain the dominant players in the domestic market and, furthermore, have been very active players across the Asia Pacific (APAC) region with Chinese institutions representing four of the top mandate arrangers in the region. Even in highly developed markets like Australia, Chinese banks have been competing with domestic institutions and participating in syndicated deals. Foreign banks, meanwhile, tend to focus their financing activities offshore in Hong Kong in credit denominated in euro, dollar or yen. Occasionally foreign banks will arrange a syndicated loan for a European subsidiary that have not been able to build relationships strong enough yet with the Chinese banks. By and large, however, most of the large RMB denominated transactions we see being executed onshore in China come from Chinese lenders.

A turning point?

Taken together though, the credit extended through syndicates onshore and offshore account for much of the credit growth that we have seen across the region in recent years. "China has really been at the forefront of syndicated lending in APAC in the past few years, largely due to the overall growth in investment in infrastructure," says Amit Chopra, Syndicated and Commercial Lending Specialist, at Misys. "If we look at year-on-year growth, 2015 has not been as great in terms of percentage growth, but China has still been the biggest contributor in the region, excluding Japan."

More moderate syndicated lending activity is being reported offshore especially. Does this mark the beginning of a turning point in which demand for syndicated financing begins to fall off, both in Hong Kong and mainland China? Not necessarily. To understand why syndicated lending has not been so robust during the past year, it is important to consider where a large chunk of the demand the banks were seeing originated from. While a lot of demand for financing has come from clients with an underlying requirement for foreign currency, such as an acquisition, a sizeable portion of it has also been arbitrage driven. For some companies it made sense to borrow in foreign currencies like US dollar or euro, before converting back to renminbi to arbitrage between the low offshore borrowing costs and the high onshore CNY deposit rates. But since the two downward 'adjustments' to the currency made by the Peoples Bank of China (PBoC) last year, activity around that carry trade has all but vanished.

"I think demand is still there," a loan syndications head at a foreign bank in China told Treasury Today Asia. "It is a little bit more subdued than it was, but the nature of the demand has changed a little bit," he explains. "A lot of [arbitrage driven financing] has fallen away over the past six months. But there is still a drive to go offshore and buy and acquire Western companies, whether it be to obtain technology, manufacturing capabilities or natural resources offshore. That strategically driven demand for credit remains in place, the bit that has fallen away is the companies borrowing cheaply in USD."

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Phil Lipton, Chairman, Asia Pacific Loan Market Association, agrees that diminished opportunities for arbitrage is likely to mean less offshore syndicated lending in foreign currencies. "I think we have seen a shift back to onshore borrowing," he says. "That is not just the depreciation – China has cut interest rates too, so raising money in China is now a lot more attractive than it used to be. For these two reasons there is more liquidity in the country now. As a result, you will see companies, in relative terms, raising more onshore – and I think that is going to increase going forward."

Bad loans

Meanwhile, the outlook for the onshore loan market remains relatively favourable into the medium term, underpinned by prospects for strong – although decelerating – economic growth (which the IMF expects to remain above 6% until 2020). However, slowing growth and the commodities slump will have some impact on the market, with lenders expected to become a little more selective in what they finance. Already we are seeing a decline in syndicated loans and one sector, in particular, is facing some steep credit challenges.

In a 2015 report, analysts at Australian investment bank Macquarie looked at the figures on China's debt profile and found that companies in sectors such as mining, smelting, and material now have debt levels that are so high the firms are under "extreme strains to survive". Essentially, corporate debt in this sector increased substantially in the past three years, and the earnings of the companies who have borrowed have not increased at anywhere near the same pace. Naturally, banks are becoming a little reticent when it comes to meeting demands emanating from this space.

But while that has been the focus of much of the concern, the change in sentiment has not been entirely restricted to the commodities sector. On the contrary, privately owned enterprises and even some of the less eminent state owned enterprises (SOEs) are also feeling the squeeze. Several years ago, banks were lending to nearly everyone who required it. But today, financing – especially for companies linked to commodities – is becoming much more difficult. There is also less enthusiasm to finance third or fourth tier SOEs than before, while some banks refuse to touch privately owned enterprises altogether, due to the perceived risk.

Also weighing on the minds of lenders, perhaps, is asset quality deterioration from problematic legacy loans. New non-performing loans (NPLs) held by Chinese banks more than doubled in 2015 according to recent news reports.

Even by the Chinese authorities own, more optimistic statistics, bad loans rose to RMB 1.27trn by the end of 2015, sending the NPL ratio up to 1.67%. "The NPL ratio is alarming," says Chopra. "And it gets even worse when you look at the second and third tier of the banking sector."

This worrying development has not escaped the attention of the institution responsible for regulating the Chinese banking system, the China Banking Regulatory Commission (CBRC), who recently introduced a minimum loan loss provision ratio (although the central bank, now in full easing mode, recently cut the requirements in order to stimulate borrowing and prevent a further currency devaluation). Consequently, banks now have to set aside more cash than they did previously for future losses by the total of NPLs.

Chopra says this change will inevitably have a big impact on the flow of credit and syndicated lending in particular: "The CBRC is taking an active step in this and, obviously, this will impact the banks' ability to lend as openly as they did in the past," he notes. "One of the steps is around Loan Loss Provision (LLP) ratio and Chinese banks are required to keep a minimum ratio of 150% and some of the large banks are currently very close to this LLP ratio. This obviously means that banks will have to infuse more capital if they want to remain above this ratio while continuing to lend in market. The NPL's and interest rate liberalisation can have an impact on bank's profitability going forward."

But credit should continue to flow, so the experts say, to the less distressed areas of the Chinese economy, irrespective of the NPLs accumulating on the balance sheets of banks and the debt troubles of commodities firms. Perhaps this is why, despite all the market turmoil at the beginning of the year, credit expanded by 12.7% in January, the fastest pace since April 2015. "The banks will be lending to companies where they are seeing growth," says Lipton. "There may be an aversion to where there is stress in a sector. Corporates that are having more problems are going to be a lot more cautious about borrowing new funds and leveraging up, whereas on the domestic front there's still growth, so we will probably see banks moving their focus in that direction."

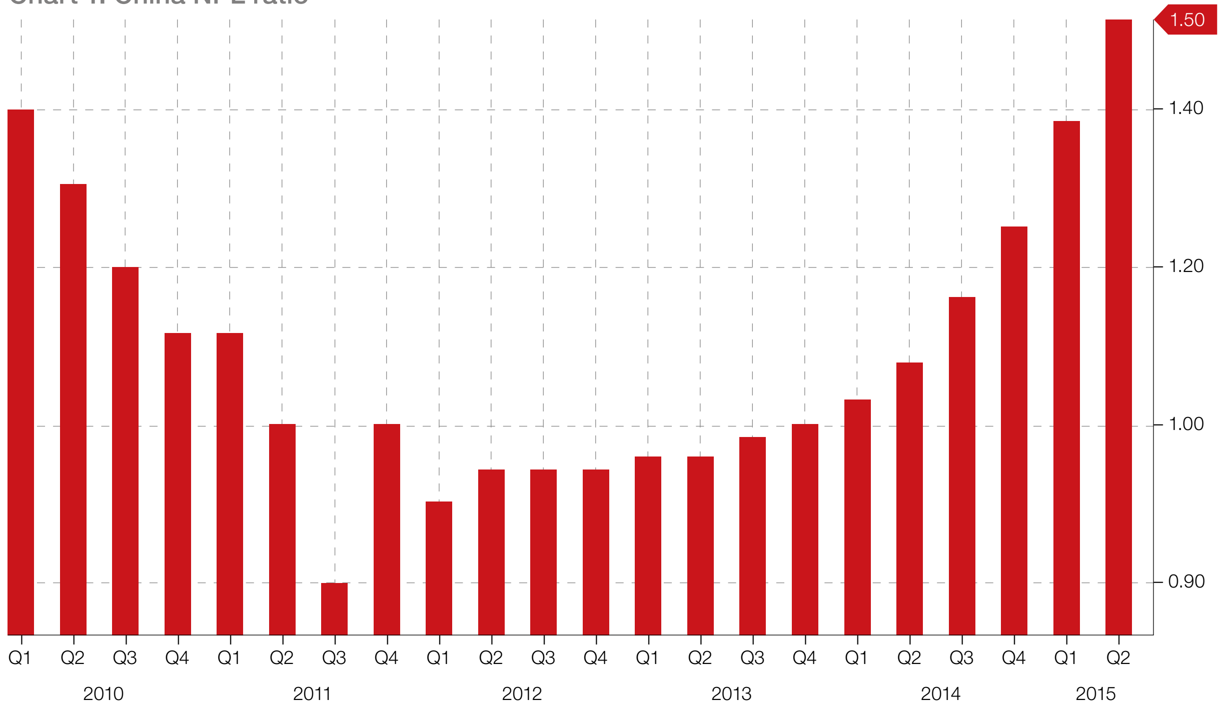
Advice for borrowers

What should treasurers take from this? Well, those who require financing in the near future – as many companies will all the while the M&A upsurge continues – should not have too much difficulty raising it through the loan market, with the notable exception, that is, of all those heavily leveraged companies in sectors most exposed to the slump in commodity prices.

For everyone else, the advice is twofold: do not hang around, and do not get too distracted by the pricing. Companies with a financing requirement should go to the market as early as possible, and understand that it may make sense to pay for certainty in the current market. That might mean paying banks to underwrite or dealing with banks that are slightly more expensive, but the cost of debt is not going to be as important as making sure the company achieves what it want to achieve from a financing perspective.

But with lower borrowing costs and wider availability of funds on the debt capital markets, will syndicated loans continue to be the fuel in the Chinese growth engine? Chopra believes we will see more companies in China financing themselves through bond issuance going forward, but this should not, he says, have too great an impact on the demand for syndicated loans. "The bond market is certainly an attractive option, especially for organisations that have already exhausted syndicated lending or wish to diversify their overall portfolio", he adds. "But I would say that any company that wants to raise considerable capital from the market, syndicated lending will continue to be one of the favoured vehicles."

Chart 1: China NPL ratio



Source: Bloomberg

A matter of policy

If a treasury investment policy has not changed to reflect the 'new normal' of regulatory reform, market volatility and struggling interest rates, then something is very wrong. Taking lessons from Europe and the US, Treasury Today Asia looks at the processes involved in establishing an investment policy that is fit for purpose.

With regulatory reforms in the money market fund (MMF) space and the far-reaching implications of Basel III making their mark on the financial community, corporate investments are facing the kind of pressures now that warrant very close attention. This attention must inevitably extend to investment policy as treasurers struggle with an unprecedented period of low interest rates across the major currencies that shows little sign of lifting anytime soon.

"It's clearly an extremely challenging environment," says Roger Merritt, Managing Director, Fitch Ratings. "I cannot think of a time, certainly in the past 25 years, that treasurers have faced so many different challenges at the same time with regards to how they can effectively manage their liquidity."

Back in April 2015, Fitch Ratings published a report suggesting that if treasurers are not already looking at a policy review in this context, then they really should be. The report said that it is high time for "a proactive, strategic update of investment guidelines" and that corporate investors should give particular thought to future changes in cash management products and ratings coverage. "If the world of cash management is changing and the products that you are used to investing in are not available any more – or perhaps not available to the same degree – then flexibility with regard to the type of products that fit with your investment guidelines is important," Merritt explains.

The balance of yield versus liquidity versus the inevitable cost of carry that holding cash incurs is an unenviable task. It is thus the role of an appropriate investment policy, in the words of the UK's Association of Corporate Treasurers (ACT) Handbook, to "encapsulate how a company's risk appetite translates into practical objectives and rules." This appetite will be determined by a number of factors including the nature of the industry within which it operates, the strategic direction of the company itself and the resources available to manage risk (both in terms of skill and experience of its personnel, and its ability to absorb any losses).

Think again

There are three areas treasurers may wish to focus on when revising policy, says Hugo Parry-Wingfield, EMEA Head of Liquidity Product at HSBC Global Asset Management. First, as ratings agencies continue to review and in some cases downgrade banks, corporates should be thinking about whether polices do indeed remain 'fit for purpose'. "Companies should not simply adjust their criteria downward in response," says Parry-Wingfield, "rather there should be a deep analysis to decide whether they have the right – and sufficient – counterparties."

The second area for consideration is the investment products referenced in an investment policy. If the ability to place some short-term deposits with banks is becoming limited, then perhaps treasury needs to explore if other instruments are needed, such as MMFs or direct securities (see the section 'Trying something new', opposite).

Finally, in light of Basel III and the introduction of the LCR, corporates should also be thinking about how their investment policies define their liquidity profile. "The treasurer should now be reviewing what liquidity they really need to run the business. There is always an opportunity cost to holding too much liquidity but we believe that is going to be accentuated in the months to come," adds Parry-Wingfield.

As part of its Treasury Leadership series of videos, J.P. Morgan's 'Is Your Investment Policy Holding You Back?' provided viewers with some thoughts on structuring an appropriate investment policy. Jose Franco, J.P. Morgan Liquidity Solutions, EMEA Regional Executive, considered the realities of investing in the current environment, commenting that the negative rates seen in some European countries (and now Japan) means treasurers "could be breaching the company's investment policy as negative yield erodes capital".

The J.P. Morgan take on this situation is that treasurers can either adopt the view that, in time, interest rates will rise above zero (whilst realising that their current investment policy is not adequately structured to deal with a negative rate scenario) or alternatively, they can help re-write the investment policy to address the risks associated with these unusual market conditions. In the latter, the suggestion is to consider reducing reliance on overnight balances by extending the yield curve. This strategy, it advises (in concurrence with HSBC's Parry-Wingfield), must be balanced against liquidity requirements and risk appetite, since some businesses may feel that sacrificing liquidity will not compensate for a longer-term investment's potential returns.

The changing face of policy

The purpose of an investment policy has necessarily changed in recent times, notes Steve Baseby, Associate Policy and Technical Director, at the UK's ACT. The emphasis since 2008 has been more about return of capital than return on capital, and counterparty exposure management has risen to the fore. With the availability of funding now in question for some borrowers, he feels that policy will also tend to lean towards depositing surplus cash with relationship banks, "as a reward for offering credit facilities", although the demands of Basel III are making short-term cash deposits less attractive for banks.

And when it comes to steering policy in the right direction, Baseby notes a current tendency to be far more reactive. "Prior to the 2008 banking crisis, a treasury policy might have remained almost static for years on end; now there is usually a requirement to change it in the period between regular reviews." Often there will be provision for 'emergency changes' to be effected. With improved communication and awareness within business, counterparty exposure for cash holdings is something that he sees as "high on the list of things most executives and non-executives will monitor".

Aside from changes in the risk of target counterparties, bringing policy into line with current needs requires that a number of other key elements be considered when establishing or re-visiting an investment policy.

Treasurers are still thinking in terms of what can be done if they need to access their money quickly. Investment policy must dovetail into the liquidity requirements of the business and the evidence seems to be that most are sticking with simple deposits because they can build in fixed maturity dates, Baseby notes. In fact, in a very high turnover cash business, it is likely that most or all maturity dates will be short term, but for other business models, forecast accuracy is increasingly important as a means of determining investment strategy – there is after all a boardroom requirement to know that, should some event beyond treasury's control suddenly impact the business, it will not run out of money. "Forecasting used to be something that companies did on an approximate basis, on a weekly cycle, over the next quarter. Now it is done in much more detail."

For this reason, there is today more active oversight of where funds are, and why they are there. But how often should policy be inspected to keep investments relevant? "Investment policies are not supposed to be something that change every six months," says Jim Fuell, Head of Global Liquidity, EMEA at J.P. Morgan Asset Management. "They are broadly written, but with a level of constraint. Having said that, though, I think it is also important to build in some level of flexibility that allows you to navigate through some of the impending changes without necessarily having to go back to the board for further approval."

A general rule of thumb is that it should be revisited annually at least, but more often during times of market stress. Certainly a policy that never changes should be a thing of the past, but conversely there should be a wariness of over-analysis. One means of avoiding so-called analysis paralysis is to make accurate and timely data easily available in a format that avoids confusion.

Sitting on the dashboard: case study

Harvesting and presenting information to fulfil the high level needs of the board and the broad practical requirements of treasury is a function of advanced technology. The confluence of IT and investment policy is an approach taken by Dow Corning, a global leader in silicon-based technology and innovation. Its specific focus was counterparty risk management which had, by the company's own admission, historically fallen short of industry standards. The process had involved a considerable amount of manual monitoring, was primarily reactive versus proactive and was limited in scope: "Treasury realised that this approach was not acceptable," says John Coon, Global Treasury Manager, Dow Corning.

With thoughts of protecting its $2bn-plus in cash and investments from counterparty default to the fore, in 2014 Dow Corning created a Global Cash and Investments Committee. It consisted of a cross-functional team with members from Customer Financial Services (CFS) and Treasury. The team adopted a mission statement to "ensure that the risks associated with the company's global cash and investments are monitored and are made transparent, leading to best in class practices supporting our investment objectives as defined in the Dow Corning Corporation Investment Policy".

With this in mind, it set itself a number of practical goals including the implementation of a counterparty risk limit model, and the creation of a monitoring system in which risks could be quickly identified and remedied. The result – a Treasury Today Adam Smith Award 2015 Winner – was an internally developed risk limit model capable of aiding and checking the implementation of investment policy. This uses multiple independent sources of counterparty and default risk metrics including balance sheet health at bank-parent and subsidiary levels, as well as regulatory data such as Basel III risk ratios. Aggregated data is presented via a centralised "fully-automated one-stop-shop" dashboard for treasury. It enables easy daily monitoring of financial counterparties and provides a clearly defined escalation process when credit events occur. Functionality includes limit usage by financial institution (delivering real-time monitoring with alert notifications for breaches) and breakdowns of limit usage by cash type (for example bank accounts or time deposits). In addition, it provides background credit ratings information and credit default swap (CDS) activity for all counterparties.

Counterparty risk management solutions tend to use one or two sources of data to monitor risk. Dow Corning has developed a comprehensive limit model using in-house quantitative measures and credit risk metrics with real-time updates to a dashboard that incorporates supplementary sources including Bloomberg and Credit Risk Monitor. Coon explains that the overall process includes a "forward-looking, scalable model" to assess counterparty risk. It gives a 40% weighting for in-house quantitative measures using bank financial statements. Short and long-term credit ratings from multiple rating agencies are given a 25% weighting. Probability of default, calculated using a third-party tool with real-time market data, has a 25% weighting. The final 10% is made up of the Dow Corning Intangible index, incorporating a scale of bank service offerings and other relationship criteria.

"Like any risk management solution, it is difficult to place a figure on an event that you avoided by having the necessary safeguards in place," says Coon of the system's value to the company. "What we can say is that our ability to rest easier at night knowing our assets are allocated appropriately is worth a lot to us."

Trying something new

Whilst treasury should always adhere to policy, the generally changeable state of the market requires having the flexibility to respond in a timely manner to any cash or investment issue. It is therefore Baseby's view that companies should have an "escape valve" to use when investment for some justifiable reason cannot remain within those conditions. A treasurer may be granted power to step beyond policy in certain circumstances but usually an exception would be executed through the Finance Director, CFO or, if a major breach of policy is required, then by referral to either an internal committee of senior executives or the board.

Regardless of the difficulties that investing may present, dealing with lower-rated institutions and products is not inevitable in today's low/zero return environment. "Treasurers are beginning to find other ways of achieving security," notes Baseby. The repo (repurchase agreement) market is developing to enable short-term (usually three to six months) investors to mitigate counterparty risk by taking baskets of high quality securities (such as bonds or equities) in exchange for cash.

Repos are often perceived as difficult to administer by the inexperienced user: this is almost certainly criticism levelled at bi-lateral deals where a corporate must find a custodian, manage a complex contract and have valuation, settlement and variation margin capabilities. But as an antidote to such difficulties, tri-party repos are gaining ground. Here, an appointed collateral agent does most of the background work so that beyond fine-tuning the standard contract (the Global Master Repurchase Agreement or GMRA), establishing any policy restrictions and preferences, and issuing instructions to go to market, the operational involvement of the treasurer is minimised.

> "What we can say is that our ability to rest easier at night knowing our assets are allocated appropriately is worth a lot to us."
>
> John Coon, Global Treasury Manager, Dow Corning

Indeed, Baseby's observation is that this route into the repo market appears to be the favoured one for the corporate investor although, he adds that the agent may seek to manage a number of counterparties on behalf of its corporate client to make it worthwhile. In policy terms, this may be desirable anyway, as not only will treasurers feel more comfortable lending more to counterparties with covered cash than without, it also means they can lend against the quality of collateral, not the borrowing institution, and this in itself may generate more scope for deals.

This may even open up safe non-bank financial institutions as viable deposit counterparties – insurance companies and pension funds sitting on high quality securities from time to time need short-term cash. This could be a market to watch as a means of diversifying investments without degenerating credit quality. As long as there is full understanding of what is being done, and that it does not conflict with policy, then arguably any collateral is better than no collateral in risk management terms.

With treasurers in ever-closer engagement with the wider corporate finance function, it has placed them in the driving seat as far as preparing and acting on investment policy is concerned. An effective investment policy need not prevent a progressive approach to cash and liquidity so that it is entirely possible to reflect the dynamic landscape of regulatory reform, market volatility, and low, zero or even negative interest rates whilst providing sufficient headroom to add yet more value.

Unlocking the strategic potential of SSCs

Since the 1980's, businesses have looked to adopt a Shared Service Centre (SSC) model, in order to outsource their low value, high volume financial activities with the promise of reduced operating costs and improved efficiency and control. Whilst for many this has proved a success, progressive companies are realising that a SSC can be of strategic value to the business. Here Ricky Kaura, Managing Director – Head, Corporate Sales Asia Pacific at Standard Chartered Bank, outlines how greater value can be unlocked from a SSC.

It is undeniable that since the global financial crisis the role of the corporate treasury function has grown beyond its original brief to become more closely aligned with the business and operate as a true, value adding strategic partner. It could be argued however, that the evolution of the function has not only been facilitated by market realities, but also due, in part, to the fact, that for many companies the laborious low value, high volume activities such as payments and collections are now completed in a SSC – leaving the treasury free to focus on more strategic matters.

Whilst a successful strategy, there is a quiet revolution occurring in a number of progressive companies which are realising that a SSC can follow the lead taken by the treasury and offer even greater value to the business. For these companies, the SSC is no longer a low cost, process-driven function, but a centre of excellence driving process change from within and, in some cases, fundamentally changing the way the financial supply chain operates.

When carefully considered, the elevated position of the SSC makes sense. The centre has an intimate and holistic understanding of some of the most vital financial functions in the business, accounting for numerous key performance indicators. Its management team has likely developed a vast amount of knowledge around process optimisation and the various technological innovations that can enable this. And, overall, it probably has already proven that it can contribute materially to the commercial success of the enterprise – it is time to recognise this.

The SSC is increasingly a board level conversation, and its leadership team is beginning to form the 'holy trinity' of financial strategy with the CFO and treasurer, working together to drive change and offer value to the rest of the organisation. And for those businesses wondering where to start, it may be prudent to look at one of the most tangible and compelling areas where the 'trinity' can add value: improving the collections process.

A centre of efficiency

Cash collection objectives are straightforward: namely to collect payments quickly and cost-effectively, and reconcile these promptly and accurately against outstanding invoices. But, whilst a simple concept, implementation is fraught with difficulties. In particular, the diversity of collection instruments, both within each country and across regions, especially where there is a heavy reliance on cash, cheques and other local documentary instruments. This creates fragmentation and hampers efforts to standardise, accelerate and reduce the cost of collection. It also places an increased burden on the sales team in the field which has to focus its efforts on collections, rather than its core function, selling. As companies look for competitive advantage, the often underestimated burden and associated opportunity costs can be significant.

It is here that the SSC and treasury can begin to work together in order to resolve these issues and seek more efficient, ideally electronic, payment methods, particularly those that improve the predictability of collections, such as direct debits and increasingly mobile wallets where these are supported, with the latter growing at startling rates. Both functions have something to offer to this process: the treasury can evaluate the various markets, and utilise its understanding of the regulatory environment and the various challenges the sales teams are facing; the SSC can use its intimate knowledge and analytics of the collections process to evaluate how the new proposed methods of collection will impact the operation and make a recommendation based on this. In theory, and with close cooperation, the views can be married together and the best solution can be obtained, leveraging digitisation efforts and process re-engineering to drive optimal processes that facilitate reconciliation efforts.

One of India's leading direct to home (DTH) satellite service providers conducted a project similar to this in order to solve their growing collection challenges. In brief, sales teams were spending too long on collections, and traditional advance payment models limited the ability to set up innovative arrangements with channel partners.

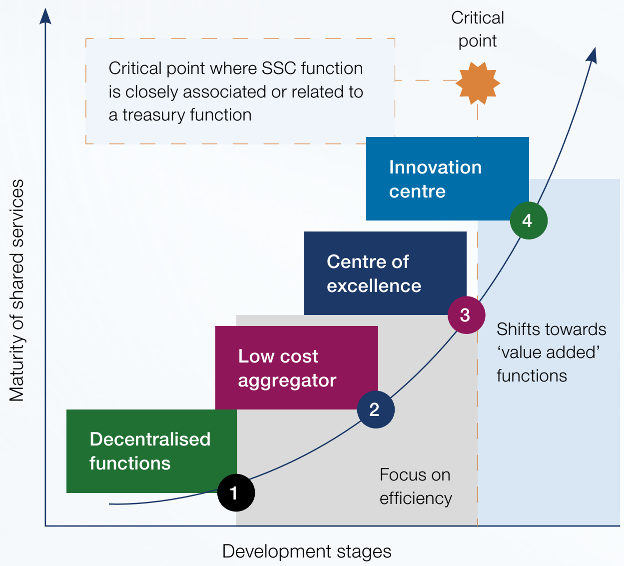
To resolve this, the treasury and SSC worked with Standard Chartered to implement a national ACH (automated clearing house) model with an innovative e-collection platform for same day collections, and supported the roll-out countrywide. This accelerated the collections clearing cycle from two to three days to same-day settlement, and allowed new mandates to take effect within a week, from 21 days under the previous arrangements, with automated confirmation.

In this example of how the treasury and SSC can work with a banking partner to offer greater value to the business, not only was working capital improved, but sales teams needed to spend far less time on collection activities, with far greater control over these processes.

A centre of information

A further area where a SSC can seek to add greater value to the overall enterprise's collections process is through working with the treasury to push for, and implement solutions that provide rich and structured payment information. This is crucial because in today's market environment, corporates of all sizes, and particularly those operating in emerging markets, are conscious of the risk of over-extending credit lines to customers in their sales networks. Most therefore monitor credit lines very tightly, and block new sales

Chart 1: SSC – stages of maturity



	Characteristics
4	● Innovation hub and R&D. ● Moving up the value-chain with role shifting towards advisory and control. ● More trend towards business partnering functions. ● Global process owner. ● Hybrid SCC function with treasury capabilities. ● Value creation versus cost reduction.
	Critical point
3	● Multi function shared services covering all transactional processes with all business units and locations supported. ● Centre of excellence with access to scalable talent. ● Outsourcing strategically used.
2	● Single function shared services covers most transactional processes with tactical on/offshore outsourcing. ● Most BUs and locations supported by shared services. ● Outsourcing tactically used.
1	● Decentralised functions with little central control over business support services. ● Outsourcing not used.

Source: KPMG and Standard Chartered Bank

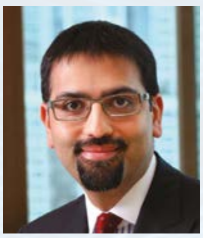
until collections have been posted to keep outstanding exposures under credit lines within acceptable levels. If a business does not have the ability to post collections promptly and accurately however, there can be a considerable impact on sales revenues and customer relationships.

Incoming payments therefore need to be supported with sufficient structured information to identify the payee and the invoice(s) to which the amount relates. This in turn facilitates sophisticated rule-based solutions for prompt, accurate reconciliation and posting to customer accounts. However, in Asia, obtaining rich, consistent information on incoming flows to facilitate this is challenging because of disparate payment methods and diverse payment formats across clearing systems, currencies and banks. Remittance information is therefore held in different fields within a payment instruction or advice, is of varying length and quality, and there is a risk that this data may be truncated or lost during the exchange of payment information as it passes through different clearing systems and banks.

To overcome this challenge, a growing number of companies are implementing virtual accounts, where each customer is provided with a unique account number for remitting funds, enabling them to identify individual customers. In these instances the accounts receivable teams that sit within the SSC can perform accurate, automated matching of payments to customers. This ensures that when the solution is tied with an automatic reconciliation solution that extracts files from a customer's ERP or accounts receivable system, reconciles open invoices with information captured from clearing systems using customised matching rules, before passing the reconciled invoices back to the accounts receivable ledger to update the customer accounts.

In doing this, the SSC has the ability to become the single source of truth within the company and to facilitate a clean line of communication to the credit teams regarding who can and cannot be extended further credit, thus potentially enabling further sales, fostering greater relationships with customers and perhaps giving the business a competitive advantage.

Moreover, in this instance, aside from the strategic value that the SSC can add, it is also able to improve on its more traditional metrics as there can be a reduction of external accounts, more efficient, cost-effective processes, enhanced working capital and the ability to access working capital finance programmes for further working capital improvement.



Ricky Kaura
Managing Director – Head, Corporate Sales Asia Pacific

Maximising the value of a SSC

By focusing on these two examples, the SSC, working in conjunction with the treasury department can go a long way towards adding value to the business. And today, thanks to the development of innovative technology, digitised optimal processes and solutions, this can be achieved more readily than ever before.

Building a SSC is a long-term strategic decision to support the business and deliver tangible value to the organisation. Ricky Kaura works closely with his teams who are actively involved in creating transformational approaches for clients, encompassing advanced solutions within their broad eco-systems. An area that Standard Chartered continues to lead within the Transaction Banking business, and an area of excellence for the bank. Kaura was previously with J.P. Morgan Chase & Co for over two decades, holding various business and functional executive roles, as well as being elected to the Asian Banker's "List of Leading Practitioners". He began his career at International Business Machines (IBM), General Electric (USA) and J.P. Morgan before joining Standard Chartered. For more insights on how Standard Chartered's award-winning teams can help your journey, email **ricky.kaura@sc.com**.

China: approaching the last mile

In recent years, China has taken great strides to reform its economy and liberalise the market and we are now arguably entering the final stages on this journey. In this article, a number of experts give their opinions on what they expect the future to hold for China both on a macro-level and also in terms of corporate treasury operations.

It was Chinese philosopher Laozi who said "a journey of a thousand miles begins with a single step," alluding to the fact that even the longest and most difficult ventures have to begin somewhere. For the Chinese economy this proverb has rung true in respect of its transition from a planned to a market orientated economy.

China took its first steps towards financial reform in the late 1970s through incremental economic reform that helped generate high growth, improve living standards and also eliminate supply shortages. Such was the success of these reforms that in 1993 China decided to abolish its planned economy altogether and fully chart a course towards a market driven economy.

The rest is history: China has become the world's second largest economy, a manufacturing hub, a mega trader, and overall a country with substantial economic and political might. However, we are now arguably beginning to enter the last mile of China's journey, and if the first step was tough, the last, if recent events are anything to go by, may be the toughest yet. And as China moves closer to the 'new normal', corporates, perhaps more than ever, need to keep a close eye on what is happening.

Boom or bust?

At the forefront of many business leaders' minds may be the economic health of the country. Much has been made of the slowing GDP growth, volatility in the stock markets, the debt-to-GDP ratio, as well as a host of other performance metrics that seek to provide insight into the well-being of the Chinese economy. Yet, as Gordon Orr, Senior Advisor at McKinsey states in a recent article: "In debates about whether growth is a percentage point up or down, we often lose sight of the absolute scale of China's economy." And as Orr goes on to point out: "China's economy is today made up of multiple sub-economies, each more than a trillion dollars in size. Some are booming, some declining. Some are globally competitive, others fit for the scrap heap. How you feel about China depends more than ever on the parts of the economy where you compete."

That being said, overall GDP growth remains a key focus in discussions around China, perhaps because even half a percentage point shift accounts for such a huge number in real terms and creates ripples that extend beyond its borders. The news therefore that in Q415 China's economy grew at its slowest pace in 25 years, at a rate of 6.8%, again brought up questions around if it is heading towards a hard landing.

For Kelvin Lau, Senior Economist at Standard Chartered, there is little need to worry about such an event primarily because, just as Orr alluded to, of the diversity of the economy. "Whilst we have seen a slowing in the GDP numbers, if you look at the month-by-month numbers we are beginning to see signs of it bottoming out," explains Lau. "If you take this one step further and begin to look at the individual parts of the economy, then of course there are some aspects that are struggling, but on the other hand there are many that are starting to bottom-out, like services and retail."

For Lau, this is to be expected and highlights the success that China is having in rebalancing the economy to one less reliant on areas such as investment, real-estate and manufacturing, to one driven by consumption and services. But China cannot be complacent, and to continue to strive towards its goals Lau argues that further policy easing is required. "This should be monetary easing in terms of reserve requirement ratio (RRR) cuts and on the fiscal side the government should look at tax cuts and fast tracking key infrastructure projects." Overall his message is positive. "Over the next five years we expect to see China deliver 6.5% growth – enough to meet the ambitions to double the size of the economy outlined in 2010 – this is a long way away from a hard landing."

That being said, this isn't a view shared by all. For some the risk of a hard landing is still very real. "The risk has not diminished and is, in our view, increasing," says Chris Leung, Executive Director Group Research at DBS. "The reason being that many structural problems, such as overcapacity and resource allocation, remain unresolved and are deepening."

Despite this view, there is hope that this can be avoided. "There is an increasing popularity of supply side economics within the Chinese government," explains Leung. "This shuns short-term demand-side stimulus. Rather, it emphasises tax reduction, deregulation, and innovation to sustain long-term economic growth. Although these steps are positive there is still plenty of work to be done. For instance, allowing non-performing loans to surface to enable the banking sector to function normally, allowing the exchange rate to shoulder some of the pressure, moving ahead with state owned enterprise (SOE) reforms and quicken service sector deregulation."

Although many have accepted numerous aspects of China's 'new normal' there may be less understanding that policy responses from the Chinese government are also changing. This change in thinking was encapsulated by the remarks made by Chinese Premier Li Keqiang, who in January stated that market forces will play a role in solving many of the structural issues in China, including leaving those businesses which are unable to compete to die out – a marked policy change from previous years where the government would typically intervene.

Overall, whether China is heading for a hard landing or not comes down to a matter of perspective, but what might be more important for corporates in the short term is adjusting to China's change in macro management philosophy. "Those who don't will be caught off guard," stresses Leung.

The road to reserve

On 11th August last year, many market participants were caught by surprise by China's sudden devaluation of the RMB – the biggest in two decades. The 1.9% downward move by the central bank sent shockwaves through financial markets and shone a spotlight on the Chinese economy, which some market commentators argued was perhaps weaker than the numbers let on.

Yet, despite recent bumps in the road, China's strategy around its currency, and in particular its ambition of making the RMB globally recognised, can largely be seen as a success. Significant work has been done by the Chinese government to promote the currency and make it easier to use on and offshore. This includes the creation of RMB hubs in various countries around the world, improvements in infrastructure through the creation of CIPS, and regulatory relaxation, in particular the ability to pool and sweep the currency cross-border. The result according to Lum Yin Fong, Managing Director Global Transaction Services at DBS is a greater usage of RMB by corporates. "We have definitely seen an increase in the use of RMB as a payment currency and in trade," she says. "In fact, recent SWIFT data shows that the RMB has surpassed the Japanes yen to be the fourth most used payment currency, it is also the second most used currency for trade transactions. Now with the recent announcement that RMB is being added to the SDR basket of currencies we expect an increase in RMB usage, not just in trade, but in other areas as well."

It is not only China that has been on a journey in regards to the RMB. Corporates with operations in, and even outside the country, have also been closely tracking the currency's rise. "When China first began to liberalise its economy the concept of using RMB as a functional currency sounded interesting to many of our clients, but for the most part few of these had any need to use the currency outside of China," says Sridhar Kanthadai, Regional Head, Transaction Banking, Greater China & North Asia at Standard Chartered. "Yet in recent years, more and more corporates have been asking us about the RMB and how it can be used and managed both on and offshore."

Indeed, many of these conversations have been with Chinese corporates, for which the RMB is their natural currency. But, Kanthadai has also been having many conversations with multinationals around adopting the RMB as a treasury currency. "Many Asian companies that don't have a bias towards the US dollar are looking at the RMB as an alternative option, as are some European companies," he says. "US companies, as you may expect, are a little slower but the pace is beginning to build."

A bright future?

Moving forward, it would be hard to argue that the RMB will not continue to gain in popularity amongst corporates around the world. "If you look at the proliferation of offshore clearing centres, the access to liquidity, the deepening of the financial markets – FX, hedging products, investment products, dim-sum bonds – I think the market has developed to a point that it can be considered a broadly usable currency not just in China but also in trade with China," adds Kanthadai.

That being said, China hasn't yet reached the finish line and there remains lots of work to be done. As Miguel Otero-Iglesias of the Elcano Royal Institute highlighted in an op-ed for the Financial Times, the currency only represents around 1% global reserve assets and is eighth in terms of international bond issuance and ninth in global currency trading. And whilst the numbers on the trade side look impressive, 80% of RMB trade is conducted with Hong Kong and as he states: "Perhaps more importantly, in most international trade contracts the RMB is the medium of exchange and not the unit of account. In other words, the Chinese currency is the means of payment, while the dollar remains the invoice currency, which is much more important because that is where the exchange rate risk lies."

Otero-Iglesias goes on to say that perhaps the main reason for these less than impressive figures is down to confidence and the fact that China still highly regulates the capital account and conversion of its currency. A nod is also made to the lack of transparency around its political and legal frameworks.

If confidence was already limited then the recent bouts of currency volatility, beginning on 11th August 2015, may have spooked people further. But, for Kanthadai, it should be seen as an opportunity to begin looking at the RMB as a market based currency that will continue to face two-way volatility. "China can, and will continue to, promote the currency through infrastructure developments and policy changes, but for confidence to really be installed in the RMB it needs to be seen in a different light, akin to other major currencies."

Spreading its wings

A potential key driver in both the RMB's continued assent and the overall fortunes of the Chinese economy is the government's belt and road initiative. The strategy looks to reawaken the historical routes used by silk traders between China and neighbouring countries on three continents, and export China Inc. to the rest of the world on a massive scale.

It is a complex, multi-faceted and highly ambitious project and as yet hasn't been fully outlined by the Chinese rule makers. It is therefore unsurprising that some commentators are cautious about its overall ambitions, with some going as far to say that we are entering a period of Chinese hegemony. Some argue on the contrary. As Xu Sitao, Chief Economist at Deloitte China points out: "Contrary to conventional wisdom, China's belt and road initiative is neither a scheme to export China's excess capacity south and west, nor a grand scheme to exert geopolitical control over the regions concerned. Quite simply, it is an effort to boost regional connectivity in ways that would help China manage certain domestic economic challenges. If China can do this while exporting its growth model to partner countries, the initiative could be considered a success."

Although the overall ambitions seem opaque, one area that does seem clear and that corporates certainly will be paying attention to is the role that the belt and road initiative can have in boosting the use of the RMB. For DBS's Leung, it may have particular significance: "To finance infrastructure spending, Beijing is encouraging Chinese banks to extend credit to project participants – most likely in the Chinese currency." Moreover, the strategy also looks to boost China's overseas direct investment. "Recipient countries would use RMB to purchase capital goods, construction materials and services from the mainland. The circular nature of these flows will further raise RMB settlement for China's exports. Closer trade and business ties with China would increase regional demand for the RMB."

Whilst in its nascent stages of development, the belt and road initiative seems to be having some impact already. Recent research from merchant bank Grison's Peak highlights that outbound policy loans, equity investments and M&A activity has reached its highest levels in seven years. Yet, the path ahead may be a difficult one, especially for those companies that have had little experience operating outside of their home markets.

A much improved treasury environment

As many Western corporates will testify to, moving out of your home market and into unfamiliar waters creates many challenges, especially around achieving standardised processes. This challenge is amplified in the treasury department, which has to adhere to the differing regulatory regimes as the business moves from country to country.

For nearly two decades it was China that caused a headache for international treasurers, with its tight regulatory regime and opaque internal mechanisms. Yet steps taken by the government in recent years have certainly improved things, with treasurers afforded more freedom to manage their cash and liquidity, both onshore and cross-border. Achieving standardisation, best practice and integrating China into global treasury operations is starting to become a reality.

"The relaxation of many rules and regulations has enabled our corporate clients to strive towards centralising and standardising their processes," says Yigen Pei, China Country Head, Treasury and Trade Solutions at Citi. "As a result corporates are frequently coming to us and asking what they can do and how they can look to implement solutions such as shared service centres, cross-border pooling structures, payment on behalf of (POBO) and receivables on behalf of (ROBO)."

Things look set to further improve given the recent moves by the Chinese regulators to free up interest rates. For corporates, investing in China has therefore become more like investing in other parts of the world. This should also enable corporates access to cheaper and more flexible funding options. Moreover, in levelling the banking playing field DBS's Lum believes that corporates will be afforded even greater access to best-in-class products and services. "Corporates will gain from having more options, banks will need to innovative in order to stay competitive and support their customers."

Although treasurers in China are now operating in a greatly improved environment, there remains a need to pay attention to the changing regulatory environment. "Whenever you operate in a foreign market you have to adapt to the local context," says Pei. "In China, the regulations are changing so quickly that it is important to stay close to them in order to know what you can and cannot do. This also gives you a chance to be part of new regulation formation as they are being developed." Many companies have successfully demonstrated the benefits of this approach including Adam Smith Award Winners Intertek and BASF.

Yet, despite all these improvements, the last mile is often the hardest. Treasurers across the board will hope that recent issues such as restrictions on liquidity management, imposed limits on FX transactions and government induced volatility are unintended consequences or necessary evils of China's rapid development and not the beginning of a new set of challenges to contend with. One thing is for sure, the world, and in particular the world of corporate treasury, will be watching China's next steps with a keen eye.

The fine art of corporate finance

Pratibha Advani
Chief Financial Officer TATA COMMUNICATIONS

With more than two decades of experience in corporate finance, Pratibha Advani has built a reputation for knowing exactly what is required to take a company forward. Her most recent role, as CFO for a global telecommunications company with Indian roots, is a challenge she relishes and one which allows her to exercise her creative impulses to their fullest extent.

Tata Communications is a global business headquartered in Mumbai and Singapore. The $3.2bn listed company owns more than 210,000 kilometres of terrestrial fibre and claims the world's largest wholly-owned submarine fibre network, formed of more than 500,000 kilometres of subsea fibre. Its vast infrastructure means almost 25% of the world's internet routes are on Tata Communications' network, and around 70% of the world's mobile network operators use its services.

The idea that artistic minds cannot or will not flourish in the commercial world is one perpetuated by the romantic notion that impoverishment somehow unleashes true originality. However, despite many great artists throughout history claiming destitution, the creative muse can and does find its expression in the business environment. And when the vision of imaginative individuals are channelled towards commercial endeavour the results can be exceptional.

As CFO at Tata Communications, Pratibha Advani is responsible for its strategic financial management. She is also a talented artist with a creative style that finds its expression in many different ways, not least through her approach to her responsibilities with this $3.2bn listed high-tech and telecommunications company.

With over two decades of experience ranging from financial strategy, project financing, M&A, risk management, and legal and secretarial, Advani has had plenty of opportunity to develop her creative methodology. But on her own admission, she entered the world of commerce "by pure default". Although she felt a natural inclination towards artistic expression she recalls that whilst still at school her introduction to business as a study area was taken as a challenge – of which she proved more than capable of rising to. Following her foundational success she gained a Bachelor of Commerce (Honours) degree before engaging with professional accountancy exams. "It was still by default that I became a chartered accountant and then stepped into the world of corporate finance," she recalls.

Art into business does go

Arguably Advani was moving ever further from her artistic aspirations, but with the progressive development of her creative approach to business she feels this was not the case at all. In fact, as her career advanced, she soon realised that "creativity knows no limits". Corporate finance provided her with a stimulating exposure to a broad range of commercial issues, at times offering fascinating insights into a variety of businesses and sectors in which the imaginative individual can explore new models and methods as they seek to transform functions and whole organisations.

Driven by the knowledge that imagination can be applied in every function, Advani quickly moved up the ranks to become CFO & VP of Finance at GE – SBI Cards, and later at Barclays Shared Services in India. A similar high-ranking role followed as CFO at NIIT Technologies where she led the global Finance, Secretarial, Compliance, Regulatory, Legal and Investor Relations functions. In May 2015 the call came to join Tata Communications as CFO, "finishing work one night at NIIT Technologies and the next morning taking up the post with Tata Communications".

CFO: a new meaning

The acronym CFO is well-understood to mean Chief Financial Officer but this is not enough for Advani. She sees the role as having evolved over time into that of the Chief Facilitation Officer. "It requires one to be an effective organisation leader, balancing the responsibilities of stewardship with those of business partnerships," she explains. In the high-tech communications sector, the challenge is to "act as a catalyst, promoting new ideas, sowing the seeds of innovation and improvisation, and driving productivity and efficiency within the organisation while also pursuing growth within a highly regulated environment".

In reality, the rules and regulations faced by all those operating in the tightly controlled communications sector are not a source of frustration for Advani, even if she admits they can slow progress sometimes until "realignment to the changes" is effected. "As CFOs we have to make the organisation both commercially and compliance-savvy. Once this foundation has been laid, it is not so difficult," she reports. Her ultimate objective is to ensure "sustained growth with profit maximisation within these constraints, alongside wealth creation for the stakeholders". This understanding is cascaded down to all those in her finance team.

Keep learning

In the "all-encompassing" role of the CFO, the need is to keep one eye on "just about everything". Every transaction in some form or another has a monetary impact so that "like it or not, you do get involved". From this standpoint, Advani sees her position as both challenging and fulfilling. But it has been a conscious career decision to move across various industries as part of her mission to absorb as much information and knowledge as possible. She has had the "good fortune" to work in manufacturing, hospitality, retail, various financial services, IT and now telecom as she continues to satisfy her quest. The fact that she initially saw both IT and telecoms sectors as "too complex for a creative person like me" but entered both nonetheless is testament to her sustained willingness to take on a challenge and "continuously be high on the learning curve". But keeping cutting edge businesses ahead of the game is just the kind of creative challenge upon which the artist within her thrives.

Despite her initial misgivings, Advani's immersion into the world of technology has clearly now extended her appreciation of its value to the decision-making process of corporate financial operations. She recognises that it underpins "nearly every industry and business process today", improving efficiency and helping more informed, timely and correct judgements. "The integration of systems is critical for the success of any enterprise; if the back end and front end do not communicate and allow seamless movement of data it could be an operational nightmare for any industry player."

The high-tech challenge

Tata Communications is at the heart of an industry that is unavoidably high on investment but long on payback cycles, notes Advani. "The way that the industry is transforming today brings a strong flavour of IT services, which is currently unregulated, so that within this sector a business must try to balance opposing demands," she comments. "For Tata Communications there is a need to balance the needs of a 'bricks and mortar' company, with all the essential investments in infrastructure we must make, coupled with the 'start-up' mentality we adopt as we open up new opportunities around the world."

The fact that this balancing act takes place against a backdrop of global financial volatility adds to the pressure. "We have to have the ability to raise capital at highly competitive rates and at the same time satisfy the complex regulatory and tax environment across the world [Tata Communications has around 45 subsidiaries globally]. We also have a very diverse range of customers: we really are sleeping with the enemy, working with other telcos and businesses across the wide spectrum of the industry, and this requires us to develop bespoke pricing models – this is a highly price-sensitive industry which also obliges us to continuously find a balance between chasing volumes and maintaining profitability."

Few companies have been insulated from current financial volatility and Tata Communications is no different. But its global presence as a communications business is "both a challenge and a boon for us", notes Advani. Market shifts can cause short-term disruption but they also provide opportunities. "If one particular market stops firing we have the fall-back option of focusing on our growth markets," she explains. As its mature markets had been tapering or remaining steady, it found opportunity in EMEA and APAC. And with a behavioural shift towards data usage putting pressure on its "bread and butter" voice business in terms of volume drop and pricing pressure, it has been able to leverage huge opportunities in data services, especially with the rise of 'superpower' tech businesses such as Google, Amazon and Netflix.

This awareness of and response to market changes is something very much in the remit of the CFO as the need arises to optimise resources across all capital investments. In addition to continually balancing investment in innovative ideas with the upkeep and development of essential investments in its fibre network, Advani explains that she also has to take tough decisions on timing when pulling the plug on ideas and investments that are not delivering the right return. The latter, she explains, is one of her biggest challenges but points out that facilitating and enabling growth is critical. Getting this right necessarily involves finance partnering with its business colleagues.

Building relationships

The relationship between the office of the CFO and the rest of the business may have moments of tension but the management of the financial process requires "discipline, governance and rigorous evaluation", says Advani. She is a strong believer in partnering and collaboration: "It is not individuals that win but teams." Whilst at times tough decisions are taken which may impact people in other functions, she is adamant that actions are taken in the interests of the organisation and that these must align to the corporate strategy and the vision. "I think if you communicate – and there is no such thing as over-communication – you are transparent, if you can show that there are no hidden agendas, then coming to a consensus is not too difficult." And by listening to the collective worries of colleagues and accepting their diverse viewpoints, a far more robust organisation is built.

As a firm believer in the importance of human relationships in business, Advani advocates respect for others. The development of the so-called soft skills – including empathy and sensitivity, communication and presentation skills – are thus a "prerequisite" for every professional. "More so for finance people," she adds. "Given the nature of our role, we are required to take tough decisions and implement them. I think that if an idea or decision can be socialised, that is the first step to opening the minds of people to something new." She continues: "We cannot just be number-crunchers; we should also be able to communicate the logic behind those numbers. Today's finance professionals are not like old-fashioned bean counters – we have a much more proactive role to play as business partners in drafting and implementing business strategy."

The proactive role extends to managing external stakeholders and investors, and unless the right soft skills are in place, maintenance of such relationships can be difficult. "I am a believer in the measurement of RoE – Return on Equity – in business," says Advani. "But when it comes to people, you have to modify RoE to read 'Return on Ego' – and that means respecting the voice of another individual."

Bank catch-up

This is a two-way street of course. One of the external partners for the finance function is the banking community. Some of the criticism levelled at it in recent time is not unfounded, says Advani. The global economy has and still is paying heavily for mistakes made, but even though there are more compliance and governance layers, increased focus on risk, the stripping out of non-core businesses and so on, she feels that bank/corporate relationships generally continue to be supportive. "At Tata Communications we do enjoy a very supportive relationship with our global banking partners but in talking to my counterparts across a wide spectrum of industries, the sentiment is that banks behaved in a somewhat knee-jerk fashion, suddenly starving long-gestation capital intensive projects from funding. This puts those businesses in a Catch-22 situation." Both banks and corporates need to work closely to secure funding for these stalled projects; this will be the biggest catalyst for reviving growth, at least in India, she feels. "A very myopic, distressed-asset focused view from banks will not be able to untangle these complex webs."

Banks need new ideas but their level of creativity is in catch-up mode right now, notes Advani who suggests that most innovations are actually coming from new non-bank market entrants (in Europe the PSD2 regulation has paved the way for many new payments service providers). Whilst the tightening of the regulatory environment means banks are constrained in being able to deliver more innovative and imaginative products she stops short of offering her sympathy but feels many have become so risk-averse that infrastructure projects requiring finance are not being supported. "They have to find a balance between turning on the tap and being conservative."

Don't worry, be happy

Although at an earlier point in her career Advani did find aspects of the job that concerned her, she recalls the day when her CEO questioned the value of worrying and losing sleep. "That was the day I realised that there will always be issues and challenges and that we have to learn to deal with them." It worked for her. "Nothing keeps me awake at night now," she states. In fact, she sees challenge as a force for good, arguing that if there were no challenges there would be no creativity. "Risk remains an integral part of conducting any business; we need to be aware of it and work on our mitigation plans but at the same time be aware that we cannot be in control of each and every situation – the world is dynamic and we have to play along."

This forms part of her advice for anyone plotting a career trajectory that takes a path through the world of corporate finance. That journey, insists Advani, must be underpinned by self-belief and by a sense of ownership of what you do. In achieving this state of mind, she believes the individual will never feel "that they are just doing a job".

Of course, for someone with a balanced approach to her career, Advani places a strong emphasis on what she calls "me time". She loves to paint and write poetry and is a self-proclaimed "fitness freak". If the world of finance had not been offered up as challenge at the start of her career, perchance, inspired by her love of colour and artistic design, she feels she might have achieved great things as a textile designer. Even today she makes time for her local community of artisans and weavers, attending exhibitions around Delhi and curating her unique collection of fabrics. But just maybe, with the inspiration, curiosity and imagination she brings to bear on her work as CFO, Advani is already weaving her skills as an artist into a calling that is perhaps not so different after all.

Women in Treasury Asia Forum

Thursday 14th April 2016

The South Beach, Singapore

We are delighted that Pratibha Advani is one of our four industry panellists at our Women in Treasury Asia Forum in Singapore. To find out more about participating in this key industry event, please contact Lisa Bigley, Global Head of Events **lisa.bigley@treasurytoday.com**

Over-supply and demand: living through an asset rout

Commodities pricing is at the mercy of a number of factors as diverse as market mood, political intervention and the weather. For corporates, managing the risk of price swings is crucial to protect the bottom line. Where does risk materialise, why, and how can it be mitigated?

Commodities such as gold and oil have, for a long time, proven to be a rich seam of literary inspiration as the quote, "there's gold in them thar hills – and there's millions in it," from Mark Twain character, Mulberry Sellers, attests. But in today's volatile markets, they can also be a source of great consternation for corporate end-users.

Commodities are the key elements used in just about every production facility the world over. As raw materials, commodities will either be soft (agricultural products such as wheat, coffee, cocoa or sugar) or hard (mined or extracted products such as iron ore, copper, gold or oil). Although traded in the primary economic sector (as opposed to the manufactured), they still appear to have a life of their own. Indeed, from a financial perspective, the purchase and sale is often carried out using futures contracts through the 50 or so specialist regulated commodity exchanges around the world – in Asia the list includes the likes of Central Japan Commodity Exchange, the Vietnam Commodity Exchange, the Hong Kong Mercantile Exchange and the Australian Securities Exchange. Derivatives of futures are also increasingly traded using spot prices, forwards, futures, and options.

All commodities exchanges operate to a standardised quantity and minimum quality (the basis grade) of the commodity being traded. This helps to satisfy the sale so that in effect, the commodity is pretty much the same wherever it is bought. The problem with commodities traded in this way (and in this quantity) is that price can be very easily affected by political and regulatory change, seasonal variation, weather, technology and general market conditions (including supply and demand). All of this, for the commodity-exposed corporate, translates into risk which must be managed.

And at the moment, there is much to consider as the commodities markets demonstrate just how fragile they are.

According to a December 2015 edition of the BondSquad 'Making Sense' newsletter, commodity prices have been "beaten down" for more than a year and for the past several months conditions have "deteriorated dramatically". As with most asset routes, the crash in commodity prices started with the fundamentals, said the report's author, Tom Byrne. These include lower-than-expected demand (or demand growth) and significant over-supply of many commodities. Oil is a case in point as the over-production war between OPEC and the US rages on, but other commodities have been impacted too as production capacity had been massively expanded to feed Chinese and EM market growth that has stalled, leaving the world in a state of glut. For buyers, this seems like a good thing, but it is not as simple as that.

The regional view of a rollercoaster ride

Asia Pacific is a major source of global commodity exports. The UN Economic and Social Commission for Asia and the Pacific (ESCAP) Trade Insights paper issued in Q2 2015 reported that regional economies currently accounted for 38% of global mineral and metal exports, as well as 29% of global fuel exports. Asia Pacific harbours many commodity-exporting economies, accounting for over a quarter of global fuel and metal exports, as well as over a third of global mineral exports. Some countries in the region play a significant part in global commodities production, with Australia, for example, producing 28% of global mineral supplies. The extent to which extraction and trade of commodities forms part of some economies means that if markets fall they can have a serious impact on local economies – there are 18 net commodity-exporters in the region, with commodity-trade surpluses ranging from 0.11% of GDP in Myanmar to 59% of GDP in Brunei Darussalam. When prices slump, ESCAP notes that export revenues and economic growth can expect negative impact in these countries.

At a macro level there is cause for concern as some international commodity prices continue to fall. In August 2014, oil stood at $115 a barrel but prices settled under $37 a barrel (the first time since the financial crisis) after data from the OPEC reported in mid-December 2015 that the group increased its crude production in November. Furthermore, recent stock market falls are perhaps based on the pain likely to be felt by oil producing countries and the companies that sell to them (luxury goods and car manufacturers remain on edge).

ESCAP reported on continuing falls of many commodity prices (from June 2014 to January 2015) which extended across all commodity sectors in the region. Energy saw a 50% decline, metals and minerals a 16% decline and agriculture a 7% decline. In the energy sector, oil and gas prices fell between 37% and 54%. In the minerals and metals markets, coal, copper, lead and tin prices fell between 12% and 24%, while iron ore prices plunged 47%. In the agricultural sector, corn, cotton, palm oil, and soybean prices also fell between 12% and 26%. However, the prices of some commodities actually increased. Zinc, aluminium and nickel prices increased in the period due to export bans and supply-side issues, whilst orange, cocoa, cattle and coffee prices rose, due to crop failures and poor weather.

Metal market mayhem

A business using base metals will need a certain amount of raw material on its factory floor at any given time. The nature of the business and its prevailing business model will inform the precise stock level, according to whether it needs to hold substantial inventory or if it can take delivery just-in-time. Of course, high volatility brings great opportunity to those corporates heavily exposed to such metals if they are in a position to lock in record-low prices now through a derivatives strategy enabling future gain. On the other hand, those with a large unhedged inventory have a challenge on their hands: not only does forecasting become difficult, but also a price crash could be seriously damaging to their balance sheet.

This volatility underscores the importance of taking a proactive approach to commodity trading and risk management for corporates. Today we are seeing a 'what-if' scenario made real as base metals head out on a wild rollercoaster ride, with iron ore prices plummeting to 2009 levels and copper also sinking to its lowest level in six years. What's interesting about the dramatic fall in the copper price is that it was triggered by a seemingly unrelated factor – problems in the Chinese equities market where in August 2015 it very nearly saw the biggest possible decline.

Although the metals market can exhibit periods of relative stability, with steady rises or falls, prices tend to be more generally mobile compared to other asset classes, with rapid movements often being driven by major economic events or even just talk of an event. In the past, the main market players, apart from a small group of speculators who created the liquidity, were the mines, the processors and the end-users. Whilst the industrial supply and demand of metals changes little from one period to the next, even more volatility has been introduced because metals started to gain traction as investment products for fund managers, ETFs and macro-economic hedge funds, many of whom are now trying to bail out.

The current level of movement is therefore not likely to be just a blip that can be ridden out by commodity-exposed firms. As investors are becoming more sophisticated in terms of the investments they make, they are still looking at metals and other commodities as an asset class, albeit a bumpy one. And as long as this pattern of behaviour exists (and OPEC and the US producers slug it out over oil), there will be spikes of volatility in the market and these spikes will impact the industrials as they go about their day-to-day business. There is thus increased urgency for treasurers in these organisations to mitigate risk. Hedging against price volatility is a common response but the decision to hedge is far from simple.

Measure and analyse

The simple spreadsheet is still the technology of choice for some businesses when managing their commodities deals. Unsurprisingly, this is becoming less of a practical proposition as volatility, compliance issues, regulatory reporting and market complexity reigns. Indeed, it is becoming increasingly necessary for treasurers to analyse what happens to their portfolio of commodities contracts as market prices rise or fall and they need to correlate this information with the downstream effects on functions such as production and sales in terms of cash and planning. But whilst it is important to understand the 'here and now', it is advisable also to evaluate a number of what-if scenarios, to stress-test all assumptions about pricing and risk and create optimal hedging strategies for a number of outcomes.

The need is to be able to see what the production plans are, what the requirement is for components for these plans, what is held on inventory, what the forward commitments are in terms of those components, and what has to be purchased. As this is being calculated, it will be necessary to assess the effects on the overall position of assumed price, currency and interest rate changes over that period. Armed with this information it will be possible to create different hedging strategies based on these scenarios actually playing out.

From a treasury perspective, gaining insight into the real exposures and risks of multiple contracts for different commodities across all regions could be a major challenge. If a particular exposure cannot be fully rolled up across the group, there is a chance that inefficient hedges will be placed. Treasury is also faced with the challenge around understanding and gaining visibility to the sub-components of physical purchases and their embedded risk. Without an ongoing appreciation and understanding of the organisation's positions in relation to market conditions, it is possible that hedging policy becomes stale very quickly. The goal surely is to protect the downside so that if prices move against the organisation, it already has an appropriate hedge in place. But hedging by region, plant or even by individual trade simply because the bigger picture is not available will be more expensive than leveraging a consolidated global position, particularly if those hedges are placed individually with banks or brokers.

An accurate and timely view of commodity inventory, current forward purchases and exposures across the business, can facilitate more accurate tracking not only of the pricing of each deal but also of how effective existing hedges are. The challenge is being able to handle all the physical commodities contracts, with their underlying sub-components (such as basis, freight and grades) and combine that information with the financial hedges. Being able to report this view inside treasury will give the treasurer better insight to their overall risks and underlying cash flows. Having this information means that as prices move, the decision to exercise any options, for example, becomes that much clearer. To this end, a number of trading and risk management solutions are available from vendors such as OpenLink, Reval, Thomson Reuters, SunGard or Triple Point. Again, there is a cost and another layer of complexity to consider but these have all been tried and tested using years of best practice and market knowledge; the business case for in-house development and maintenance may not withstand close scrutiny in this light and in any case having all commodities and treasury functions on a single platform is an advantage.

With a fuller appreciation of commodity positions – calling upon data from purchase contracts, production requirements, procurement needs and sales forecasts – comes the opportunity to engage with more sophisticated (and thus effective) hedging tools (beyond simple futures and options). Being able to understand and isolate the component risk of non-financial items (now permissible under IFRS 9 Hedge Accounting rules) for example, is potentially far more effective and efficient: an airline's jet fuel trades may only need hedging of the crude oil component. Of course, where a non-US airline or other business is hedging in USD (because that is how oil and many other commodities are priced) as USD strengthens, so the embedded currency risk of the deal fortifies; this is another consideration for treasury.

The sustainable model of production

Despite the current slow-down in countries such as China, continued economic growth in emerging markets has driven demand for resource. This contributes to higher and more volatile commodity prices. The projected growth for steel consumption between 2010 and 2030 has been reported as high as 80%, with the demand for energy set to increase in the same period by 33%.

Manufacturers can create value, cut costs, and reduce exposure to volatile commodity prices by improving their resource productivity, according to McKinsey & Company. The concept it espouses effectively means using fewer resources for each unit of output. In the spirit of sustainability and corporate responsibility initiatives, collaboration with suppliers and customers "can keep used products, components and materials in circulation". Rather than engaging in the traditional supply chain, which creates a linear relationship between stakeholders, McKinsey refers to a business model that requires rethinking ownership of materials in terms of a "supply circle". This proposes the regeneration of natural assets through repair, maintenance or recycling of materials or products at every stage of production, across the full supply circle.

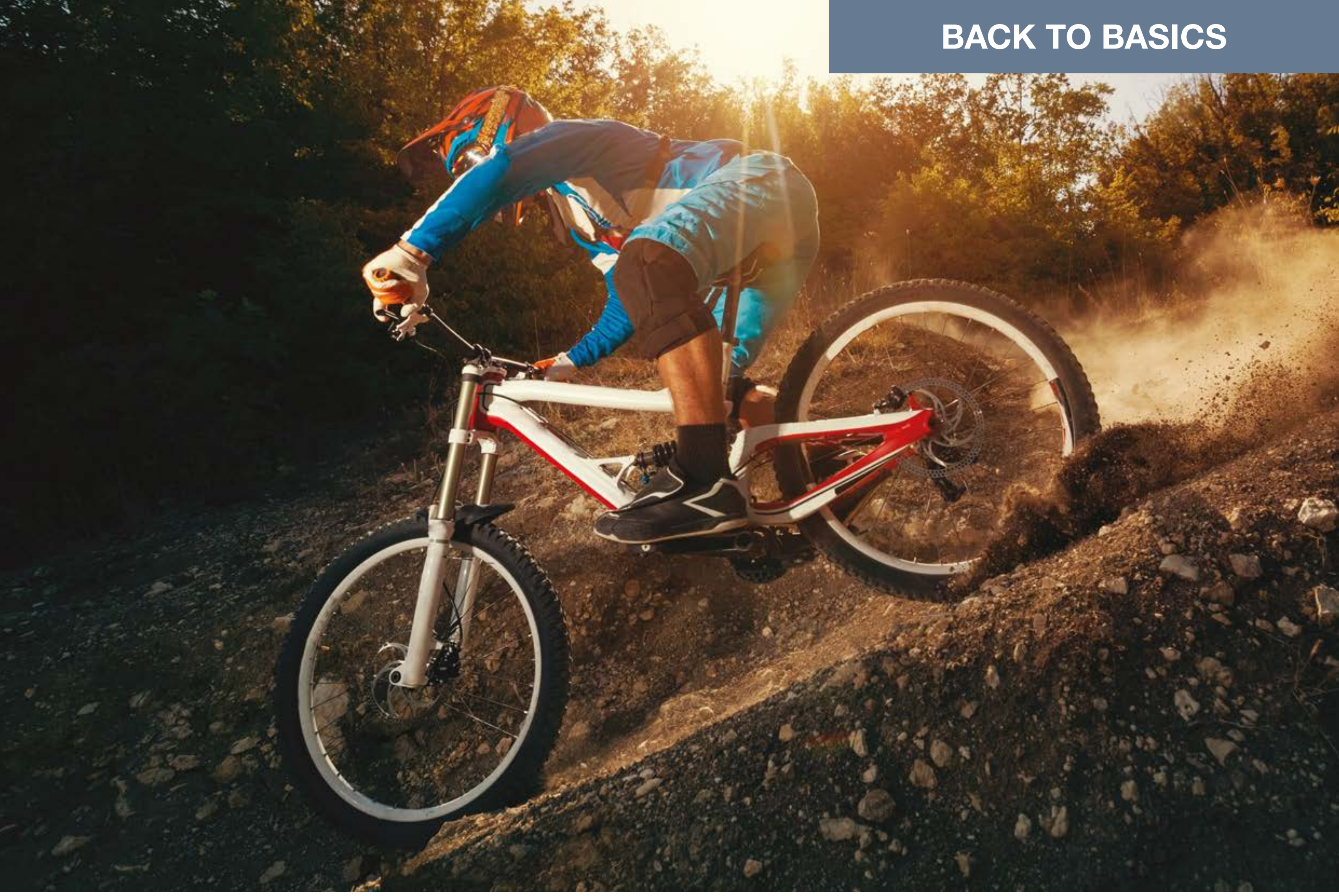
At the core of this effort is a need to analyse how raw materials are extracted, how components are produced, how products are designed and how return (recycling) markets are organised. McKinsey suggests that large companies can start to exercise influence in the supply circle where previously it would have no direct control.

There is a cost. McKinsey warns that without digital supply chain management, it will be almost impossible to co-ordinate all the moving parts a circular supply chain requires in real-time. There may be a need to consider a new business model, where producers lease rather than sell in order to retain ownership of materials embedded in products (the automotive industry could adapt in this way). There may even be a requirement to rework the cash flow demands of a circular supply chain, compared to a linear one, and although margins might improve, the suppliers' need for cash may change which will need addressing.

Take a decision

The prices of commodities have generally fallen in recent years but this situation will not last forever. Some businesses are better prepared for change than others. In 2008, Southwest Airlines in the US took the decision to lock in the price for about 70% of its jet fuel based on oil at $51 per barrel. For 2009, it locked in 55% of its jet fuel based on that same price, and its strong financial position allowed it to continue to lock in fuel prices over the next few years. Many did not understand this move at the time, but as oil went to $100 and beyond, Southwest's strong financial position allowed it to turn a profit when most others were reporting losses.

For corporates in Asia, managing commodity risk and any imbedded currency risk is now an essential part of the job: taking a proactive stance at the right time can – as Southwest demonstrated – make all the difference. In essence, real-time visibility of commodities trade allows treasury to become a more pro-active partner for the rest of the business.
For companies where margins are thin to begin with, this approach seems logical. However, the proactive management of commodities risk is not an Asian issue per se; there is clearly a commonality of themes and issues across all regions. For treasurers, knowing when and how to react is becoming another crucial part of the skillset and making sure they have the right tools to do the job can set them apart from their competitors.



A valuable proposition

Often cheaper and faster than using external banking infrastructures, in-house banks can revolutionise a company's cash flows and significantly reduce the expensive time cash spends stuck in the banking system. But given that corporates must streamline their payment processes and increase the visibility and control over cash flows first, Treasury Today Asia explores the role of a treasurer in implementing the structure.

Predominantly established by medium-sized businesses upwards, an in-house bank (IHB) acts as the main provider of bank services, which are traditionally provided by commercial banks, to all group subsidiaries – on a regional or global scale. Rather than relying on local external banking partners, therefore, each subsidiary directs its cash flows through accounts held at the IHB. The internal bank is then responsible for netting out the resultant debit and credit balances across the whole group. This structure can result in huge savings of both time and money, as well as boasting limited disadvantages (see Table 1 overleaf), so what do treasurers need to know?

Firstly, it must be noted that IHBs should not be seen as the first port of call when trying to streamline cash flows and payment processes. There are several other elements that are needed in conjunction: efficient external payment processes, shutting down bank-specific payment tools and electronic payment stations, making sure you have straight through processing established and cleaning master data and bank account management, for instance.

The reoccurring advice is to start with the standardisation and automation of payment processes and then establish an in-house bank to achieve the added value from this.
For instance: a consolidation of FX transactions and a greater ability to recycle cash within currencies.

Communicating benefits

The implementation of an in-house bank should be seen as a transformation project, and its design is not to be planned in

Some considerations in Asia

The regulatory hurdles in Asia meant, for some time at least, corporates in the region favoured a more traditional set-up. But recently, the popularity of IHBs in Asia has been on the rise; expansion has been occurring rapidly in some of the less restricted markets such as Hong Kong, Singapore and Australia. In these markets, the IHB processes payments and collections through its own accounts but where the use of local currencies for cross-border transactions is restricted, an account held in the name of a local entity can be used.

Even in extreme cases where the IHB can only operate as a processing agent – utilising local accounts held by subsidiaries, rather than accounts held with the IHB, to process payments and collections – benefits of standardisation and greater control can still be felt. Careful due diligence, in terms of the legal, tax, accounting and technology issues, is required for each market in order to address whether any level of local customisation of the IHB structure is necessary. Often, specific in-country requirements will drive an IHB's operations in Asia. In South Korea, for instance, strict data privacy rules will restrict any IHB holding company data offshore.

isolation but in partnership with the overall business. The structure's benefits need to be articulated to the key stakeholders. Treasury should demonstrate to all areas of the business how an IHB can add value. Since treasury teams are under increasing pressure to drive down internal operational costs and to increase visibility and control, the argument for IHBs is persuasive.

What's more, core banking partners should be brought into the early stages of development to provide the banking infrastructure and consultancy expertise necessary. This is because when all of the internal transactions have been carried out by the IHB, any remaining investment, financing and hedging needs will be fulfilled by the company's preferred group of external, relationship banks. IHBs should be seen as complementary to existing bank landscapes.

It would be wrong to assume that traditional banking relationships suffer – the set-up may actually deepen them. IHBs are often run with the support of just one of two banks, to carry out final stage transactions, so they are likely to handle more flows than previously. This isn't to say, however, that IHB structures necessarily suit every company.

Table 1: Advantages and disadvantages of an IHB

Advantages	Disadvantages
Economies of scale achieved.	Group treasury must be confident that each subsidiary will submit all its transactions via the in-house bank.
The number of bank partners and bank accounts is streamlined.	Loss of interaction between local subsidiaries and local banks may reduce local competence regarding treasury and banking issues.
More competitive rates are offered to subsidiary borrowers and lenders, compared to those that may be obtained locally.	–
Group treasury has greater control, improved transparency and access to more accurate data.	–
Group treasury can operate the in-house bank as a profit centre.	–

The benefits of IHBs are dependent on the presence of several factors, including:

- The number of countries (and different currencies) involved with the company's outgoing payments.
- FX volume and extent of hedging activities.
- The number of transactions – internal and external – treasury is responsible for.
- Total amount of bank fees.
- Group structure and geographical distribution of operations.
- How centralised treasury management is, including the IT structure (ERP systems, interfaces and electronic banking systems, for instance).

Location, location, location

In order to provide the most value to the business, the location of the IHB needs to be considered too. This selection process will involve wider elements of an individual company's operating model, such as: current business operational locations, whether certain countries have specific requirements, associated tax and regulation issues and the company's articles of association. For those countries with nuances, it is advised that control is centrally maintained, even if the country's bespoke model sits outside the main IHB structure. For instance, the IHB executes the transactions in the name of the local subsidiaries.

To avoid centralisation and standardisation being compromised by country-specific concerns – local payment instruments, technology capabilities and banking infrastructure maturity, for instance – explicitly entails a large amount of research prior to implementation of a full service IHB available to all subsidiaries of a group. Including exceptions and nuances in the overall design will ensure treasury's key priorities, compliance and operational risk for instance, are not undermined.

However, the end visibility this affords is important to the success of an IHB. By having more control over all payment traffic, treasury can provide strategic information to the board – in turn, allowing them to make informed decisions. Any organisation considering rolling out an IHB structure should evaluate the costs, of course. But other factors to

Firmenich

Case study

Founded in 1895, Firmenich SA is a private Swiss company in the perfume and flavour business. Employing 6,000 people globally, Firmenich is the largest privately owned company in the industry and ranks number two worldwide.

The challenge

As part of a global financial transformation project – to ensure that it had the necessary structure and governance to operate with rigour and discipline moving forward – Firmenich was looking to replace its traditional decentralised cash management solution with a global solution.

One of the company's requirements was to reduce the number of external banks used by the affiliates to one core bank while offering, at the same time, the possibility to opening internal bank accounts with the in-house bank (IHB). Firmenich also wanted to deliver uniform payment and security processes, to ensure compliance with its risk management and internal control standards and to deliver true automation.

The solution

After putting the mandate out to tender, Firmenich selected BNP Paribas for Europe, Citi for the rest of the world with the exception of the CHF covered by UBS to be their partners for the new solution. Working together with the banks Firmenich implemented a global cash management solution covering all 28 affiliates allowing them to join its global cash pooling solution as well as its inter-company netting process. This was completed by the implementation of a payment-on-behalf-of (POBO) structure serving more than 20 affiliates.

In less than two years, Firmenich has set up a global IHB. This was made possible by the existence of a single SAP instance (ECC6 version) implemented earlier to which two new SAP modules (IHC and BCM) were added to run the IHB. Today, the IHB is:

- Heading a global cash pooling structure (26 affiliates zero balanced on a daily basis on master accounts held in Switzerland and UK), offering full control on the cash around the globe.
- Running an internal netting (ICO) process to settle the payables and receivables of 25 affiliates.
- Paying on behalf of 22 affiliates using only three banks.
- Providing a complete change in the payments process of the company, transforming inter-company payments into internal settlements with no cash transfer and cross-border payments into domestic payments.

Key benefits include: reduced reliance on bank credit lines, reduction in bank charges, productivity gains (on average, 800 intra-group invoices are processed on a weekly basis without any rejection) and a daily view on more than 95% of the total cash of the group, out of which more than 75% is captured by the cash pooling structure.

address before implementation include: educating the workforce, deciding upon new workflows and who will carry out what. Clear segregation of duties is needed when operating an IHB. There are various banking functions, such as bank account services, financing and hedging services and payment services, which can be brought in-house but it might not be in every case worthwhile to implement all.

Any changing of processes need to be well articulated to local teams. Starting with the benefits may ease some of the potential frustration as a result of losing control. For instance, from the local entities perspective, the IHB bank account will function like any other bank account. Employees can settle payments and receipts, as well as monitor such activities. Additionally, IHBs are closely linked to the company's ERP system and treasury systems; subsidiaries can export statements to integrate with AR/AP and accounting systems.

Internalising banking services

The centralisation of treasury operations has been an increasingly valuable proposition for some time now, but one which recent technological advancements and regional harmonisation are allowing to gather momentum. Although an IHB structure can also be used to enhance operations whilst keeping a decentralised structure, one of the major drivers for establishing one is the centralisation of liquidity.

Working capital optimisation, bank fee reduction and returns on idle cash are some of the many benefits corporates can expect from an IHB, which, in the current climate, would be well received. However, it is that same climate where the greatest threats to IHB structures originate – currency restrictions, political sanctions and regulation are the key things to bear in mind in 2016.

Mitigating FX execution risk

Derivatives have always presented delicate control risks and corporates, with their limited resources, are particularly exposed. This article explores these risks and suggests practical risk mitigation, specifically four eye FX dealing.

Rogue traders

Some recent accounts of rouge traders in the press set me thinking about the risks for corporate treasury. Granted, many of the famous cases involving rouge traders occurred in financial institutions and trading houses. This makes sense because such institutions tend to trade huge volumes and to hold derivative positions for profit, entailing greater risk.

Corporates, on the other hand, generally use derivatives for hedging purposes alone and have relatively smaller volumes. That said, a derivative hedge is still an outstanding position in the derivatives book. Furthermore, corporates are often resource constrained, and cannot afford the organisational bulk and complexity that financial institutions deploy to mitigate derivative risk – leaving room for foul play.

The danger of derivatives

Most of the famous rogue trader cases involve financial instruments like stock indices, bonds, and some commodity instruments. In fact, many were in futures markets, which are relatively transparent but presumably the rogue positions were hidden in large complex positions.

For the corporate treasurer, the greatest dealing risk comes from pure derivatives with future settlements. Over the counter (OTC) products, often used by corporate treasurers, normally trade against credit lines which makes them more easily hidden than futures, for example, which entail margining and daily mark-to-market with brokers.

If we exclude commodities as a minority sport in corporate treasury, the main OTC derivatives used by corporates are interest rate swaps and FX forwards. Given that interest rate swaps tend to involve longer tenors and therefore more complex and hard to hide credit discussions, the most common vulnerability is probably from FX forwards.

In contrast, cash transactions such as loans, deposits and spot FX settle promptly (instantly or nearly instantly). Any damage caused from foul play can arguably be limited because the results of the transaction remain hidden for less time. There are of course exceptions to this rule. Take for instance structured notes or deposits which tend to be cash deposits with derivatives (usually options) embedded. These can pose nasty risks, but corporates should not be using these in any case.

Front office risk

In the days of phone dealing, corporates simply had to trust their front office. There was little that could be done to stop a dealer who had gone off the rails from sneaking in a large unauthorised trade. And, even in the absence of malignancy, there was also the risk of human error – buying instead of selling or mistakenly adding an extra zero.

Whilst open plan offices have helped in creating a self-regulating environment, there is still plenty of opportunity – particularly in small teams with colleagues frequently travelling or in meetings – for a problem to occur. Moreover, small treasuries often don't record phone lines and by the time a paper confirmation has arrived, it may be the case that the market has turned against you.

> "Visibility and segregation of duties are essential to mitigate the risk of rogue trading."

FX trading

For the majority of corporate treasuries, the control situation is now much better than in the days of phone dealing. Most corporates deal FX online through multi bank portals like FxAll, Currenex, 360T and Bloomberg. This gives a powerful audit trail that can be monitored by middle office in real time. A large number also use electronic confirmation, which provides near real-time awareness of FX deals – usually with segregation of duties where the front office deals and back office confirms.

In some parts of the world however, eFX is less well accepted. Treasurers seem to believe that they can obtain better prices from their buddies at the banks' treasury sales desks. And some fear that eFX will damage bank relations. The reality is very different.

It is very clear that eFX dramatically aids price discovery. The ability to get multiple prices at once while viewing market rates is unbeatable. While it is not recommended to ask too many sources for each deal, treasurers can cover far more counterparties with eFX than by using multiple phone lines. And the risks are far lower because the eFX portals update in real-time, which is not possible with over the phone dealing.

On the bank relationship side, eFX allows treasurers to show more deals to more banks than would be possible by phone dealing. Thus it offers banks more opportunity to win business and can thus improve the relationships. In addition, during relationship reviews, eFX provides detailed bid data that helps banks understand how to win more business. eFX also reduces costs for banks, so everyone gains.

Four eye dealing

A major source of dealing risk comes from one individual being able to deal alone. The Holy Grail in this respect is to have four eye dealing – segregation of duties within the dealing process itself. Note that the deal approval feature in most TMSs is no help because it happens after the deal is executed and cannot guarantee that the deal was correctly captured, or indeed captured at all, in the system.

One treasurer that I worked with resorted to doing FX deals by having a dealer and manager on the phone at the same time, and insisting that banks only book the deal when the manager has confirmed. This is extremely cumbersome and complex (which means operationally risky) for the banks, not to mention a waste of time for the corporate. The solution we found was to segregate roles within the eFX platform.

The different roles and user rights are:

- **FX risk team.** This team collects and analyses exposure forecasts from subsidiaries, and calculates the net exposure per currency to be hedged. Within the dealing platform, they have rights to enter the deal currency, amount, and maturity. They do not have the right to deal.
- **Front office.** This team comprises the dealers themselves. Within the dealing platforms, the dealers' rights do not allow them to input currency, amount and maturity. They are only allowed to execute the deals that have previously been entered by the FX risk team.
- **Middle office.** This team monitors financial and operational risk to ensure compliance with policy.

Within the dealing platform, they have read-only rights to the whole system, so they can see what is happening in real-time. They are notified with real-time emails of all significant events within the platform.

Obviously, confirmation, settlement and reconciliation are segregated to back office in the normal way.

In constructing this process, we have been able to create a system of enforced segregation between determining what is to be dealt and dealing itself – the FX risk team enters what is to be dealt but cannot deal while the front office executes deals but cannot enter what is to be dealt.

Not all corporates will have large enough organisations to allow different teams. That is not important. All that matters is to have different individuals take each of the roles above, to ensure proper segregation of duties.

Visibility and segregation of duties are essential to mitigate the risk of rogue trading. eFX platforms provide this for the most common derivatives traded by corporate treasuries. With the proper set-up of user access rights, a good eFX platform can even enforce four eye dealing – a segregation that was not practical with phone dealing.

David Blair, Managing Director

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

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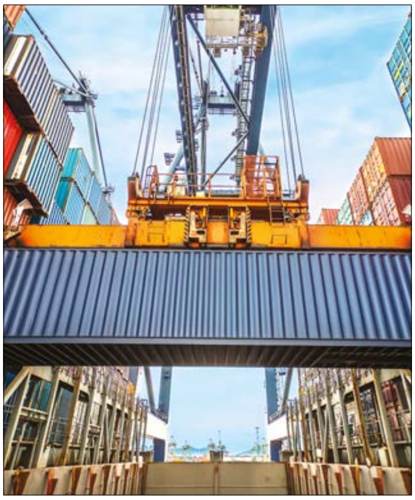

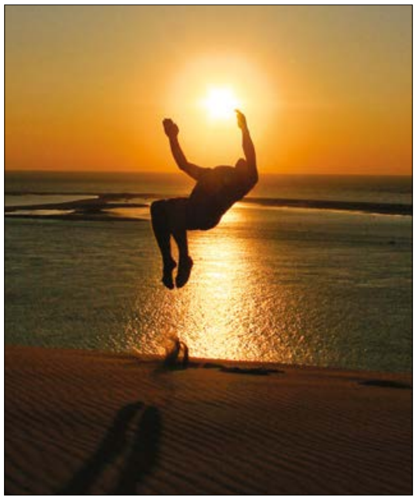

INSIGHT AND ANALYSIS

Selecting the right banking partner in Asia

In recent months, the news surrounding some of the world's largest banks has not been overly positive, and as a result, anxiety is building around the global banking sector and it's health. Given this landscape, it might be a prudent time for corporates in Asia to analyse their banking partners to see if they are able to continue to provide support where it is needed. But, how do you do this? Treasury Today Asia investigates.

TRADE

Asian trade corridors

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

TECHNOLOGY

Building a best in class treasury

For corporate treasurers, the advent of the digital world and the development of innovative solutions has brought with it huge opportunities to drive efficiency and gain greater control and visibility over treasury operations. But, with so many tools now available, and a steady stream of new products being developed, how do the pieces all fit together, and how can a treasurer utilise these effectively to build a best-in-class treasury?

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

Pratibha Advani, CFO, Tata Communications; Ian Banks, Editor, Ellen MacArthur Foundation; Steve Baseby, Associate Policy and Technical Director, ACT; Jan Bellens, Asia Pacific Banking & Capital Markets Leader and Global Emerging Markets Leader, EY; Jocelyn Blériot, Executive Officer, Ellen MacArthur Foundation; Axel Boye-Moller, Head of Global Transactional Services, Asia, Westpac; Catherine Bremner, Global Head of Sustainable Finance Solutions, ANZ; Amit Chopra, Syndicated and Commercial Lending Specialist, Misys; John Coon, Global Treasury Manager, Dow Corning; Ranu Dayal, Senior Partner & Managing Director, BCG; Loic Dujardin, Director, Research, Sustainalytics; Lum Yin Fong, Managing Director, Global Transaction Services, DBS; Jose Franco, J.P. Morgan Liquidity Solutions, EMEA Regional Executive; Jim Fuell, Head of Global Liquidity, EMEA, J.P. Morgan Asset Management; Sridhar Kanthadai, Regional Head, Transaction Banking, Greater China & North Asia, Standard Chartered; Ricky Kaura, Managing Director – Head, Global Corporates, Standard Chartered; Kelvin Lau, Senior Economist, Standard Chartered; Chris Leung, Executive Director, Group Research, DBS; Phil Lipton, Director, Asia Pacific Loan Market Association; Roger Merritt, Managing Director, Fitch Ratings; Thiam Hee Ng, Principal Economist, Asian Development Bank; Hugo Parry-Wingfield, EMEA Head of Liquidity Product, HSBC Global Asset Management; Yigen Pei, China Country Head, Treasury and Trade Solutions, Citi; Gavin Power, Deputy Executive Director, UN Global Compact; Xu Sitao, Chief Economist, Deloitte China; Christina Tonkin, Managing Director – Global Loans & Advisory, ANZ; Siobhan Toohill, Group Head of Sustainability and Community, Westpac.


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