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Treasury in China's new era

As China enters a brave new era its policy makers must manage significant risks in its economy without impeding growth. This is likely to present opportunities to some corporates in China, whilst creating new challenges for others. Treasury Today Asia analyses the forces driving the country's transformation and looks at what this all means for treasury.

The Corporate View

Amit Baraskar

Vice President & Head – Treasury
Thomas Cook (India) Ltd

Risk Management

All businesses are at risk of cybercrime. Yet many are still not putting in place suitable measures to mitigate the risk. How then can quantifying the impact of a cyber-attack spur the business into action and what role can treasury play?

Treasury Practice

Putting cash first

Country Focus

The rebirth of treasury in Japan

Back to Basics

Cash pooling

Question Answered

The impact of US tax reform on Asia

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Will Asia thrive in the Year of the Dog?

Countries across the region celebrated the Lunar New Year in February, ushering in the Year of the Earth Dog. According to the Chinese Zodiac, the Earth Dog is kind, efficient and skilled in communication. It holds the notion of fair play and social justice dear and, given the dog's role as a protector of the home, could be interpreted as time for a shift geographically and politically from predominantly offensive positions to more defensive positions.

In a period of great geopolitical unrest and uncertainty, this is certainly a welcome notion. We may have already seen the evidence of these ancient mystic forces at work with the cooling of tensions in the Korean peninsula during the Winter Olympics – a combined Korean ice hockey team was unimaginable for much of the Year of the Fire Rooster.

Whilst one threat subsides – albeit marginally – others increase. For corporates across the region, the risk posed by cyber criminals gets scarier every day. Asia is the world's top destination for cyber criminals, who are taking advantage of inadequate systems, processes and controls to extort millions of dollars.

Although businesses are aware of the risk they face, many are still not doing enough to combat it. To help, Treasury Today Asia explores the various methods that can be used to combat cybercrime, explaining why quantifying the financial impact of cyber-risk can be the best way to highlight the problem to the board.

Another risk that has certainly grabbed the headlines in recent months has been the staggeringly high levels of corporate and household debt in China. The IMF has cited China's credit boom as being on a dangerous trajectory that may be the makings of the next financial crisis.

This view should certainly sound an alarm bell for any treasurer, with the memories of the last great financial crisis still strong. However, in our deep dive analysis of what is currently happening in China, we find that whilst these debt levels are not ideal, the danger of the bubble bursting and bringing down the global economy is low. Indeed, rather than a bad news story, our analysis of China paints a positive picture, telling the story of a country and economy in transformation as it looks to fulfil its promise as a leader on the global stage.

Elsewhere, we investigate the evolving corporate treasury landscape in Japan and hear how Japanese corporates are looking to re-establish global treasury centres in their home country. Treasury Today Asia also learns from Amit Baraskar, Vice President & Head – Treasury at Thomas Cook (India) Ltd. about his career and how he manages the treasury of a constantly evolving business.

Treasury Today Asia wishes all our readers a very happy and prosperous Lunar New Year.

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President Xi Jinping heralded the dawn of a “new era” for China at the recent 19th Party Congress and called for the country to strive towards the “China Dream”. What will this new era look like, what are the challenges that China faces and what does this all mean for corporates operating in China? Treasury Today Asia finds all this out and more.

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Japan, the world's third largest economy, is home to some of the most innovative companies on the planet. Yet the role of corporate treasury in Japanese companies remains largely siloed and operational. Treasury Today Asia finds out why this is the case and hears how the profession in the country is moving up the value chain.

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Cyber-risk continues to be a focus for businesses around the world and is increasingly becoming an area of focus for corporate treasurers. How then can treasurers go about quantifying the risks they face – and how can these risks best be managed?

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Amit Baraskar

Vice President & Head – Treasury

Corporate treasury is not only a job for Amit Baraskar, Vice President & Head – Treasury, Thomas Cook (India) Ltd: it is a passion. In this exclusive interview, Treasury Today Asia hears how he is tasked with shaping the strategic vision of the treasury department and ensuring that it is well positioned to support the group as it enters a period of rapid expansion and spreads its wings across the globe.

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Pool party

Notional or physical pooling? The basics of both forms of this popular liquidity management tool are explored.

US tax reform

“How should corporates in Asia be preparing to handle US tax reform?”

Tony Kinnear

Managing Director, ASEAN and North Asia, Thomson Reuters

The US Republican government led by President Trump has arguably ushered in the biggest tax reform in US history, and its ramifications extend way beyond the US. As a part of the tax reforms under the ‘Tax Cuts and Jobs Act of 2017’, the United States will:

1. Reduce its corporate tax rate from 35% to 21% and reduce or eliminate other related deductions and credits.
2. Eliminate corporate alternative minimum tax.
3. Change the US tax system from global to territorial with respect to corporate income tax.

Following these reforms, corporations in Asia – whether they be a holding company, a subsidiary or a permanent establishment with a presence in the US – will need to review their tax structures to ascertain the impact of the reforms. Here are a few things corporations in Asia might consider:

- For Asian corporations with US links, it will be important to review their transfer pricing structures. Relevant US reform measures include the new anti-deferral tax on global intangible low-taxed income (GILTI) and the new base erosion and anti-abuse tax (BEAT) on outbound related-party payments. Coming hard on the heels of the BEPS measures and the compliance processes they mandate, the US reforms will keep many corporations very busy.
- The reforms also allow US corporations a 100% deduction for foreign-sourced dividends received from foreign corporations which are owned at least 10% by the US company. This applies to dividend distributions made after December 31st 2018. Asia Pacific companies that fit the 10% ownership rule may see some pressure to pay dividends if the US parent is seeking that 100% deduction. This will, however, be a case-by-case situation.
- The value of unused tax losses for the Asia corporations could also be impacted as a result of the US reforms. When a re-measurement of deferred tax balances arising from a change in the relevant tax rate is done, the amount of the change will be recognised through income tax expense, unless the deferred tax relates to an item recognised directly in equity (for example, movements in an asset revaluation reserve).
- Post the Tax Cuts and Jobs Act (TCJA) implementation, Asian corporations will have to pay particular attention to:
  - The interest expense limitation to 30% of adjusted taxable income (tax EBITDA for tax years beginning on or after January 1st 2018).
  - The base erosion minimum tax measures – these apply to taxpayers with US gross receipts exceeding US$500m and are calculated on income modified to add back certain deductible payments made to foreign related parties (5% for tax years beginning on or after January 1st 2018, increasing to 10% until December 31st 2025 and then to 12.5%).
  - The allowance of immediate 100% expensing of qualified property for five years purchased after September 27th 2017 and before December 31st 2022. This could provide significant tax benefits where applicable.

Lastly, Asian corporations must be cognisant that lower tax rates may make the United States an attractive investment destination and create a strong pull for American corporations to repatriate funds from other economies where companies are taxed at a higher rate. This might pose a challenge to Asia’s competitive position at a time when labour costs in the region are already rising. However, owing to the reduced tax rates, this reform may also present an opportunity for Asian corporations to make new or enhanced direct investment into the US market and deploy more cash into the US market.

The practical implications of the US tax reforms will take some time to for corporations to properly work through. If they have not started already, the time to start is now.

Sandip Patil

Asia Pacific Global Liquidity and Investments Head, Treasury and Trade Solutions, Citi

The US tax reform is one of the biggest tax regulation changes we have seen in a long time. In addition to lowering tax rates, it brings fundamental changes including moving to a territorial tax system, Base Erosion Provisions (BEAT) and Tax on Global Intangible income (GILTI). This presents a unique set of opportunities for companies in Asia – for both US companies based in the region as well as Asian companies operating in the US.

For US subsidiaries in Asia, this presents a unique opportunity in the long term for clients to revisit their legal entity and vehicle structures. As a consideration to the potential impact of BEAT provisions to high value services, US corporates should review restructuring intercompany recharging mechanisms for treasury and shared services, inter-company funding and trading structures, as well as potentially establish/revise the scope of their regional treasury centres or in-house banks.

In the short term, most companies are reviewing the remittance of historic retained earnings back to the US. As US companies in Asia still have operations and significant business presence, we do not expect any immediate action or material USD liquidity shifts from Asia to US as a consequence.

While cash and cash equivalent retained earnings are estimated at US$1trn internationally, less than one-third of this is estimated to be in Asia. As such, we do not estimate significant shifts given the growth potential in Asia, irregularities of working capital funding, regulatory nature of markets as well as wider manufacturing operations.

However, it does provide an ongoing window for companies to remit longer duration surplus back to headquarters. Another factor impacting these decisions is the need for liquidity at HQ in terms of retiring debt or capex or stock buybacks. Corporate restructuring opportunities will drive the broader direction but without material impact to Asian foreign exchange markets.

As the largest bank for US companies in Asia, we continue to work very closely with our clients, guide them on specific aspects of their evaluation as well as connect the thought process with their headquarters.

Similarly, for Asian companies operating in the US, we continue to help them operationalise their cash management strategy in the US and work with their headquarters in Asia to streamline inter-company transactions by providing them with structured solutions around their specific needs. We do anticipate the direction and enablement of these companies achieving increased self-sufficiency of vehicles operating in US.

Overall, we expect these tax changes to provide fundamental restructuring opportunity for our clients' global business.

Allison Cheung

International Tax Partner, PwC Singapore

Nikki Mullins

Senior Manager, PwC Singapore

As multinational businesses evaluate opportunities (both regionally and globally) to position their operations for success, a key consideration is to assess the impact of US tax reform on treasury departments. As such, modelling the impact of US tax reform is pivotal to rewrite the rules of treasury departments for Asian MNCs.

Below we highlight four key areas of focus where disruptions are more often experienced by the treasury department of these MNCs, assuming they maintain a moderate to significant operation in the US:

Cash management and planning. The improved cash tax position arising from the reduced corporate tax rate from 35% to 21%, accelerated cost recovery of capital expenditures and other cash tax improvement items under the new law will need to be rebalanced with the additional tax costs attributable to the less cash tax-friendly provisions. These provisions include the toll tax on mandatory deemed repatriation of foreign untaxed earnings, expanded limitation of net business interest expense deduction, potential additional tax burden from base erosion payments, GILTI.

FX/hedging risk management. As additional cash needs become apparent for US arms of Asian based MNCs to meet their toll tax obligation (albeit over an eight-year payment period), these US companies may be required to bring back offshore cash which could be in various non-US currencies, likely disrupting standing FX hedging programmes. Treasury departments will need to revisit FX and trades to ensure adequate levels of US currencies are maintained in meeting the additional US cash tax needs.

One common practice for multinationals is separate cash pool structures for US and non-US cash. An influx of cash to the US, combined with lower tax costs associated with the dividend participation exemption, may trigger increasing interest in exploring one global cash pool, or cash pool arrangements with multi currency notional cash pooling features.

Capital market and cost of funding. The expanded limitation on net business interest deduction is expected to increase the cost of capital in the US. Depending upon companies' access and ability to borrow locally, this may hamper attractiveness to borrow in the US for funding the investment needs of the group's global operations. However, in countries such as Hong Kong and Singapore, where interest expense incurred for the acquisition of investment that generates non-taxable income is not deductible, the US interest deduction regime becomes more attractive when MNCs borrow in the US for the group's financing needs in and outside of the US (where the deduction limit is not breached).

Liberation of repatriation increasing collective liquidity/investments. The participation exemption essentially liberalises the means to bring back non-US earnings to the US arm of Asian based MNCs. The MNCs now have freedom to implement repatriation plans without the legacy US tax burden. As part of cash management planning, MNCs will need to consider how to redeploy the cash efficiently including paying down existing high interest debt, increasing capital expenditures spend, fund M&A activities and declaring dividends.

Next question:

"Can corporate treasury live without Excel spreadsheets?"

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

China: a delicate balance

As China enters a brave new era and looks to gain even greater political and economic prominence around the world, new opportunities and challenges will emerge for organisations doing business in the country. Treasury Today Asia analyses the forces driving the country's transformation and looks at what this all means for treasury.

President Xi Jinping heralded the dawn of a "new era" for China at the recent 19th Party Congress. He proclaimed that thanks to decades of "tireless struggle", China stood "tall and firm in the east" and it was time for China to transform itself into "a mighty force" that could lead the world on political, economic, military and environmental issues. He called this the "China Dream".

Xi's words come at a time of broader global upheaval, with uncertainty awash in the world's other great spheres of power. It is therefore possible that Xi is being opportunistic and taking advantage of the chaos elsewhere to further China's ambitions. Xi has certainly positioned himself as the opposite to US President Donald Trump by denouncing isolationism and championing cooperation among nations, which gives weight to this claim.

Yet a broader analysis of Chinese political and economic systems shows that rather than being opportunistic, Xi is simply guiding China on a course that it has been on for over a decade now. And as China spreads its wings, gaining even greater political and economic prominence around the world, new challenges and opportunities will emerge. Indeed, rather than just bringing a "new era" for China, the country's ambitions may usher in a new era for the world. As a result, corporates, perhaps more than ever, need to keep a close eye on what is happening.

Changing economic direction

China's economy – the world's second largest – powers the country's global aspirations. However, it is an economy currently in transition. This has seen growth in China's economy slow down, with growth rates dropping from double digits to between 6% and 8%. A decade ago, the 6.9% GDP growth posted in 2016 would have spelt trouble for China's leadership, which measured its success on these numbers. Today, China's economic ambitions are different and these numbers are regarded as the "new normal". The focus for the government is on quality and sustainability, rather than the pace of China's economic growth.

Debt held by non-corporates in China stands at US$18trn

Driving the shift to quality economic growth is the rebalancing of the economy. The objective of this structural transformation is to reduce the dependence on investment and manufacturing and shift towards a more service, innovation, and household consumption-driven economy. "This is something the government has been pursuing for some time and the evidence of this is starting to come through," says Louis Kuijs, Head of Asia Economics at Oxford Economics. "For example, the role of consumption in the economy is rising whilst the role of investment is declining in line with what we all would like to see. There has been a pronounced trend towards a larger role for the service sector in the economy."

This positive news has seen China enter 2018 on a decent footing. However, some sizeable risks still exist. "When it comes to China, sentiment often changes faster than the underlying risks," says Kuijs. "High levels of debt, which is the big risk people were emphasising a year ago, have not gone away. If anything, debt is still only rising as a share of GDP."

These debt levels saw China's long-term sovereign credit ratings cut by one notch to A+ from AA- last year by S&P Global Ratings. And the rating agency still has concerns about China's macro-credit path, calling it "unsustainable".

"Credit growth remains higher than nominal GDP growth, although the gap has narrowed in the past year or so," says Paul Gruenwald, Chief Economist at S&P Global Ratings. "Although there is a healthy rebalancing toward consumption taking place, GDP growth targets need to be lowered below 6% in the medium term and reform of the credit-heavy state enterprise sector needs to be accelerated."

Balancing risk and growth

The careful balancing of risk and growth is what Julia Wu, President of J.P. Morgan Chase Bank China and Head of Corporate Banking for J.P. Morgan China, pinpoints as the biggest trend in China right now. "The government has publicly stated that preventing systemic risk is its top priority," she says. "This is why it is pushing local corporates to deleverage, pushing the banks to bring off-balance sheet items back onto the balance sheet, and strengthening the regulatory regime."

China's vast shadow banking sector is one area that has come under particular scrutiny. This has led the regulators to put several reforms in place to curb risks. One of the most notable for corporates has been the measures introduced by the CSRC to strengthen China's money fund industry – which has total assets under management of around RMB6.5trn. These measures impose tighter limits to reduce concentration risk, limit a fund's exposure to any single borrower and reduce

a fund's ability to invest in assets with a lower credit rating. Asset managers are also no longer able to promise investors a guaranteed rate of return.

Another area of China's shadow banking industry impacted by the regulators is the use of entrusted loans – loans that are made from one company to another with a bank earning revenue by guaranteeing and arranging the transaction. Towards the end of 2017, Beijing began to clamp down on these products, meaning that banks are no longer able to provide guarantees for the loan. They have also stopped the loans from being used to buy equities, bonds or derivatives by the company borrowing.

Whilst these moves are clearly a step in the right direction to drive risk out of China and align the country more closely with 'international standards', there is a fear that they will negatively impact growth. However, with China's economy growing faster than expected in the fourth quarter of 2017, this isn't happening just yet.

China is also balancing its regulatory tightening by loosening its grip on other parts of the economy. Notable moves include the launch of bond connect – a mutual market access scheme that allow investors from mainland China and overseas to trade – which further integrates China's financial markets with international markets. Elsewhere, China has said that it will remove foreign ownership limits on banks, while allowing overseas firms to take majority stakes in local securities ventures, fund managers and insurers – a move that will make China's banking sector more competitive.

Local impact

J.P. Morgan's Wu says that local Chinese corporates will feel the biggest impact of these changes. "They are clearly going to have to deleverage faster than they might have initially expected," she says. "These companies, especially those heavily engaged in or reliant on the shadow banking sector, will also be required to rethink their processes and operations."

This will accelerate a broader evolution within many Chinese companies that are looking to adopt best in class principles to ensure they also achieve lasting and sustainable growth. "Many local corporates are moving overseas and expanding their operations," explains Wu. "At the same time, they are also refocusing to ensure they concentrate on their core business."

Both these trends are requiring enhanced treasury capabilities, says Wu. "Treasury teams of local corporations are very interested in how global businesses manage risk and liquidity when operating across many different markets. They are then coming to us and asking for solutions that provide them with visibility, efficiency and that also enable them to hedge risks."

Mobile payments in China **totalled RMB81trn** for the **first ten months** of **2017**

In focus: the debt pile to end all debt piles?

Corporate debt is a problem in China. A big problem. Data published by the Bank of International Settlements (BIS) at the end of 2017 highlights this, showing that debt held by non-financial corporates in China stands at US$18trn.

This debt is making people nervous. The IMF has called it "dangerous", whilst Zhou Xiaochuan, Governor at the PBOC, has acknowledged that companies in China have taken on too much debt. The fear is that with corporate debt in China continuing to grow faster than the economy, the bubble will eventually burst. The impact of this on the Chinese and global economy could be devastating, potentially creating another global financial crisis.

The good news is that the risk of a near-term crisis is relatively low, according to Paul Gruenwald, Chief Economist at S&P Global Ratings. "Owing to its high savings rate and current account surplus, China is a self-funded country," he says. "As long as domestic confidence remains high – which remains true at present and shows little chance of changing – the risks of an economic crisis are contained."

This doesn't mean that the problem doesn't need to be solved by the Chinese authorities. "There has been a large accumulation of bad debt in the economy," says Louis Kuijs, Head of Asia Economics at Oxford Economics. "Around a quarter of this is found in sectors with weak financial indicators where there are sub-par rates of return and high debt to equity ratios. But these firms continue to borrow and it will become increasingly harder for them to repay."

The Chinese government is aware of these issues and has issued various statements calling for Chinese companies to reign in debt. One such statement came in August last year when the finance ministry issued directives saying that state-owned companies should improve returns, control risks and make sure that "projects are financially viable before decisions are made".

"SOEs are heeding the central government's directive to control debt leverage and they made tentative progress in 2017," says Christopher Lee, Analyst at S&P Global Ratings. "We expect SOEs to put in a bigger effort to control debt leverage in 2018-2019 because the regulators have recently announced that SOEs need to reduce leverage by 200bp over the next two years. We expect SOEs to raise equity, sell non-core assets and undertake debt-for-equity swaps to improve their leverage."

It's clearly a delicate balance for the Chinese authorities. On one hand, they want to curb risks that exist in the economy because of corporate debt. On the other, they do not want to stifle economic growth. The IMF has noted that growth will come first and the Chinese authorities will do what it takes to attain the 2020 GDP target. As a result, it expects China's non-financial sector debt to exceed 290% of GDP by 2022.

Tied to this uptick in treasury sophistication, Wu is seeing many companies looking to centralise their treasury activity. "Hong Kong is becoming a very attractive destination now for Chinese corporates looking at establishing regional or global treasury centres," she says.

Highs and lows

The move to align the Chinese economy more to international standards can only be a good thing for international corporates. However, treasurers at these companies are not getting carried away or expecting that operating in China will be like operating in Singapore or Hong Kong anytime soon. Recent experience has shown them that in China, things can change very quickly.

This is especially true when it comes to currency controls. "For a while, the regulatory environment was relaxing and we were able to move money into and out of China quite freely," says Anthony Osentoski, Head of Corporate Treasury and Insurance, Asia Pacific at Solvay. "Then in late 2016/early 2017 things changed and the regulators introduced rules that brought in tight quotas, limiting the amount of CNY they could transfer offshore."

For treasury teams, this 'window guidance' has had multiple impacts. For example, some corporates had spent considerable time and effort building cross-border cash pools that overnight they were no longer able to use. For Osentoski, window guidance meant that Solvay had to readjust its processes. "We were working on rolling out all of our intercompany payables to be paid in CNY — buying into this vision of CNY being a world currency," he says. "When window guidance came in we had to roll all this back and revert to using the US dollar for cross-border settlement."

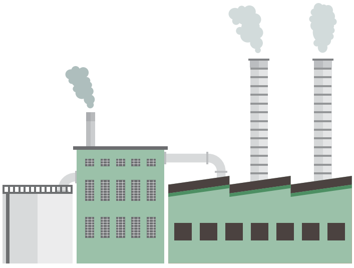
With window guidance lifting, Osentoski is hopeful for the future and expects things to become easier for treasury teams. However, he is cautious that China could, at any time, put the brakes on again. "Despite the challenges that window guidance created for many treasury teams dealing with China, the policy ultimately worked and allowed the authorities to regain control over cross-border cash flows. Therefore, if something like the events of late 2016 happened again, I think we might see the reintroduction of these rules. So, whilst the opening of China is positive, we must always remember that this is happening with an underlying control mechanism ready to be put in place whenever needed. This is very different from many other developed economies."

Leading the world

Another area in which China is different from other developed economies is the development of its digital payments ecosystem. China is arguably leading the way when it comes to being a cashless society thanks to the rise of platforms such as WeChat Pay and Alipay.

Whilst in the corporate space the initial impact of this development is being felt largely by B2C companies, the entire corporate ecosystem in China is beginning to find value in the use of digital payments. To provide an example, Sam Xu, Head of Transaction Banking, China at Standard Chartered, talks about the work the bank has done with a company that services elevator shafts across China.

"This company uses contractors to carry out maintenance," he says. "Traditionally, the building owners would pay the contractors in cash, and the contractors would then be required to take the cash back to the company that hired them. The issue for the company was that the contractors were often slow in bringing the company the cash, and, in some cases, misplaced it."



Chinese SOEs have been asked to reduce leverage by 200bp over the next two years

This created a big problem for the treasury team, which was solved by a solution that utilises WeChat Pay. "Each elevator now has a QR code that the contractor's scan once they have completed the job," says Xu. "This automatically initiates a digital payment for this work that goes straight to the company. In addition to removing the risk posed by asking contractors to handle cash, this solution has also added-value by allowing the treasury to achieve automated and straight through reconciliation of payments."

It must be noted that given the incredible surge in popularity around QR code-based forms of payment in China, the regulators are paying attention. In a bid to encourage payment companies and merchants to adopt better and more secure technology, at the end of last year, the Central Bank introduced rules to set daily payment limits for individuals across all their registered mobile wallets. The limits are tiered based on level of security, with static QR codes capped at CNY500 and dynamic QR codes capped at CNY1,000 per day to uncapped for transactions verified with two or more authenticate factors. "This is a positive move," says Xu. "It will increase protection to consumers and give room for mobile payments in China to continue their impressive growth."

Looking ahead

With so much happening right now in China, it can be difficult for businesses to think too far ahead. But as previously mentioned, the only way to be successful in China is to keep one eye on the future and understand the direction in which the country is heading.

For Oxford Economics' Kuijs, the future is looking bright for China. "Despite some of the difficult issues and reforms that China needs to tackle, I am relatively optimistic on China's outlook," he says. "If you look at what is happening in the real economy, there are lots of positives – and China is well placed to do well in the global economy."

Cash first

How changing company cash culture can improve forecasting

If the whole organisation understands the importance of cash, it becomes easier to harvest more diverse, accurate and timely data. From here, better forecasting can drive stronger working capital performance. It's what most stakeholders expect, so how can it be delivered?

Cash is King, maybe; it's hard to tell as the power that this particular monarch carries has not always been appreciated. However, since the global economy tanked and then started on its long road to recovery, the value of understanding cash basics – such as how much, where and in which currencies – has been rising higher up the agenda.

An accurate picture of current and future cash needs is only possible if every function that affects the ebb and flow of cash understands its importance. Indeed, every touchpoint needs to be able to report its cash position to treasury, with equal accuracy and timeliness, if an enterprise-wide viewpoint is to be achieved.

However, rallying the troops has not always been easy. The list of key protagonists required to achieve this in an industrial context, for example, includes departments as diverse as sales, procurement, finance, production and logistics; each will harbour their own private drivers and agendas.

Regardless of how many functions commune with the King, the importance of building a sustainable cash culture cannot be overstated. It is the driver of accurate forecasting, which is used primarily as a tool to help improve accuracy in investment and borrowing decision-making by identifying in advance potential surplus cash or gaps in cash flow.

> Cash generation is the clearest measure of success for an enterprise and this is why we have decided to place such an emphasis on working capital.
>
> Todd McElhatton, CFO, SAP North America

Forecasting matters

Producing today's cash position is relatively easy compared to accurate forecasting weeks or months ahead. The further out treasury goes, the harder it becomes to offer anything beyond an educated guess. Nonetheless, the ability to deliver accurate cash predictions can be the difference between running out of money and not running out of money, says Tim Bartlett, Senior Liquidity Commercialisation Manager, HSBC. Indeed, he comments, no matter how much a company is valued on paper, without accurate cash flow forecasting, running out of day-to-day cash is a potentially fatal risk.

There is no one correct method of creating a forecast; it depends upon factors such as the nature of the business or sector, the type of forecast sought, its purpose and format. This may sound somewhat unscientific, but with so many unknowns with which to contend, not least macro-economic 'events', forecasting is very difficult to optimise, notes Bartlett.

Of course, there will be some regular and predictable incomings and outgoings which make forecasting a little easier: predictability is the friend of the forecaster. Nonetheless, delivering detailed forecast data with a high degree of accuracy remains a challenge.

Actuals are used to validate forecasts, giving the opportunity to adjust and improve the margins of error in light of any variances identified (and any targets set through KPIs). These validations may be made daily, weekly, monthly or on a longer timescale, according to appetite and ability to monitor, extract, analyse and respond to the data. The more frequently a forecast is updated with real numbers, the more accurate it will be but there comes a point where the effort outstrips the return.

Methods and tools

There are many different forecasting methodologies – the distribution method, regression analysis, and time series trends and seasonal variances, for example – most relying on analysis of historic cash flow data. Because there is no guarantee that patterns identified using historical data will reoccur, these techniques will generate a forecast probability which is commonly weighting, in the form of an accepted margin of error. As the actuals are made available, the degree of 'wrongness' can be fine-tuned with each set of actuals.

The use of technology can take some of the hard work out of this process. Off-the-shelf solutions, from third-party providers such as Kyriba, CashAnalytics and FiREapps use analytical algorithms written with the benefit of the wider industry experience of each vendor. These can offer complex mathematical responses to common scenarios which will be tuneable to more closely represent a company's individual circumstances and strategic approach.

Indeed, such systems can improve forecasting accuracy, for example, by incorporating a computer-based understanding of the behaviours of clients in terms of incoming revenues, and the expectations of suppliers in terms of outgoings.

Of course, many businesses use spreadsheet calculations, adding their own margins of error and iterating each set of results to reach the next waypoint. With output from bank reporting tools having become more sophisticated in recent times there is no suggestion that companies cannot produce sufficiently accurate forecasts using their own tools.

However, the nature of forecasting is such that there is always room to increase accuracy, driving stronger working capital performance.

The cutting edge

One area in which advancement is being made is in the adoption of pre-cognitive technology that borders on the realms of artificial intelligence. This is widely used in fraud detection, enabling the recognition of complex patterns of flow and the predictability of certain activities. This, argues, Bartlett, is the kind of solution from which forecasting can and will benefit.

The encouragement of open banking (largely through regulatory measures such as PSD2 in Europe), where institutions share data flows through API-led connectivity could also bring a more easily aggregated view of flows across a multi-banking environment.

Regardless of technological advances applied to any aspect of treasury or finance, Bartlett comments that "these are only ever tools, and tools by definition are something people use to help get the job done". Of course, the treasurer must know how to use these tools but Bartlett notes a fine line between using them simply as a means of looking for or proving a preconceived notion, and accepting what these tools deliver as the absolute truth.

Higher expectations

Is there appetite for change? Achieving 100% accuracy every time is an unrealistic goal. However, although some businesses do let cash flow drift to the point of becoming technically insolvent, many do not. This suggests that today's forecasting measures are, by and large, adequate.

But with many treasuries having become P&L centres in their own right in recent years, Bartlett argues that there may be expectations of increased return overall for the company, itself demanding higher expectations of forecasting precision.

We know specialist software can bring about a greater degree of accuracy and this may in turn bring about greater working capital efficiencies. But it is clear that to achieve sustainably positive results, not only is the treasurer's input vital but also cash has to be given a commanding position by all parts of the business.

Spread the word

There is an essential "anecdotal" component that must be applied to sharpen the cold logic of technology. Treasurers must have a real feel for, and understanding of, their own business, customers and suppliers. The human element is in part based on the treasurer's own experience and professionalism but this can be enhanced when allied to a strong communicative approach to the role.

This is where the enterprise-wide promotion and support of a corporate cash culture plays out. Indeed, the ability to reach out to other functions – such as sales, procurement and production – and to incorporate their accurate, function-specific data into the forecast in a timely manner, will deliver the greatest level of forecasting accuracy. For treasurers and other stakeholders such as the board, the investors and the analyst community, this is highly beneficial.

The practical power of cash

One company that has spotted the power of putting cash front and centre of every part of the business, is global tech giant, SAP. "Cash generation is the clearest measure of success for an enterprise and this is why we have decided to place such an emphasis on working capital," says Todd McElhatton, CFO at SAP North America.

Developing a culture of cash across an organisation as vast as SAP has been a challenge, with some fundamental changes required at an operational level. One of the keystones of project success has been the incentivisation of employees to see cash in this new light, shifting KPIs to reflect first-class working capital management principles and practices.

By developing a creative new set of KPIs for SAP's sales team, for example, it was able to evolve that function into an effective cash collection team. In the spirit of the old adage that 'it's not sold until its paid for', the sales reps now receive their commission payment for a sale once payment has been received from the customer, explains McElhatton. "Through linking cash collection and commission in this way, our sales reps are now engaged with finance to understand who has and hasn't paid and chasing up any late payments."

It was readily acknowledged that such a fundamental change to the day-to-day working practices of the sales team had potential to create resentment; without their buy-in, and that of other teams, the project to drive working capital performance would never work.

For SAP, the natural solution was to leverage technology. "At the same time that we have focused on working capital management, we have also focused on building a world-class finance department to support these efforts," he explains. Core to this has been the adoption of new technology that has created efficiencies and provided enhanced visibility and analytics, allowing the company to better align the goals of the different departments within the business.

In one practical example, this has seen cash collections benefit from machine learning and AI technology. The approach, says McElhatton, has allowed the finance and sales teams to collaborate closely, focusing only on problematical non-payments. Where finance has a real-time and historical overview of customer payments performance, it can better understand the nature of non-payment, working with the sales team who can reach out to customers only where necessary to begin resolving the issues.

Through the clever application of technology and the adoption of considerate change management techniques, SAP has been able to progressively transform its cash culture across the whole organisation. It has delivered on its initial working capital improvement objectives but will remain focused for some time, says McElhatton who adds that real-time information provides many more opportunities for improving working capital performance.

Taking off with automation

Another example of where an analytical approach has yielded results is with India's low-fare airline, IndiGo. As the Overall Winner of the 2017 Adam Smith Awards Asia Best Cash Flow Forecasting Solution, the company demonstrated how automation of its entire cash forecasting mechanism could offer a huge payback on several levels.

Not least of the benefits has been the realisation that it can bolster its institutional placement funding with its own optimised cash reserves to purchase rather than lease most of its planes as a more cost-effective option.

IndiGo is one of the largest airlines in India with almost 40% market share. With over 20 banking relationships and more than 40 accounts, its treasury team was having to tackle numerous cash management challenges on a daily basis.

Lacking full visibility into many of its accounts, it was troubled by a liquidity management model that it felt was fraught with manual administrative exercises. The lack of visibility also meant it was susceptible to various financial and operational risks.

Shveta Kapur, Associate Director, Treasury, Finance, recalls that its treasury model "lacked much needed scalability". It was realised that existing processes needed "an immediate re-engineering" to manage treasury operations more effectively. In partnership with its principal bank, IndiGo carried out an end-to-end review of its liquidity management processes. This set it on a path towards a number of core objectives.

To give it accurate cash positioning and risk mitigation, it wanted real-time and actionable visibility on all its cash positions and flows. From here, automated rules-based movements could facilitate "easy cash mobilisation", providing centralised access and control. As a third goal, treasury wanted to apply automation to its daily investment programme. This, it was felt, would enable IndiGo to put a major portion of its significant (and growing) daily collections immediately to work, enabling it to earn better interest.

The key to success was a multi-bank cash pooling platform. By automating its entire cash forecasting mechanism, Kapur says the solution was able to eliminate all manual intervention in the IndiGo's liquidity analysis and interbank fund management.

The project also enabled it to reduce manpower and improve productivity, affording it annual savings of around 2,000 man-hours. In creating a single consolidated view, process automation also introduced enhanced analytics and the kind of cash forecasting accuracy and liquidity yield that treasurers often strive for.

DIGITAL ASIA

INNOVATION, DISRUPTION AND FRICTIONLESS TRADE ACROSS THE SECTORS

The momentum driving the digital agenda across Asia has, as its source, the increasing power of the consumer.

Ernesto Pittaluga
Asia Pacific Sales Head, Treasury and Trade Solutions, Citi

As Asian demographics change and consumer wealth rises, the interest in 'frictionless' relationships with vendors gains ground. Failing to meet consumer wants and needs can and will lead to loss of business on a grand scale.

Innovation and the adoption of disruptive technologies has become a key marker of the commercial will to thrive, not just to survive. With pressure mounting on the supply-side to deliver, the impact is being felt across multiple sectors. This is enabling some clear winners to emerge in 'Digital Asia'.

Major online retailers understand that a strong and sustainable digital relationship with consumers is critical. They know that granting consumers easy access to goods and services is essential; from channels to payments, to transportation and logistics, all must flow in the most frictionless manner possible. Online retailers understand that there is fierce competition and that standing still is not an option.

Strategic shift

With digitisation deeply impacting the corporate space, we see global consumer brands switching marketing strategies. Where they were building relationships with their retailers, supporting brand recognition with consumer advertising, they are now showing a far greater understanding and use of digital platforms that are capable of reaching and allowing interaction with consumers directly. This is informing product and service offerings, with knock-on effects across many different sectors, from media and telecoms, to utilities to manufacturing. It seems that many corporates are having to relearn how to run their business.

This dynamic can potentially generate challenges for treasurers. The flow of payments and collections across new platforms may be less than optimal in terms of the value and availability of data harvested. However, the move towards immediate payments, request-to-pay and real-time 24/7 clearing technologies provides new opportunities, for example, the reduction of friction facilitating significant working capital improvements.

We, at Citi, are well positioned to support our clients as they digitise. Our Treasury and Trade Solutions business is organised around truly 'global, simple and digital' lines, enabling access to a broader solution set, deeper analytics and wider connectivity. In China, for example, we were the first foreign bank to connect to the People's Bank's IBPS, in support of a client's B2C relationships, providing 24/7 immediate payment updates that allowed quicker release of inventory to the buyer.

Gathering pace

The drive towards digital enablement and eCommerce will continue apace. All businesses must be prepared to innovate and to transform. However, this is a fast-changing environment that requires an agile way of uncovering and responding to trends.

Although this is largely a consumer-driven transformation, the dynamics in many different industries will change. In fact, it is difficult to think of an industry that will not be impacted. Of course, the banking industry is revolutionising its own approach and Citi is at the forefront of that change.

In this article, we look at sector specifics, revealing the key trends and innovative digital responses that are enabling treasurers to move with confidence towards frictionless digital trade.

OMNI-CHANNEL AND DIGITISATION

SHAPING CONSUMER AND HEALTHCARE STRATEGIES IN ASIA

Rohit Jamwal

Asia Pacific Consumer and Healthcare Sector Sales Head,
Treasury and Trade Solutions, Citi

The consumer and healthcare companies in Asia are at an inflection point of growth. By 2025 the world will look different due to a continued shift from West to East. Asia will be driving the growth due to urbanisation and burgeoning middle class. This potentially will disrupt the West-centric model that many companies have followed in the past. A challenge will be to drive innovation in a global marketplace that's heavily weighted to Asia Pacific. Rohit Jamwal, Asia Pacific Consumer and Healthcare Sector Sales Head, Treasury and Trade Solutions at Citi, explores the options and opportunities.

Across Asia Pacific there has been a continued shift toward online retailers as consumers increasingly skip traditional brick-and-mortar stores and the growth of mobile commerce and contextual commerce becomes ubiquitous. At the same time, mass production and messaging has less appeal today than ever, says Jamwal, so companies are focusing on the localisation of products and crafting personalised advertising strategies to appeal to an increasingly sophisticated consumer base.

Opportunities and challenges

With sales growth on everyone's agenda, the race for "the next one billion consumers" is all about opening up new markets, demographically and geographically. Reaching these markets is necessarily pushing digital strategy to the fore. Improving data accessibility is creating opportunities for companies to exploit direct-to-consumer models, allowing the introduction of new channels whilst maintaining traditional customer touchpoints. New banking technology (eg APIs) is facilitating bundling of products and a readiness for product extension (eg consumer finance) to accelerate point of sale conversion.

Rapid expansion of eCommerce brings a fulfilment challenge, while traditional multi-layer distribution models may no longer be efficient, especially in terms of inventory management, logistics (notably so for perishables) and data fidelity. To thrive, companies need to re-assess distribution and procurement value chain. Social networks may disrupt online businesses in some categories since on-demand retail is feeding instant gratification for consumers.

The liberalisation of government policies is also helping to grow consumption of consumer and healthcare products by the burgeoning middle class across Asia. For example, on December 1st 2017, China implemented new tariff rates on a selection of 187 consumer goods, reducing import duties from 17.3% to 7.7%. The goods covered in the import-duty reduction including food, healthcare products, medicine, clothing and other daily-use products.

Digital channels are the new normal

Digitisation holds many answers and is seen as a disruptive force for many reasons. It removes many entry-barriers for challengers, but also provides speed-to-market for all participants, ultimately creating a "battle for the customer", notes Jamwal. In the consumer ecosystem, for example, the corporate adoption of the Internet of Things (IoT) can help drive internal efficiencies by fortifying supply chain management. Companies are also using store beacons – which communicate with a shopper's smartphone in the hopes of improving the in-store shopping experience – store beacons are immersing retailers with data that they never previously had access to.

But the most obvious use is in how the company interacts with its customers. For example, consumer-focused companies are beginning to use chatbots as service and marketing channels, while artificial intelligence, augmented reality and virtual reality are driving customer experience and expectations. This is something to which all serious contenders must respond.

Technology advancements are also priming major changes in the life sciences sector, offering greater access to information and a rapidly improving ability to respond to it, notes Jamwal. Biosimilars, genomics, point-of-care diagnostics, electronic medical records and wearable health care devices, for example, are reshaping the way in which the sector interacts with the market.

The non-traditional players seeking to monetise Big Data are enabling digitisation of healthcare administration ecosystems. As government healthcare spending reduces, and consumer 'out-of-pocket' costs for popular treatments increase, the sector can only keep up by investing in new technologies, creating new, more efficient models.

At the same time, notes Jamwal, the shift towards holistic patient management and the customer experience has seen companies revisit their marketing models, heralding the arrival in Asian healthcare of packaged financing and subscription modelling.

Treasury facilitator

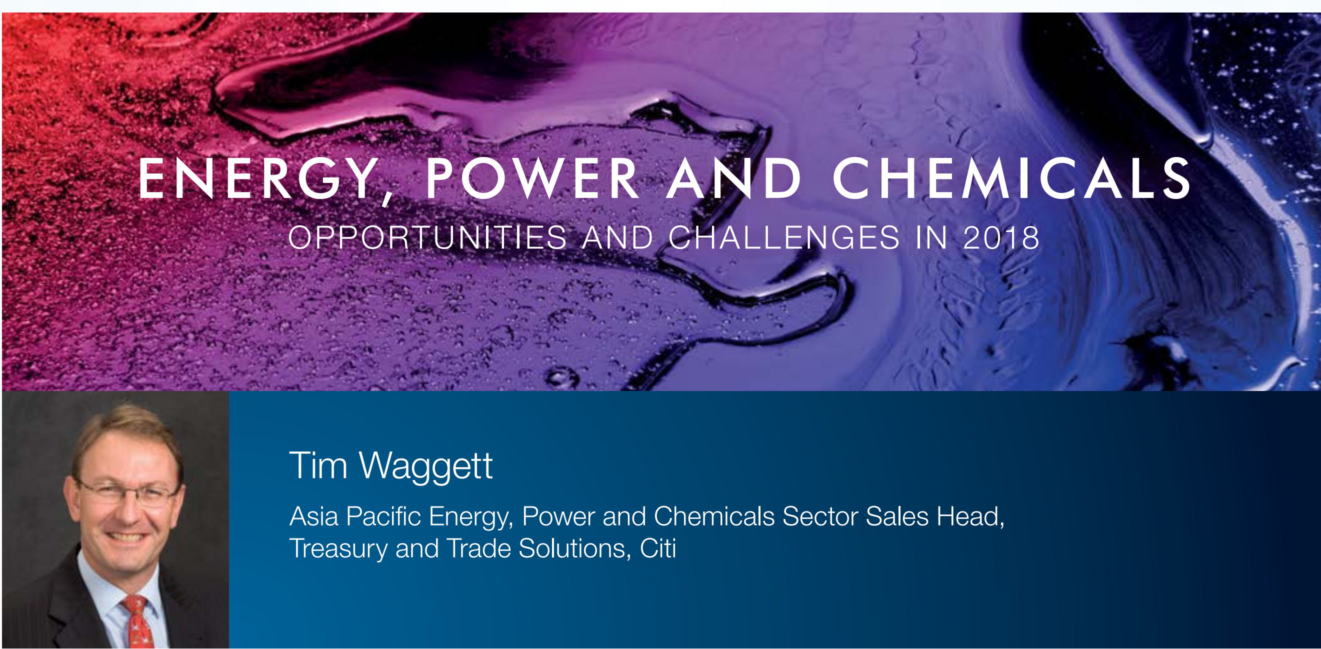
As new models such as these surface, treasurers are emerging as the go-to advisors on key matters such as implementing new payment methods, credit management and working capital management where extended cash conversion cycles and stretched supply chains threaten continuity.

Due to digitisation and innovation, the positive effects are reaching the corporate back offices and shared service centres, notes Jamwal. But market fragmentation in payment methods means treasury's selection of the right banking partner becomes integral to achieving end-to-end efficiency and delivering enhanced customer experiences.

A banking match

For consumer players offering the omni-channel experience, and for healthcare firms seeking cost and technology synergies from account structures such as on-behalf-of, arguably it is their banking partner that holds the key to success.

With Citi hosting "the largest ecosystem of consumer and healthcare sector corporate clients, individual consumers and B2B suppliers", and providing access to an expansive network of networks, on-ground support to business, Jamwal believes clients have a major opportunity to "plug into Citi's infrastructure and drive business growth". What's more, with "best-in-class in technology and regulatory compliance" on tap, that growth is both scalable and sustainable across the region and the world.



As 2018 dawns, a number of themes will continue to provide opportunities and challenges to companies across the Energy, Power and Chemicals (EPC) sector. These include the recovery in the price of crude oil, a greater focus on driving financial returns, nascent investment in upstream and alternative assets, M&A within the Chemical subsector and the impact of China's hugely significant Belt and Road Initiative (BRI). Tim Waggett, Asia Pacific EPC Sector Sales Head, Treasury and Trade Solutions at Citi, explores the key themes.

Following the precipitous fall in the price of crude in 2014/5, OPEC and non-OPEC countries have extended their production quotas to mid-2018, providing producers with much needed relief, as prices will likely remain range-bound. Despite disruption from US shale

producers contributing to oversupply, many shale producers are now focused on debt reduction to strengthen balance sheets after years of profligate borrowing. This will likely help to underpin more robust and higher prices.

Some industry estimates suggest ~US$1trn of capex investment has been removed since 2014/5 which has had a profound effect across the industry, none more so than Oilfield Service (OFS) companies as major participants in the energy supply chain. In an effort to drive down costs, OFS have made significant headcount cuts and been involved in M&A transactions.

For an industry that had become used to high prices, the impact of significantly reduced revenues has "unquestionably" forced energy companies to rethink their strategy and focus on returns, for which the industry has a mixed track record, says Waggett.

Time to move

With environmental and political pressure to deliver on climate emission reductions, clean energy, the potential disruption within the automotive sector, renewables and the rise of Liquified Natural Gas (LNG), energy companies continue to strive for improved financial returns at a time when 'peak oil' is the cause of some concern for the industry, given the duration required for new projects to generate acceptable ROI.

That said, Chinese and other State-Owned Enterprises have combined with the supermajors to participate in the bidding rounds organised by the Brazilian and Mexican governments for offshore exploration blocks. Citi's global network has supported a number of successful JVs and will continue to do so as explorations progress.

Further significant activity has stemmed from China's Belt and Road Initiative. As a key part of the country's expansion of its commercial influence across the region and into Europe, ~25% of investment is attributed to power and energy companies, according to Citi research. Chinese SOEs are at the vanguard of this initiative, with Western expertise increasingly assessing the business opportunities.

And further restructuring is evident in the chemicals sector, as companies seek to scale up as firms aim to take advantage of anticipated significant population and economic growth, notes Waggett. The US$156bn Dow Chemical and DuPont merger has created the world's largest chemical company but other M&A transactions have enabled Asian firms to go global. North American and EMEA headquartered companies are also participating in the industry consolidation.

Everyday efficiencies

From an operational perspective, EPC clients are adopting commercial cards as a more efficient payments mechanism, notes Waggett. By supplementing low-value, high-volume traditional T&E cards with a variety of higher-value procurement card formats (including virtual cards), treasuries have been channelling spend through a single provider, both regionally and globally.

Using aggregated card data and Big Data analytics, efficiencies can be derived across the organisation, driving working capital benefits, he explains.

This renewed focus on working capital has encouraged many to investigate supply chain finance (SCF) to drive further efficiencies. "This is where digitisation and Citi's use of Big Data analytics has significantly moved the needle in terms of being able to dissect client flows and change the angle of engagement with clients," says Waggett.

As an example, Citi's partnership with Visa and Mastercard provides insights on how many clients' suppliers are card-enabled as a merchant. This information is analysed to better understand client flows and metrics around these, potentially revealing more efficient payments structures which may be replicated in other treasury centres.

Trading paper

And as the sector is predicated on trade flows, the need to digitise and automate has taken on a new urgency. Removing paper to enhance workflow is a key area of focus, says Waggett.

Where manual intervention has been eliminated, the focus of productivity can shift to advanced technologies such as machine-learning and AI. These, says Waggett, offer "further practical improvements to workflow and operational efficiency". Some EPC players are, he notes, already engaging with these cutting-edge ideas.

Disruption

The rise of mobile payments, and the move to faster payments in various jurisdictions, is also assessed by forward-thinking companies with downstream businesses. Such disruptive digital solutions are creating new efficiencies and ultimately enhancing working capital, notes Waggett.

"But there is also recognition by treasurers that more disruption is coming," he adds. "The sooner they get on board, the better equipped they will become as meaningful contributors in the discussion."

The understanding of what disruptive technology means for the business, and where the opportunities exist, should be the focus of the debate for all now, he believes. "This is where trusted advisors such as Citi can bring a globalised and cross-sectoral view to the discussion."

THE INDUSTRIALS EVOLUTION

HARNESSING THE POWER OF DISRUPTION

Vincent Couche

Asia Pacific Industrials Sector Sales Head, Treasury and Trade Solutions at Citi

At first glance, industrials might seem a stable sector. However, in reality, it is in the midst of a fundamental transformation, impacting businesses across all sub-sectors. Vincent Couche, Asia Pacific Industrials Sector Sales Head, Treasury and Trade Solutions at Citi, highlights the latest trends.

The industrials sector is currently undergoing a period of transformation. This is driven by significant M&A activity across the various subsectors – including aviation, automotive, heavy machinery, shipping, power and construction – as companies seek to expand into new geographies and take advantage of technological innovation.

This activity is hugely exciting for a sector that creates the backbone of the global economy, says Couche. "Technology is creating the opportunity for many of these companies to redefine themselves and differentiate their products as they pivot towards future growth," he comments.

Evolving sales opportunities

At the heart of this transformation is the proliferation of eCommerce and the technological disruption brought by the Internet of Things, cloud-based solutions, additive printing, robotics and artificial intelligence across Asia Pacific. These disruptive forces have already had a significant impact on the automobile and logistics industries. For some time, companies in both industries have recognised the opportunities that arise from embedding technological innovations in their products and their manufacturing techniques and from selling directly to consumers. "Other industries are not quite as advanced," says Couche. "But all companies recognise that digitalisation is an enabler for growth."

Simply creating a digitisation strategy does not guarantee success, however. Couche explains that for industrials companies to be successful they must offer a first-class user experience to customers. "Key to this is the payment experience," he says. "If paying for the goods and services is inefficient, then consumers will simply take their business elsewhere."

Because of this, treasury teams have become a crucial part of the eCommerce strategy, working to understand the payment trends that exist in the markets that the business is selling in. This is especially pertinent in Asia, where alternative payment methods such as Alipay and WeChat Pay dominate in key markets such as China. "We work with clients to ensure they can receive payments through these different methods in the most efficient manner," says Couche.

Paradoxically, the increase in volume of low-value digital payments can create reconciliation issues for treasury teams in industrials companies. If managed incorrectly, this may increase costs and complexity internally.

Citi has developed a host of tools to help treasury teams solve this issue. For example, the growth of eCommerce is leading to a surge in popularity of Citi's sophisticated Virtual Account and Payer ID solution set. "These allow our clients to easily identify who has paid and what they have paid for," says Couche.

Working capital focus

Disruption is also occurring on the supplier side. Couche explains that a combination of the increasing cost of labour in traditional manufacturing hubs such as China, tied with the adoption of digital solutions in manufacturing processes and into end-products, is

allowing industrials companies to re-evaluate their supply chains. As a result, many are working with a greater number and a different set of suppliers to get new technology and to reduce both costs and counterparty risks.

Treasury is very much at the forefront of these projects, notes Couche, who is also seeing a growing alignment between treasury and procurement. "These two departments, which have traditionally worked in relative isolation, are working in tandem so that new suppliers can quickly be onboarded," he says. "Treasury is also driving a greater working capital focus throughout the organisation, and that is leading companies to think more strategically about the payment terms they offer." Couche notes that treasurers are also thinking about how SCF solutions might enable them to achieve their working capital objectives.

The widening of the supply chain and the increase in the number of crucial suppliers is seeing corporates think beyond traditional SCF solutions, many of which only cater for the strategic portion of the supplier base. "We have seen a growing adoption of purchase cards and virtual card solutions for single and recurring low-value payments," says Couche.

Citi has also seen an increased interest in dynamic discounting solutions, whereby a supplier can request an early payment in return for a buyer discount. These solutions have the dual benefit of supporting suppliers across the supply chain while also offering the buyer returns on spare capital that are more attractive than most short-term investment solutions. "Citi has recently partnered with fintech firm C2FO to offer these solutions to our clients," Couche says.

Incoming opportunities

The most exciting thing for Couche is that there is so much more technological disruption to come. He cites the growth of connected technology and the rise of 3D printing as just two forces that may redefine how companies in the industrials sector operate. "Technology is providing businesses with the opportunity to refine themselves and achieve further growth," he says. "We advise that treasury stays close to the business to understand the direction that it is heading and to be the catalyst for change where possible."

When these industry-specific changes are considered alongside the emergence of faster payments and hyper-connectivity – where data flows in real time – with banks through APIs, the future will look very different, says Couche. "In my view, it is the perfect time to be a treasurer in the industrials sector," he comments. "These changes will create ample opportunity for treasury teams to build on their strategic mandate and find new and exciting ways to add value to their organisations."

To be successful in Asia Pacific's highly competitive technology, media and telecoms sectors, the local needs of customers must be met. Aman Singh Chadha, Asia Pacific Technology, Media and Telecoms Sector Sales Head, Treasury and Trade Solutions at Citi examines the options available for clients operating in the sector.

Companies in the Technology, Media and Telecoms sector (TMT) are known to be trailblazers. Recent history is filled with examples of companies from this sector running on the cutting-edge of innovation, developing products and services that change the shape of the lives that we live today at an astonishingly fast pace.

This is especially true over the past decade, where the rise of the internet and the increasing accessibility of data has created a wealth of opportunity for businesses to innovate. As a result, established businesses have rapidly evolved their offerings, with a host of

> Given the sheer size of the consumer base that can be reached by opening up these collection channels, TMT companies are very interested in understanding the payment trends in the markets they operate in.

innovative 'internet-first' companies emerging in this period. It is no exaggeration to state that combined, technology, media and telecom companies have been facilitators of much of the global growth story in recent years.

Success in the internet age for TMT companies is not a given, however, notes Chadha. Indeed, to be successful in Asia Pacific, these companies must diversify their business models and build nuanced sales strategies to appeal to consumers in markets as varied and diverse as India and Singapore. At the same time, they must ensure they maintain a global outlook in order to ensure operational and financial efficiency and the cohesion and direction of their offering.

Local offerings for local people

Companies that want to be successful in the TMT sector must offer a smooth checkout process to make accessing their products and services as simple as possible, says Chadha. This means giving consumers access to their preferred payment method.

This can be a challenge for businesses in Asia Pacific, given the explosion in payment options that has occurred over recent years. Today, businesses must not only accept cash or card payments, says Chadha, they must also accept payments from a variety of mobile wallet-based payment solutions if they are to appeal to the rapidly expanding tech-aware consumer-base they desire.

The number of individuals using these solutions is staggering, and highlights why businesses are having to enable collections through them. For example, in China, the country's most popular messaging platform, which also doubles as a mobile wallet, has over a billion active users and processes billions of dollars' worth of transactions a year.

"Given the sheer size of the consumer base that can be reached by opening up these collection channels, TMT companies are very interested in understanding the payment trends in the markets they operate in," says Chadha. "They then look to work with a bank such as Citi that has a deep presence in these markets to open these payment channels in the most efficient way possible."

To facilitate these local sales strategies, TMT businesses are evolving the structure of the organisation to not only appear local, but to become local, says Chadha. For example, previously many of the big internet companies had Irish or Dutch entities that were responsible for much of the invoicing and collections activity. "We are now seeing these companies shift this onshore into the markets that they are doing business in," he says. "The shift to local buy/sell models is not just because of local tax or regulatory concerns. It also helps these companies to grow sales faster, by being closer to the actual consumer and opening up additional avenues to sell and collect."

Pushing the boundaries

By becoming local, businesses in the TMT sector are better placed to innovate for growth. This accounts for the products and services they offer as much as the way they operate.

"Companies in this sector are not interested in the status quo," states Chadha. "They want to push the boundaries of what is possible and shape the future by working with the regulators to develop new structures and ways of doing things that are more efficient and facilitate what they are trying to achieve strategically." Citi is playing a crucial role in helping its TMT clients achieve this by helping them formulate the ideas, discussing them with the regulators and, ultimately, bringing these ideas to fruition.

Treasury at the forefront

No matter whether the business is expanding its geographical footprint, shifting its operating model or opening up new revenue streams, one thing is for sure: the treasury department will be busy. It is necessary, therefore, to ensure that treasury is operating efficiently so time can be spent thinking strategically rather than managing manual processes.

This is where TMT companies see real value in their relationship with a knowledgeable banking partner in the region that can help them to quickly roll out new services and solutions to enable the company to meet its objectives.

A bank with a wide footprint across the region can also help TMT companies plug into the various in-country networks and offer payment aggregation services that allow them to use local payment service providers in an efficient manner. This helps TMT companies drive standardisation at a central level, without forsaking the company's ability to offer a bespoke experience to its customers in the different markets across the region.

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A passion for treasury

Amit Baraskar
Vice President & Head – Treasury

Treasury is a passion that runs deep for Amit Baraskar, Vice President & Head – Treasury, Thomas Cook (India) Ltd. In his current role, he is tasked with shaping the strategic vision of the treasury department and ensuring that it is well positioned to support the group as it enters a period of rapid expansion and spreads its wings across the globe.

Thomas Cook (India) Ltd (TCIL) is the leading integrated travel and travel related financial services company in the country, offering a broad spectrum of services that include foreign exchange, corporate travel, MICE, leisure travel, insurance, visa and passport services and eBusiness. The company set up its first office in India in 1881 and today spans 21 countries across four continents with a combined revenue in excess of US$1.34bn. The group is today one of the largest travel service providers across the Asia Pacific region.

Corporate treasury is not only a job for Baraskar: it is a passion. He refers to himself as a "treasury guy" and says that throughout his career, no other role has brought the same satisfaction.

That is not to say Baraskar has not been tempted to venture beyond the walls of the treasury department. Indeed, he describes himself as being "professionally adventurous" and eager to "gain holistic exposure to the business". Yet whatever route he has taken, eventually all roads lead back to the treasury department.

For Baraskar, this is not an issue. Indeed, with treasury's increasingly growing strategic importance at TCIL, Baraskar is finding that his job is evolving, giving him exposure to all corners of the business. "I have always known that treasury is where I can offer maximum value to the organisation," he says. "What I have realised more recently is that it is the role that will provide maximum value to me as well."

SME to MNC

Baraskar is a qualified Chartered Accountant and began his career heading up finance teams for several SMEs across India. These companies spanned a variety of industries including food and beverage and entertainment.

Baraskar says that this part of his career was a great learning experience, especially because it exposed him to a variety of financial techniques. Most importantly, it was during these years that Baraskar developed his passion for treasury after recognising that he had a natural flair for the role. "I became very conscious that treasury was where my strengths lay and where I could work wonders for an organisation," he says.

The chance to prove this came in 2007 when TCIL offered him a position in the treasury team. Baraskar recalls that he thrived in the environment, taking part in a variety of different value-adding projects that helped grow the status of treasury within the organisation.

Four years into his tenure at TCIL, the opportunity presented itself for Baraskar to move into a more commercial role. He recollects being torn at the time, with his passion for treasury pulling him in one direction and his adventurous side telling him to take on the Business Commercial and Credit role. "In the end, both sides won," he jokes. "As I ended up taking on the Business Commercial and Credit role in addition to my treasury responsibilities."

Baraskar managed both profiles for two years and it is a time he looks back at with mixed feelings. "I was essentially doing the job of two people and it took its toll on me," he says. Indeed, Baraskar recalls working from ten in the morning to midnight most days. "Every day that passed it became increasingly difficult to work both roles, so I had to make a decision as to which one I wanted to continue with." Treasury, of course, won the day. And the stars aligned for Baraskar and he was offered the role of Head – Treasury.

Despite the toll that working the two roles had on Baraskar, he does not regret doing it. He says that during this time he learnt many new skills, including what he calls a "Herculean ability" to manage pressure. Aside from being able to manage pressure, Baraskar's time working in Business Commercial Credit exposed him to a different side of the business. "I was also able to sharpen my soft skills as I was constantly meeting with stakeholders inside and outside of the business. Also, this enabled me to understand business dynamics which helped in aligning business and treasury priorities," he adds.

> Corporate treasury is not only a job for Baraskar: it is a passion.

Broad responsibilities

This range of skills has been very useful since taking on responsibility for the TCIL treasury, notes Baraskar. He explains that the treasury at TCIL is "unlike any other in India" because of the unique business lines it supports. This includes the Group's treasury operations in India – TCIL's key market – where treasury manages domestic liquidity, funding needs and banking arrangements, as well as providing strategic support to the business.

Baraskar is also responsible for TCIL's foreign exchange back office and mid office in India, operating a dealing room akin to that of a bank. "We enjoy the status of an Authorised Dealer II – assigned by the regulators – meaning that we are perceived to be working somewhat akin to a bank and are regulated as such," says Baraskar.

Finally, since TCIL's acquisition of Kuoni's global network of destination management specialists in 2017, treasury has provided cash management, banking and funding support for TCIL's businesses in 20 markets around the world. This includes operations in South East Asia, North America, Australia and East and South Africa.

What is most impressive for Baraskar is that all this work is carried out by a lean but "incredibly talented" team of around 17 full-time employees. "Over the years I have worked hard to build a strong team with different skill-sets and experiences that work with one another," he says.

This diverse range of skill-sets and togetherness of the team has proved especially important following the acquisitions in 2017. "The game changed overnight," says Baraskar. "Aside from all the work that was required to integrate the new businesses into TCIL's operations, we were suddenly a multinational company with operations that spanned the world."

Global challenges…

Baraskar admits that becoming a multinational posed some challenges for treasury at first, testing his management skills to the maximum. For one thing, he had to ensure the team's time was managed effectively and that all work was completed correctly. "I solved this fairly quickly by assigning different countries to different people, empowering them to become specialists in that market to provide maximum value. Also, some of the team members work from home at night. All this helped manage the funding and support required by group companies scattered over different time zones," he says.

> If treasurers do not have the right soft skills, it can be very hard for a treasury team to be effective.

Away from management issues, Baraskar has faced additional challenges. "Some businesses at TCIL are thin margin businesses and extremely cost conscious because of this," he says. "As a result, a key KPI of the treasury team is to drive cost out of the business by consolidating, standardising and putting in place stringent controls globally."

However, Baraskar is finding that this is not always possible. For example, he explains that he has been looking for a one-stop collections solution that encompasses the variety of payment methods that exist today. "There has been a lot of evolution in the payments space, which has been great in allowing TCIL to reach more customers," he says. "The challenge it poses is that it creates inefficiency when we are having to use a variety of different portals to collect these payments. Unfortunately, we have yet to find a one-stop solution that is commercially efficient and cost efficient. We are challenging our banks on this one, however."

Elsewhere, Baraskar bemoans the fact that TCIL has been unable to put in place a global pooling structure covering all its geographies because the regulations prohibit cross-border pooling in certain markets. "We are working with our banks to make it work where possible and are ready to leverage regulatory change that allows us to expand the cash pool," he says. "We are positive about getting this done soon."

...and local challenges

Whilst these global issues have proved problematic, domestic issues have presented an even greater challenge for Baraskar of late. He cites the recent implementation of the Goods and Services Tax (GST) as a prime example. "It was introduced in a hurry," he says. "As a result, the financial services industry across India didn't have time to implement GST properly before the July 2017 deadline."

This has resulted in the delay of many financial transactions across India. "For TCIL, and the whole of corporate India, the biggest issue is the turnaround time for collections of receivables, which has increased greatly," explains Baraskar. "This really hurts organisations, because every day that you are unable to collect your cash, you are incurring an interest cost that negatively impacts the business' financials."

There is not a lot that Baraskar can do to solve this issue, apart from waiting for India's financial system to catch up with GST. However, he was able to do something about another regulatory development that has impacted the business: demonetisation, which Baraskar describes as a "rollercoaster ride".

TCIL has a heavy rupee cash requirement due to its currency exchange business across India. "Demonetisation put extreme pressure on this business line as we were struggling to get the banknotes required to serve our customers," says Baraskar. "Thankfully, we were able to work with our banking partners to solve this issue after a few days. This did mean going overboard and withdrawing a huge amount of cash from the banking system, but ultimately it kept the business going. It was a tough time, but my team managed it beautifully."

The power of relationships

Since assuming responsibility for the treasury department, one of Baraskar's main projects has been bank consolidation. To a degree, this is aligned with the treasury's overall objective of cuttings costs out of the business. However, for Baraskar it is also a strategic requirement. "Strong and trusted banking relationships are vital to the success of any global business," he says. "This is especially true in times of stress or volatility."

Whilst this opinion has been shaped over more than a decade working in treasury, Baraskar finds that it is constantly reinforced. He cites a recent example where TCIL urgently required a letter of credit (LC) to be issued in the US. "LCs typically take a week to ten days to be issued by a bank," he says. "We needed it overnight. Thankfully, given the strong relationships that we have with our banking partners, one was able to step up and issue an LC in less than 24 hours and business was able to continue. Even today I still can't quite believe it happened. It just shows you that with strong relationships, you are able to move mountains."

Baraskar's deeply held belief in the value of relationships means that he believes soft skills are crucial for treasurers today. "If treasurers do not have the right soft skills, it can be very hard for a treasury team to be effective," he says. "This is because the role is about managing people just as much as it is about managing cash." As a result, Baraskar spends a lot of time working with his staff to hone their soft skills. "This isn't necessarily a formal process," he explains. "In most cases, it is simply a case of taking them to a meeting with a senior banker so that they can see how the conversation flows and how rapport is built over time."

Living well

Away from corporate treasury, Baraskar is a keen athlete and has previously held a state record in the high jump. Today, Baraskar along with his daughter continues to involve himself in individual and team sports.

Baraskar's sporting exploits have also seen him develop a keen interest in health and nutrition and he has recently launched an eBook titled 'The Boundless Powers of Superfoods', sharing his insights on how to stay fit and how foods can help. "I started writing about health and nutrition around two years ago, because I believe that after many years juggling an intensive professional career and numerous amateur sporting activities, I have a lot of experience that I can share with others," he explains. "The aim of the book is to inspire people and remove any barriers that they might have to get on the right track when it comes to health and fitness."

Professionally speaking, Baraskar is keen to continue the good work that he and his treasury team have been doing over the past few years at TCIL to support the business. And, with the company publicly stating that further M&A activity could always be on the horizon, he is acutely aware that a lot more hard work is to come. But, with his passion and drive, he is ready to take on the challenge.

Malcolm Andrews
Group Treasury Manager, SEEK

Jeff Dart
Group Assistant Treasurer, SEEK

SEEK is a diverse group of companies that have a unified purpose to help people live more fulfilling and productive working lives and help organisations succeed. The company is listed on the Australian Securities Exchange where it is a top 100 company employing over 6,000 people and with a market capitalisation close to AU$6bn.

Rapid international growth and the build up of surplus cash in complex markets has created short-term investment challenges for SEEK's treasury team. How did J.P. Morgan Asset Management's liquidity solutions help solve these problems?

Problem…

Over the past decade, Melbourne headquartered employment marketplace, SEEK, has experienced rapid domestic and international growth. Today, the company is present in 18 markets across Asia Pacific, Africa and South America.

Whilst this growth is fantastic for the company, it has created some interesting challenges for SEEK's centralised treasury team in Australia. As Malcolm Andrews, Group Treasury Manager at SEEK, explains: "Many of the markets we are present in, such as Brazil, China and South East Asia, operate strict currency controls that make it difficult for us to bring any profits home. This leaves us with significant levels of surplus cash trapped in these countries."

The issue is especially acute in China, SEEK's largest overseas market. "Traditionally our business in China has invested most of our surplus cash with domestic Chinese banks in term deposits," explains Andrews. "However, as our revenues in China have grown, we have looked to strategically diversify our investment portfolio and ensure compliance with our treasury policy, mitigate concentration risk and optimise yield pick-up."

…Solved

After an evaluation of the investment landscape in China, SEEK's treasury team selected China International Fund Management Co., Ltd. (CIFM), which is the joint venture between J.P. Morgan Asset Management Limited and Shanghai International Trust Co., Ltd. in China, to be its main provider of short-term investment solutions. "It was a fairly easy decision," says Jeff Dart, Group Assistant Treasurer at SEEK. "The investment solution provided by CIFM was very conservative, but still delivers a very competitive yield rate, which is in line with our investment policy."

While yield rate is not guaranteed, CIFM's solution targets an even more competitive investment return because of a tax advantage. "When we invest in bank deposits, there is a tax that is applied to any yield made on deposits in China," says Dart. "This reduces the return on investments and adds additional complexity because of the need to account for the tax and work with the Chinese tax authorities. There are no income taxes applied to any fund in China which means higher effective returns and fewer complexities, which is a big bonus for us."

Solidifying SEEK's decision to work with CIFM in China is the ability to access liquidity when needed. "SEEK is very active in the mergers and acquisitions space and because of this, often needs access to liquidity quickly, which CIFM's solution provides," says Dart.

This is also a reason that SEEK uses J.P. Morgan Asset Management's AUD denominated local liquidity product in Australia. "The big-four banks in Australia dominate the short-term deposit landscape, but they are mainly focused on term deposits of two, three and six months," explains Dart. "This doesn't work for us because of our cash requirements and this is where J.P. Morgan Asset Management step in, providing competitive yield and same-day or next-day access to cash."

With SEEK enjoying the benefits offered by J.P. Morgan Asset Management's liquidity solutions in some of its key markets, there is a desire to extend this relationship further. "We are keen to work with J.P. Morgan Asset Management in every market they are present where we have trapped cash," says Dart. "They are an obvious choice because they provide great diversification and are competitive when it comes to yield."

The opinions and views expressed here are those held by the author at the date of publication which are subject to change and are not to be taken as or construed as investment advice.

A NEW DAWN

FOR TREASURY MANAGEMENT IN JAPAN

Japan, the world's third largest economy, is home to some of the most innovative companies on the planet. Yet the role of corporate treasury in Japanese companies remains largely siloed and operational. Treasury Today Asia finds out why this is the case and hears how the profession in the country might be approaching a new dawn.

3RD LARGEST

ECONOMY IN THE WORLD

POPULATION

126,451,398

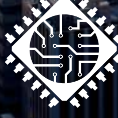
(JULY 2017 EST.)

CAPITAL:

TOKYO

MAJOR EXPORTS INCLUDE

AUTOMOBILES



SEMICONDUCTORS

CONSUMER ELECTRONICS

COPPER, IRON AND STEEL

Japan Inc. is thriving, driven by improved domestic growth, a broader uptick in the global economy and record earnings at overseas subsidiaries. This has seen the 200 companies listed on the SMBC Nikko Securities section of the Tokyo Stock Exchange report pre-tax profits of US$55bn between April and December last year – up more than 14% from the same period in 2016.

Increased profits are adding to the already significant cash war chest held by Japan Inc. Indeed, as of March 2017, Japanese companies, excluding banks and insurance companies, collectively held a record-high JPY189trn (approximately US$1.7trn) in cash and cash equivalents on their balance sheets. As of the end of the year, these same companies owned cash worth more than 140% of Japan's GDP. This is more than three times higher than the 43% of US GDP equivalent held in cash by American companies.

Despite being built as a buffer against future economic crises, some commentators claim such a degree of cash hoarding is preventing Japan from reaching its economic potential. This is because corporates are not increasing wages, a move that would help boost domestic spending power and allow Japan to drive more sustainable economic development, rather than relying on exports.

Stagnant growth of treasury

Cash hoarding is also preventing corporate treasury departments in Japan from achieving their full potential. "The main job of corporate treasury in many Japanese companies is to obtain external funding for the business," says Kaoru Ito, Director at Deloitte Tohmatsu Consulting. "The fact that many Japanese corporates have such high levels of cash reserves means that there is little need for external borrowing, however. Because of this, in the eyes of senior leadership, treasury is not a business-critical function within the organisation."

With treasury in Japan not having the kick-start it has had in other parts of the world, the role remains largely operational, says Ito. "There are also few treasury subject matter experts in Japan as staff are often rotated in and out of the department every two to three years as part of a systematic job rotation programme. There are some exceptions to the rule, where treasury has broken down its operational silo and become more strategic, but these are rare."

Era of global treasury

Corporate Japan is slowly waking up to the benefits a professional and strategic treasury department can offer. Ito notes that several high-profile financial incidents caused by overseas affiliate companies in recent years have made Japanese companies place a renewed focus on corporate governance and prudent treasury management.

Isao Kojima, Head of Transaction Services, Japan at J.P. Morgan, echoes this point, saying that corporate treasury in Japan has not become a strategic function in the way that it has in other parts of the world. However, he is gradually seeing more treasury departments step away from being process driven, involving themselves in the business and looking to mirror global best practice.

For Kojima, treasury best practice means global visibility, control and centralisation, something that few treasury departments in Japan have had before. "Japan Inc. is quite unique in how it has gone global," he explains. "Typically, Japanese companies created subsidiaries in growth markets and let them run themselves – intervention only occurred if there were serious issues."

Japanese companies hold **US$1.7trn** in **cash and cash equivalents** on their **balance sheets** (March 2017).

Although this approach has been successful for many Japanese companies, it has not necessarily been the most efficient, at least from a treasury perspective. "Treasury in Japanese companies is managed at a country level or regional level, but there is very little global oversight bringing it all together," says Kojima. "This prohibits best practice and often results in less than optimal cash management arrangement and increased costs."

The return of overseas talent and the current wave of Japanese corporates conducting overseas M&A is transforming the thinking inside Japan Inc., says Kojima. "Our clients are aware that their businesses are becoming significantly more complex and they want that global visibility to optimise and control how global cash and liquidity is managed, as well as drive costs out of the business. Those that are slightly more advanced are also looking at managing FX risk and global funding centrally as well."

Due to these trends, Kojima is seeing more and more Japanese corporates set up global treasury centres in Japan. "Many Japanese corporates have wanted to do this for some time, but there were several challenges that prevented efficient liquidity structures being created, such as clearing cut-off times, for example." Improvements in the clearing system and innovation from banks through follow-the-sun and against-the-sun sweeping structures have changed the game, says Kojima. "Banks are now able to offer the efficient liquidity structures that allow Japanese corporates to manage the world from their headquarters and thus we are seeing an increase in activity."

Ups and downs: Japan's post-war economic history

Japan has a reputation for incredible efficiency. Just look at its rail network. The latest data available from the Central Japan Railway Company, one of the country's main railway operators, shows the average high-speed bullet train arrives at its final stop just 0.9 minutes late. Compare this to the UK, where research shows that about 57 trains are significantly late (30 minutes to two hours) every day. Or New York, where commuters collectively spend 35,000 hours each day waiting on delayed trains.

Efficiency isn't just evident in Japan's transportation system: it flows through the very core of Japanese culture. This has had a big role to play in the country's post-war economic success that has made Japan one of largest and most advanced economies in the world – a success that has been called the 'Japanese Economic Miracle'.

Many factors contributed to this economic miracle – not least the successful economic reforms adopted by the government post-war, pivoting the economy towards the production of raw materials and putting the country to work. Doing so rapidly converted Japan's militarised economy to drive peaceful economic development, enabling some companies in the automotive and technology space to become world leaders.

Boosting this was 'keiretsu' – the formation of sets of companies with interlocking business relationships and shareholdings. This helped create harmony amongst corporate Japan, protecting companies from stock market fluctuations and takeover attempts thus enabling long-term planning in projects.

The forging of close ties with the United States also had a significant impact. The relationship saw Japan invited to participate in US-led free trade programmes. This gave companies the ability to thrive on the international stage with low tariffs, cheap access to oil and other raw materials needed for industrial development.

Because of these and other factors, Japanese industrial output reached pre-war levels by 1951 and exceeded them by 350% just ten years later. Economic growth was just as impressive, with Japan posting an average growth of 10% in the 1960s, 5% average growth in the 1970s and a 4% average in the 1980s.

In the 1990s the tide turned, however, as Japan went from growth to stagnation following the Japanese asset price bubble's collapse in late 1991. Throughout this period, commonly referred to as the 'lost decade', GDP fell from US$5.33trn to US$4.36trn in nominal terms, real wages fell around 5% and Japan's stock markets hovered near record lows. Excessive business and consumer saving, an ageing population and monetary policy are just a few of the factors that contributed to the lost decade.

Abenomics onwards

The lost decade became 'Ushinawareta Nijūnen' (which translates to 'lost decades') as the economy continued to stagnate at the start of the 21st century. Since then, however, reforms implemented in 2012 by Prime Minister Shinzō Abe have turned the tide. Regarded as one of the biggest economic experiments the modern world has ever seen, Abenomics centres on three pillars: an increase in fiscal stimulus through government spending; an increase in monetary stimulus through unconventional central bank policy; and a reform programme aimed at making structural improvements to the Japanese economy.

Six years on, there has been much debate on the relative success (or not) of Abenomics. It certainly has not solved all issues; weak domestic consumption and huge debt levels remain. However, the economy is much stronger with aggressive monetary policy fending off the deflationary malaise of previous years. Indeed, Japan recorded seven straight quarters of economic expansion to the end of September 2017, its longest uninterrupted stretch of growth since 1994.

Best in class

Japanese automobile giant Nissan is a company that is leading the way when it comes to treasury sophistication. Its multicultural corporate ethos has seen it adopt global best practices, unlike many other Japanese companies.
This includes senior management recognising the value of a strategic treasury department. As a result, Nissan has built a

60-person strong treasury team at its headquarters in Yokohama. This supports regional treasury teams in North America and Europe and drives the strategic direction of the treasury globally.

"It makes no sense for there not to be a global treasury team based here in Japan," says Nissan's Senior Vice President, Global Treasury and Global Sales Finance, Rakesh Kochhar. "The job of the global treasury is not just to raise money and make payments – you can do this anywhere. It is about providing senior management with strategic advice around M&A; it is about managing risks that span across the business; it is about working with sales and procurement to ensure that we are conscious about cash and making the right decisions. To do all of this you need to sit where the decision makers are."

Thankfully, Japan offers all the ingredients required to make an excellent global treasury centre location: good talent, good systems and good banks, says Kochhar. In fact, having worked in other parts of the world, Kochhar is confident in saying that it is just as easy to run a global treasury from Japan as it is in any other liberal financial centre.

Indeed, there are instances where life as a treasurer in Japan is easier than in other key treasury centre locations. Kochhar highlights the regulation governing the asset-backed security (ABS) as one example. "This is an instrument we often use to raise funds. In Japan, I am able to complete a transaction in ten days," he says. "In the US, it takes 30 days minimum because of various reporting that has to be done. This is just one example, but across various areas of finance I see Japan being an easier place to do business than the US."

The need to be close to Nissan's core banking partners also offers a compelling reason for the global treasury to be based in Japan. "We have a group of 18 banks globally, many of which are Japanese," says Kochhar. "Whilst I have found that Japanese banks operate in much the same way as US or European banks, it is true that they place a greater emphasis on the relationship. Sitting in Japan, next door to their head offices, helps me craft these relationships and get the best price for funding."

Banking on technology

Historically, Japanese banks – with their enormous balance sheets – have been famed more for their ability to lend to corporates around the world, and less for their transaction banking capabilities. This, however, is beginning to change as Japanese banks invest heavily in this part of their business to build up their transaction banking franchise around the world.

The country's biggest lender, Bank of Tokyo-Mitsubishi UFJ (MUFG), has been especially determined, with transaction banking being made part of the bank's overall medium-term growth strategy. This has seen the bank make high-profile hires around the world, including ex-J.P. Morgan banker Ken Stratton in Singapore; Yong Lee Boon in Hong Kong, who arrived from Standard Chartered; Michael Hogan, who joined from National Australia Bank and will lead the team in London; and experienced ex-Wells Fargo GTS specialist, Ranjana Clark in the US.

Japanese banks are also serious about technology, especially in the blockchain space. Last year, news emerged of a consortium of Japanese banks that are planning to use distributed ledger to make domestic and international payments. Later in the year, more news emerged stating that Japanese banks plan to introduce a digital currency ready for the 2020 Tokyo Olympics. 'J Coin' as it is known, is an electronic currency designed to pay for goods and transfer money using smartphones. It would be convertible into yen on a one-to-one basis, operating via a smartphone app and using QR codes to be scanned in stores.

More broadly speaking, digitisation is crucial if Japan is to achieve its economic ambitions in the coming years. "Japan's declining birth rate and ageing population means that it is crucial that companies look to adopt new technologies, such as the Internet of Things (IoT), big data, artificial intelligence and robotics to create new growth industries," says Masahiko Morio, Chief Manager, Economic Research Department at MUFG. "Technology can also help plug the gaps left by a shrinking workforce."

To achieve this, Morio calls for the Japanese government to support innovation and industrial restructuring through growth strategies and regulatory reforms. "They should also consider establishing a regulatory sandbox and simplifying administrative procedures."

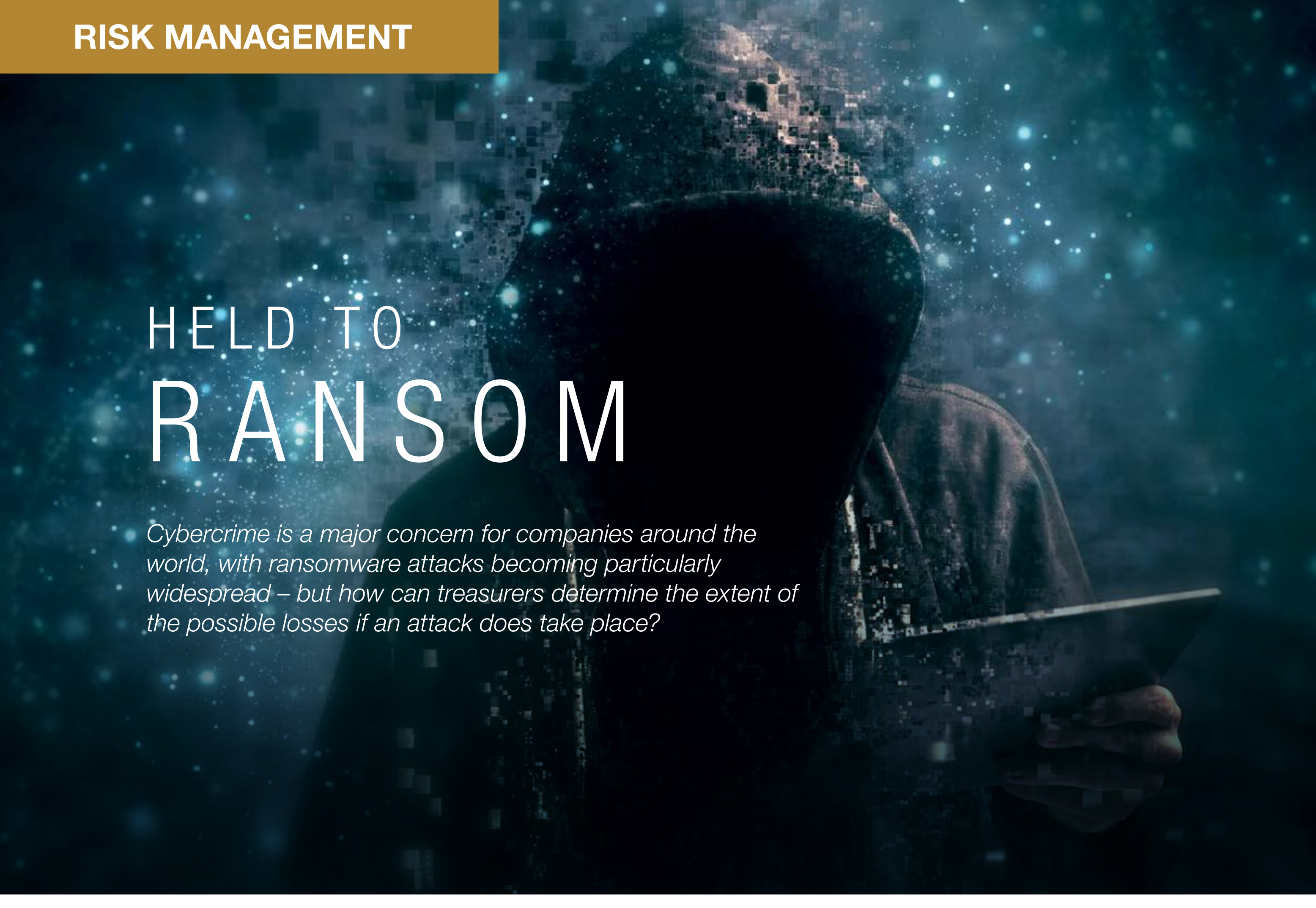
A bright future?

Japan as a nation certainly has lots to look forward to over the coming years, as it hosts the Rugby World Cup in 2019 and the Summer Olympic Games in 2020. Beyond that, Nissan's Kochhar predicts a bright future. "The economy has been doing well in recent years," he says. "And it will continue to do well because it believes in innovation and harnessing new technology." This is reflected in a revised forecast from the IMF, predicting that Japan's economy will grow 1.2% this year, up 0.5% from its October estimate. This is largely due to the broad-based global recovery gathering steam.

Whilst global growth is benefiting Japan's export-heavy economy, the world remains in an uneasy space and a reversal in economic trends could bring recession back to Japan. Domestic demand driven by consumer spending is highlighted as the key to creating more long-term sustained growth in Japan. However, at present, domestic consumption remains flat as wages in Japan have stagnated over the past five years, despite healthy corporate profits and a competitive labour market. Prime Minister Abe has urged businesses to up wages, but Japan Inc. is yet to respond with vigour.

Japan's unbalanced demographics pose a further challenge. Indeed, Japan's increasingly ageing population has the highest spending power in the country – but is reluctant to spend, stunting domestic consumption. The ageing population, combined with the record-low birth rate, may also bring labour challenges further down the line. To combat this, Japan is quietly opening up to increased immigration. Since 2013 the resident foreign workforce has in fact steadily risen, growing 40% since 2013 alone.

From a corporate treasury perspective, the influx of overseas talent can only be positive for the profession in Japan, says Kochhar. "Japan is a fantastic place to live and to work in treasury. Therefore, if the opportunity is there for treasury professionals from around the world to come to Japan to work, I would expect them to take it. In doing so, they will bring overseas expertise and raise the standards of corporate treasury across the country."



HELD TO RANSOM

Cybercrime is a major concern for companies around the world, with ransomware attacks becoming particularly widespread – but how can treasurers determine the extent of the possible losses if an attack does take place?

Cyber-risk continues to be a focus for businesses around the world. The World Economic Forum's Global Risks Report 2018 stated that cyber attacks against businesses have almost doubled in the last five years, noting the cost of cybercrime to businesses is expected to be US$8trn over the next five.

While 2016 saw US$81m stolen from Bangladesh Bank, 2017 was characterised by a proliferation of high profile ransomware attacks – the most serious of which affected hundreds of thousands of computers around the world and cost some corporations hundreds of thousands of dollars to address. Against this backdrop, how can treasurers go about quantifying the risks they face – and how can these risks best be managed?

Current trends

Cyber-risk is one of the main business risks currently affecting the corporate landscape. It's also an issue which is constantly developing. Carl Sharman, a Director in Deloitte's Treasury Advisory practice, explains that the landscape is continuing to evolve: "It's becoming more mainstream in terms of organised crime," he says. "Criminals are increasingly able to perpetrate very lucrative crimes without leaving their homes or offices."

That said, Sharman differentiates between different types of cyber-risk. The first, he explains, is where highly skilled individuals are trying to hack into systems and extract value through technological means. According to Sharman, some clients are taking action against this type of risk by inviting hackers to test their systems for weaknesses.

"The flipside is the low-technology targeting," he adds. "Although this is very technologically focused, the greatest successes are caused by testing the weakest link in the chain, which tends to be the human link."

Changing profile

While cyber-risk includes a variety of different approaches and techniques, Fenton Burgin, Head of Deloitte's UK Debt Advisory team, observes that the risk profile of cybercriminals has changed markedly over the last 18 to 24 months. "More companies are concerned about being targeted by an organisation, rather than a lone wolf individual," he says. "This fundamentally means that a broader range of companies now have to have this on their agenda."

Shirley Inscoe, Senior Analyst at Aite Group, agrees that attacks are becoming more sophisticated. "Originally, many threats were from hackers and young people who just wanted to show how smart they were by breaking into systems," she says. "Today, threats are much more serious. Many are backed by unfriendly nations, and they often are directed against key infrastructure."

At the same time, the cost of individual attacks is rising. Accenture's 2017 Cost of Cyber Crime Study found that the average cost of cybercrime has increased from US$9.5m per organisation in 2016 to US$11.7m in 2017.

The rise of ransomware

One major trend is the rise of ransomware attacks, many of which have been directed at government units and hospitals as well as businesses. Such attacks typically lock users out of their computers, demanding payment in return for restoring access. These attacks are increasingly commonplace: the

Global Risks Report noted that ransomware attacks accounted for 64% of all malicious emails in 2017.

Particularly notable was last year's WannaCry ransomware attack, which affected hundreds of thousands of computers across 150 countries. The attack wreaked havoc for the UK's National Health Service (NHS), resulting in frozen files and cancelled appointments. The ransomware, which attempted to extract payments of around US$300 in bitcoin from victims, also affected Spanish utilities, caused factories to halt production and attacked 1,000 computers in the Russian Interior Ministry. In China, meanwhile, the organisations affected by the attack included 4,300 educational institutions and 20,000 petrol stations.

Wiper malware

Not all ransomware is alike. Shannan Fort, cyber-risk expert at Aon, notes that another trend involves malware which "appears to be ransomware but is actually designed to do nothing but destroy". Last year's NotPetya attack, for example, was first believed to be ransomware but was later identified as a 'wiper' which simply destroys data without enabling victims to regain access to their files. The attack caused considerable disruption in Ukraine and Russia. It also resulted in costs of around US$200-300m for large corporations such as Merck, FedEx and Maersk.

"NotPetya appeared to be Petya at first, which was ransomware, but what it turned out to be was essentially malicious code or malware," says Fort. "The purpose was to wreak havoc by wiping systems and corrupting data."

Counting the costs

The impact of such attacks is set to rise even further. Research published last year by Cybersecurity Ventures estimated that the global cost of ransomware would be US$5bn in 2017, up from US$325m in 2015.

While the costs can include ransom payments, ransomware attacks can also bring a variety of other costs as a result of enforced downtime, loss of data, productivity losses and additional employee training. Accenture's 2017 Cost of Cyber Crime Study noted that the average time taken to resolve a ransomware attack is 23 days.

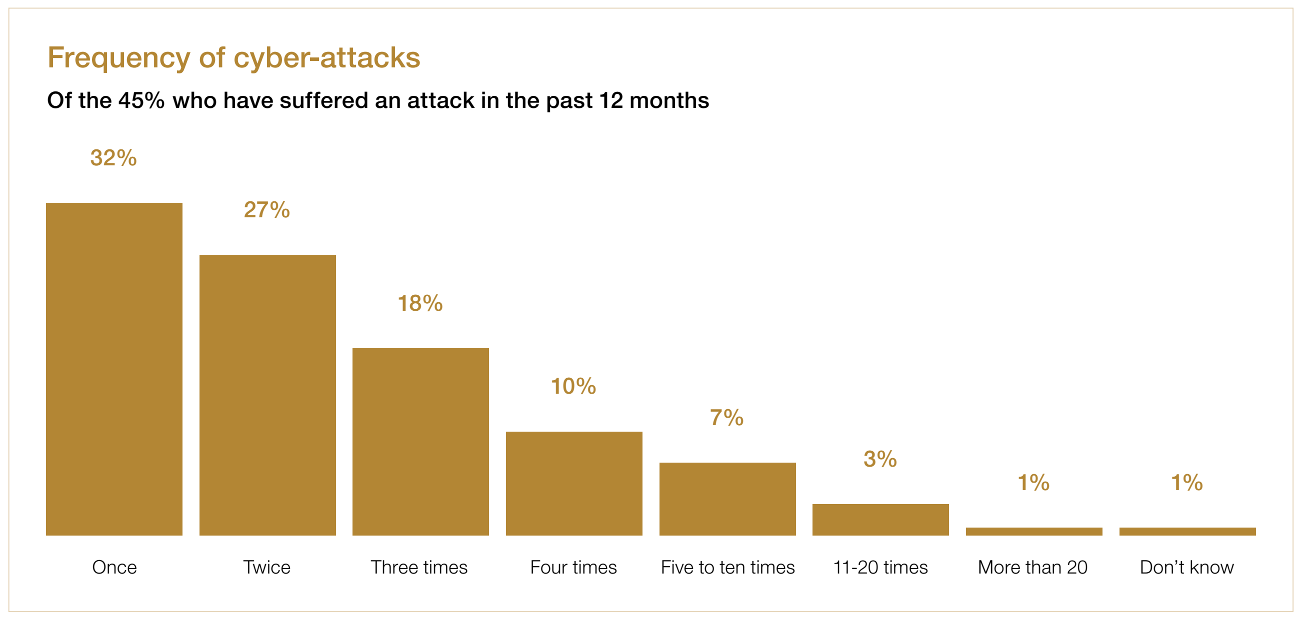
> The **average cost** of **cybercrime** has **increased** from **US$9.5m** per organisation in **2016** to **US$11.7m** in **2017**.

Businesses are often advised not to pay ransom in the event of a ransomware attack: for one thing, there is no guarantee that cybercriminals will actually restore systems once a payment has been received. In practice, however, it is largely suspected that many companies do opt to comply with demands for ransom – not least because they are keen to avoid adverse publicity. "It is very possible that corporates in this situation are choosing to pay, rather than bring this out into the public eye," comments Sharman. "This would then distort the public's view of the extent of the problem."

Beyond financial loss

It's also important to note that the damage incurred by businesses is not limited to the financial. "Financial losses are certainly important, and often include ancillary losses such as productivity losses and other hard-to-measure categories," says Inscoe. "Other losses – such as loss of life when key systems are disrupted in hospitals, or when transportation systems are disrupted resulting in accidents – are more critical."

Reputational damage is another concern, although as Inscoe notes, this may be more costly in the case of large-scale attacks and when consumers' financial accounts and personal information are breached. "There are so many small data breaches in the news that consumers seem to be tuning them out (due to the sheer volume) except when they are personally impacted," she adds.



Source: survey conducted by Forrester Consulting on behalf of Hiscox

Combatting cyber-risk: the treasurer's role

As cyber-risk becomes a more pressing concern, treasurers are playing a more important role in managing this area. Steve Wiley, Vice President, Treasury Solutions at FIS, explains that treasurers have historically relied upon the IT organisation or a corporate security function as it related to the management of treasury-related risks.

"Most organisations have shifted away from this approach over the past several years, with the treasurer taking on more of a shared responsibility, working closely with IT to mitigate cyber-risk," he says. "This has really frustrated that generation of treasurers which isn't deeply educated or trained in technology. Additionally, treasurers have been challenged in accelerating the cyber security learning curve for all core treasury, non-technologically specialised, employees."

As such, Wiley says that treasurers and CTOs are looking for third-party technology providers to play a more active role in mitigating cyber-risk, "through hosting and other managed application and data protection services". Consequently, treasurers "are re-evaluating relationships with all mission-critical service providers, including banks, specialised treasury technology providers, and consultancies providing guidance in technology related areas."

In other cases, linkages between the IT and treasury department are becoming closer than in the past. "Historically the IT and treasury department would have been in separate floors of the building – but increasingly you're seeing IT departments and the treasury function merging," says Deloitte's Burgin. "It's not untypical for the CFO of a large Fortune 500 company to have a range of technology people embedded into their treasury function across all levels".

Quantifying the financial impact

In practice there are a number of reasons why companies may not take action to protect themselves from cyber-risk. According to Inscoe, these may include competing priorities for limited budget dollars, as well as "a naïve belief that it can't happen to your company". But as Inscoe points out, "As the ongoing data breaches and ransomware attacks in the news make clear, it can happen to any company at any time, and the cost of handling the crisis probably far outweighs the cost of avoiding it."

In light of the growing threats, it's important for companies to understand just how much a cyber-attack could cost them. For one thing, quantifying the risks can play an important role when it comes to moving forward with the purchase of new systems. "Quantifying the implications of a potential attack is extremely important in order to justify technology investments to protect companies," comments Inscoe.

It can also help with risk transfer decisions when companies are considering taking out cyber insurance, a relatively recent development. "This is still a very young and new cover, and the data behind it is still developing," says Fort. "We don't have 300 years of property losses and incredibly accurate predictive modelling to rely on to help us understand the likelihood of a loss and the amount that a company is likely to suffer following that loss."

As such, Fort says it's critical that companies take steps to quantify the risks they face. "If the maximum loss you're likely to suffer is less than £10m, and you're buying £300m of insurance, you may not be making a prudent decision when it comes to your risk transfer," she points out.

Counting the costs

However, assessing the risks may not be straightforward. On the on hand, a minority of attacks can and do cost businesses hundreds of millions of dollars – but on the other, the cost of most cyber breaches is considerably less. Consequently, treasurers may face a dilemma when considering whether to spend money protecting their businesses using insurance, or whether to spend the money on strengthening their IT defences.

In practice, the nature and scale of attacks can vary considerably. As Deloitte's Burgin points out, "At one end of the spectrum, it could mean turning the lights out." It's therefore important to look broadly at the possible risks and consider a variety of different scenarios.

"Examples of such attacks should be varied, such as losing system access (eg Sony Pictures), a ransomware attack or a major data breach," says Inscoe. "For each scenario, all the negative ramifications should be defined, and an attempt to quantify the potential negative impacts should be attempted."

Fort says that companies should factor in a number of different considerations when quantifying possible loss – including the company's existing controls. "You have to look at compensating controls as well as the risk that you're facing to understand how a particular incident could impact you, and then what kind of cost you'd be looking at thereafter," she explains. "For example, a company which specialises in forensic investigations has a team available – so your cost around identifying an incident, controlling it and making sure the impact is minimal will likely be less than for a company which has no experience there."

Taking action

Whatever a company's chosen approach, it's clear that cyber-risk is an issue that needs to be managed carefully. Inscoe advises that companies should "define various threats to their environment, envision the impacts of each type of attack, define roles and responsibilities in the event of an attack, add all this data to their business continuity plan and test it periodically". She adds that an evaluation should also be performed of security gaps and a timeline developed to address all gaps noted.

Finally, Burgin notes the importance of having cyber-risk squarely on the agenda of the Board. "It's about having the right resource on your executive team to be able to lead and measure that risk," he concludes. "Going forward, our view is that you're going to see more companies having to have IT experienced professionals sitting at that board table, rather than the CFO having IT as part of his remit."

POOL PARTY

Get back to basics with the pros and cons of cash pooling in all its forms.

According to the ECB, pooling cash within a group represents a "significant opportunity to ensure that the use of internal funds is maximised and the cost of capital is minimised". It is perhaps unsurprising then that cash pooling increased in popularity in certain locations following the onset of the financial crisis. Indeed, the source of this quote – the ECB's July 2016 Statistics Paper – noted that increased adoption was driven by limited access to capital markets, reduced bank lending, low returns and higher risks on banks' deposits with corporates intent on maximising their use of internal sources of financing.

The basics

Cash pooling is an essential liquidity management technique. It brings together a number of individual bank accounts to pool balances, optimise interest and improve an organisation's liquidity management. This could be across multiple jurisdictions, currencies and entities, depending on the type of cash pool in place.

Cash pooling falls into two main types: physical and notional.

Physical pooling

This is often referred to as physical cash concentration, target or zero balancing (ZBA) or sweeping. Balances are physically swept to a header or master account on a periodic basis and may have certain parameters, for example a minimum or maximum balance, a percentage sweep, target balance and a variety of other parameters depending on the provider capabilities. Physical pooling is available on a domestic, cross-border, cross-region and multi-bank basis and is also dependent on the provider capabilities.

The acceptance of pooling structures is not clear cut in every jurisdiction. Because direct inter-company lending in China, for example, is not permitted, physical cash pooling cannot be practiced using the traditional techniques, since this sort of arrangement generates inter-company loans. In order to achieve physical cash concentration, an entrusted loan structure must be used.

Notional pooling

This is primarily a tool for interest enhancement. Notional pooling structures are typically overlay structures. Debit and credit balances on a series of accounts owned by the same or different entities and domiciled in the same country are notionally netted for interest calculation purposes, without a physical movement of cash. Multicurrency notional pooling offers the ability to achieve a net notional position in a single currency without the need to perform traditional FX or swaps, and extends the benefit of further interest savings as a result of compensating balances in different currencies.

Additionally, an **overlay cash pool** can be provided by an international bank offering physical or notional pooling on a multinational, multi-entity company level in country, in region or globally. Overlay cash pools allow changes to existing bank relationships when necessary without disrupting the operation of the cash pool and allow changes to the cash pool to take place without disrupting the underlying banking structure.

Regulatory impact

Under Basel III the cost structures of notional pooling solutions have come into question where some banks have increased their pricing for operating deposits to help meet liquidity coverage ratio requirements.

Corporate global or regional liquidity and funding structures such as notional pooling may be impacted by the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan in the countries where such structures operate.

Where International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS 32) apply, bank account balances are seen as financial instruments that must be disclosed and presented individually. However, US GAAP allows banks to net the balance sheet.

Digging deeper: physical pooling/ cash concentration

Main benefits

Control funds centrally. The concentration of all of a company's surplus cash into one account, generally managed by the group treasury, will improve its control over cash. If the net balance of the cash pool is positive, this aggregated balance can be used to invest in overnight or short-term deposits, such as money funds. Indeed, companies with large treasuries often have dedicated staff managing these investments.

The establishment of a physical cash pool enables treasuries to exercise greater control over cash flows. Ideally, all subsidiaries should participate in the cash pool, as this provides the centre with more information about the daily cash flows that exist throughout the company.

Reduce credit facility requirements. Establishing a physical cash pool means that the treasurer need only negotiate one credit limit for the entire group. This avoids the need for separate credit arrangements to be set up for each subsidiary participating in the cash pool.

The treasury has a high level of visibility over the balances of subsidiaries' accounts in this type of arrangement and can thus control the disbursement of cash. A subsidiary experiencing cash shortfalls can be funded from the master account at a cheaper rate than could be arranged locally. The treasury should be able to reduce borrowing costs significantly by using the balance aggregation to arrange inter-company funding.

Disadvantages

Inter-company loans created. The physical movement of cash between accounts creates a series of inter-company loans between the master and participant accounts.

This can have complex implications, particularly with regard to:

Withholding tax. In some countries, withholding tax may be levied on inter-company loan interest. This is because tax authorities regard the payment of interest on inter-company loans as an inter-company payment rather than as a bank payment.

Thin capitalisation. In some countries thin capitalisation rules apply – these restrict the level of financing a subsidiary can receive from its parent/major shareholder. Companies are often able to offset the cost of such loans by deducting the interest charged as an expense for income tax purposes. In order to prevent abuse of this advantage, many countries have introduced thin capitalisation rules.

The ratio of debt to equity a company is allowed before it is classed as being thinly capitalised varies considerably from country to country. Thin capitalisation levels need to be closely observed when running a physical cash pool to ensure that the redistribution of funds from the header account amongst the subsidiary accounts does not breach these rules. This is of particular concern when cross-border cash pooling is implemented.

Legal issues. The transfer of monies between a company's subsidiaries creates legal issues due to the co-mingling of funds. Care must therefore be taken with the structuring of inter-company loans to ensure that they are legal. Often separate credit agreements will need to be put in place for each loan.

Higher banking costs. The physical transfer of cash between accounts will incur high banking costs, particularly if a large number of movements takes place and/or cross-border transfers are involved.

Cash flow forecasting. The master account will fund any cash shortfalls and invest in surpluses on a daily basis. Some degree of cash flow forecasting will therefore be required to manage these positions effectively.

Concentrated banking arrangements. Most cash pooling arrangements require that all participant accounts are held with the same bank. This may cause problems for companies with operations in many countries – a bank which is strong in one country may offer a more limited service, or indeed no service, in another.

Variations on the theme

Zero balancing. Cash movements into and out of the header account are structured so that all subsidiary accounts are left with a balance of zero. Typically, zero balancing cash pools operate on an intraday basis, with sweeps occurring daily (usually at the end of the working day). The net balance in the header account is therefore available for overnight investment.

Target balancing. In this arrangement, cash sweeps are arranged so that accounts in the pool are left with a pre-determined target balance after the sweep. Different target balances can be set for the constituent accounts in the pool. In fact, it is often possible for the treasurer to set negative target balances (ie an overdraft facility) on some of the participant accounts.

Interest reallocation. Some banks allow the interest payable to the cash pool to be redistributed between the participant accounts. The bank calculates the interest payable after balances have been swept from the participant accounts to the header account. Central treasury can, if the net balance of the cash pool is positive, benefit from a 'turn' (the difference between the credit and debit rates) which may be shared with the operating subsidiaries.

Mirror accounts. Some banks offer a service whereby mirror accounts can be set up for the participating accounts in a cash pool. Sweeps on the participant accounts would be booked through the mirror accounts, leaving the operating accounts to function as if they were not part of the cash pool. Each participant account and its mirror account will net to zero after the sweep has been performed. This arrangement can help operating subsidiaries to reconcile their account balances and track the inter-company loans created by the cash concentration.

Digging deeper: notional pooling

Main benefits

Subsidiaries maintain autonomy. As no physical concentration of cash occurs, subsidiaries participating in a

notional pooling arrangement maintain autonomy over their bank accounts and retain their cash balances. The group however achieves similar economic benefits as it would with a physical cash pool.

Less administration. As balances remain with each legal entity (ie no inter-company loans are created), notional pooling requires far less administration than physical pooling.

Lower banking costs. Notional pooling incurs lower fees than physical pooling as the bank operating the pool is not required to transfer cash between accounts.

Disadvantages

Balance sheet enlargement. The balance sheet of both the bank and the company involved in a notional pool can become unnecessarily large. This is because there are no physical cash transfers occurring between the various accounts in the cash pool.

Specifically, a bank offering notional pooling services may find that it is unable to offset fully the debit and credit balances appearing on its balance sheet. This will affect the way in which the bank allocates capital, which will in turn affect the interest compensation paid to the pool. This can become a very important issue as banks have to allocate capital to all their lending. If the gross overdrafts on the participant accounts have to be carried on the banks' balance sheet, there will be a charge to reflect this, which may or may not be made explicitly. This will partially offset the gains that are made.

Legal issues. In some countries notional pooling is prohibited. Additionally, the way in which net interest is calculated may vary from country to country.

Credit facility requirements. Separate overdraft facilities and credit agreements will need to be negotiated for each account participating in the cash pool. This can make managing liquidity across a company more complex.

Main variations

Interest optimisation. This is a limited form of notional pooling whereby a bank offers a company preferential credit and debit rates (ie it returns to the company some of the 'turn' it would normally benefit from). This service is usually offered in jurisdictions where full notional pooling is not permitted.

Margin pooling. This arrangement is a variant of interest optimisation. In a margin pooling arrangement, a bank pays the company the benefit accrued by applying interest optimisation as a separate fee. The service allows for a bonus determined by the ratio between the debit balances and credit balances of the participating accounts. In effect, this operates as a sort of 'loyalty scheme' – the greater the offset between accounts, the larger the benefit paid to the company.

Other pooling arrangements

Single legal account pooling

A form of cash concentration, in this arrangement a company maintains only a master account with a bank. This master account – which is generally managed by the group treasury – contains all the company's cash and is effectively an in-house bank.

The bank maintains sub accounts for all the entities participating in the cash pool. These accounts are used by the group's operating subsidiaries as if they were not part of a cash pool (so they control their own balances). However, all transactions on the sub accounts are booked to the master account. The master account is thus a summary account for all activity occurring in the sub accounts. The bank calculates interest on the master account balance, although this can often be allocated to sub accounts.

Single legal account pooling is not especially widespread, being mainly offered by the Nordic (and some UK) banks.

Reference account structures

Reference account structures are a method of including the accounts of subsidiaries which are not officially a part of the cash pool in a pooling arrangement. Subsidiaries may be unable (eg for legal restrictions in place in their home country) or unwilling to participate in a cash pool. In this arrangement, each subsidiary has – in addition to its normal domestic operating account – a reference account in the central pooling location. Balances on the local operating accounts are manually or automatically transferred to the subsidiary's reference account in the central pooling location. These balances will then be notionally pooled, allowing for the full offset of debit and credit balances.

Overlay cash pool

An overlay cash pool isn't necessarily distinct from a notional, conventional target or ZBA cash pool, but could contain components of all three. It is a cash management service that facilitates the aggregation of liquidity from a series of multiple underlying banks or accounts into a single bank or banking structure. This could be within a single bank, but typically an overlay structure refers to a multi-bank structure.

Where balances are held at two different banks, the cash has to physically move from the local bank to the overlay bank. This can be done by the corporate instructing its local bank to push the funds to the overlay bank – where every day at a particular time the bank pushes excess cash into the overlay bank account structure. The alternative is for the overlay bank to pull the cash from the local bank at a predefined time and within certain parameters.

A virtual alternative

Given the potential for regulatory issues around the structure, an alternative to notional pooling is provided by virtual accounts. These have already been deployed for the streamlining of collections. By opening virtual accounts for each entity within a group and appending sub-level virtual accounts to these, clients of those entities can effectively remit to a central account (whether national, regional or global) using their own unique virtual account identifier. Like notional cash pooling, virtual accounts could enable corporates to allocate cash without segregating it physically.

By integrating virtual bank accounts with administrative sub-accounts called virtual ledger accounts (which populate a multi-bank cash management dashboard), a new type of liquidity management tool is created, allowing full cash concentration and visibility right across the group.

Capital structure: the cash conundrum

In the last edition of Treasury Today Asia, I wrote about how efficient cash management leaves open the question of what treasurers should do with the cash concentrated through their balance management efforts. Recently there has been more press about whether corporates' excess cash means working capital and cash efficiency no longer matters. Efficiency emphatically still matters – here's why.

Capital structure is one of the basic elements of any business set up because the capital structure determines the business' risk capacity. Other than rent seeking, risk is a prerequisite for reward (and even rent seeking carries political risks).

Traditionally capital structure is part of business resilience and sustainability. Businesses need a mix of equity, debt and cash to protect the business from adverse change – this is partly a board level management decision and partly a matter of market inputs since the weighted average cost of capital (WACC) curve gives the optimal leverage for the business.

Simply put, equity is risk free in the sense that it never has to be repaid but it is very expensive. And debt is riskier because it must be repaid and interest payments must be paid on time but it is cheaper and additionally interest is tax deductible (whereas dividends are not). However, as leverage increases, debt becomes riskier to lenders and its cost rises for the borrower. Longer-term debt is less risky because there is more time to earn cash to repay it but it is more expensive.

Cash is part of a business' financial flexibility – cash saves the business from having to raise external funding in times of difficulty. But cash is very expensive because yield on cash is very low and the cost of funding it is WACC (not the cost of borrowing alone). So investors value modest cash balances for sustainability, but the cost of high cash balances exceeds their benefit in terms of lower WACC.

The agency problem that is at the heart of businesses with shareholders is also addressed by appropriate capital structure – shareholders and the board (who are supposed to represent them) can "keep management honest" by requiring high leverage relative to the business risk and low cash.

Corporate cash exceeds USD$5trn globally

Given the traditional approach to capital structure, how can we explain the huge amounts of corporate cash that is reported in the news so much? And why are investors tolerating such seemingly inefficient levels of cash? Here are some factors:

- Fragmented market: corporate debt is also very high, so looking at net cash may reduce the apparent anomaly; further it seems that the excess cash is very concentrated in tech and pharma, so it may be inappropriate to generalise.
- Subpart-F: US corporates leave cash abroad because it would be taxed 30% on repatriation; or they wait for tax holidays that come once a decade – hence the large tech companies having huge cash balances (abroad) and borrowing cheap debt (in USA) to fund share repurchases.
- GFC: the global financial crisis, which caused liquidity fears in many markets, may have scared corporates into holding more cash as (albeit expensive) self-insurance.
- Rise of knowledge businesses: there is evidence that high R&D businesses need and keep more cash than traditional asset heavy businesses; an interesting NBER paper suggests that tech start-ups use more cash initially and may return it when they turn cash-positive.
- Competitive advantage: some researchers find that high cash buffers confer a competitive advantage to businesses and further discourage competitors with less cash.
- Governance: investors may be tolerating high cash levels – at least in developed countries– because they trust management (relatively) more than alternatives; a related view is that since managers have better information than investors they may be able to generate higher returns for the cash.

It may also be possible that the trend is reversing or at least stabilising. News reports indicate that other businesses with large cash reserves may follow Apple's lead in returning excess cash to shareholders – this is in the context of Apple repatriating US$252bn to take advantage of the current US tax amnesty. In this period of exceptional profitability and cash flow, businesses may be feeling less need to hold large cash buffers.

In summary, we can observe that at least some businesses are holding historically unusual cash balances that we cannot explain with traditional economic and corporate theory.

Finding the right capital structure

Treasurers are now faced with a conundrum – the traditional tools for determining an appropriate capital structure may no longer be working and new generally accepted practice has not resolved to replace them.

In principal – at least for public companies – letting the market provide answers would seem the logical choice. However, treasurers will be rightly reluctant to run experiments in the markets with their capital structure.

Fortunately, simulations can stand in for market experiments. One common solution is to use rating agency methodologies to find an effective capital structure, based on the not unreasonable notion that rating agencies reflect market norms. In fact, enlightened boards often specify a target rating to their treasurers rather than specific quantitative limits. Another alternative is to ask investors what they expect from the business in terms of capital structure. And of course, there is always the old standby which is following peers.

Whatever cash level or range is decided by the board should be followed by treasury. In good years or quarters, cash in excess of the decided range (or implied by the target rating) should be returned to shareholders.

Working capital and cash management

Large cash holdings come in part from tight working capital and cash management. They are not a reason to loosen capital efficiency. As quoted earlier, cash is, from an investor perspective, a liability. Investors know that profits are illusory and that value for them is generated from cash flow – so they will continue to focus on cash efficiency regardless of cash balances.

Investors value capital-efficient businesses higher than inefficient ones, so the focus on capital efficiency remains critical. There are many suitable metrics available (ROIC, RONA, EVA and NWCR) – it matters less which one is used than that one of them is used to keep the focus on capital efficiency throughout the business.

Investing cash

Once the board has determined either directly or by specifying a target rating the target cash range, treasury needs to invest the cash appropriately. Invariably treasury's investment objectives are: safety (preservation of capital); liquidity (availability of funds; and yield (interest income).

In that order. In fact, several surveys show that treasurers put 60% of their effort into safety, 30% into liquidity, and only 10% into yield. The emphasis is firmly on maintaining access to the cash rather than profiting from it (because cash is a huge cost in any case when counted against WACC).

Treasurers have a range of investment products that can be used to safely store cash, including: bank deposits; money market funds; supply chain financing; segregated accounts; and self investing.

Bank deposits

Bank deposits are becoming less easy with the advent of Basel III and especially NSFR and LCR which mean that banks are reluctant to take short-term deposits. When a bank deposit has to be committed for 60 or more days, treasurers are not meeting the liquidity objective stated earlier.

One interesting development from these regulations is that banks are remunerating current account balances that qualify as operating cash with deposit like rates, so that doing nothing with your cash becomes an attractive option. Of course, leaving cash with banks (whether in deposit or current accounts) represents a risk concentration that may compromise the safety objective stated above.

Money market funds (MMF)

MMFs have become increasingly popular with treasurers because they offer good risk diversification and high liquidity (often same day availability and routinely next day availability). This popularity is enhanced with the regulatory challenges of bank deposits above.

Regulations are also affecting MMFs. Treasurers prefer CNAV funds but regulatory and accounting pressures are pushing the industry towards VNAV funds which create more accounting complexity and can generate accounting classification issues.

Supply chain financing (SCF)

Cash rich businesses are increasingly deploying their cash to support their supply chains with techniques like dynamic discounting. The effective yield and relatively low risk are attractive but there may be difficulties with the liquidity target (cash tied up in shorter accounts payables cannot easily be liberated and disrupting suppliers may be disruptive to the underlying business) and the impact on working capital metrics (shorter accounts payables) may not be flattering unless well communicated.

Segregated accounts

Segregated accounts often seem like an attractive and tailor-made solution, but they are only viable for very large cash balances, for example over US$100m.

Self investing

Only the largest treasuries can justify the expense and managerial overhead of running investment operations in house. Further, it is difficult to get risk diversification with any but the largest balances – and this problem is resolved with MMFs which can be thought of as a way to outsource investment to more professional larger scale institutions.

Conclusion

Capital structure and the consequent cash level decisions have become more complicated in the current low interest rate environment. This may prove to be the new normal but for now treasurers do not yet have established models and maths to guide them. Nonetheless, tight working capital and cash management remain critical for firms because investors need to be paid from cash flow. Determining the appropriate cash levels and communicating them to investors is a key foundational element of treasury and indeed business effectiveness. Cash investment remains a non-core activity focussed on damage limitation rather than yield.

David Blair, Managing Director

Twenty five years of management and treasury experience in global companies. David Blair has extensive experience managing global and diverse treasury teams, as well as playing a leading role in eCommerce 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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The views and opinions expressed in this article are those of the authors

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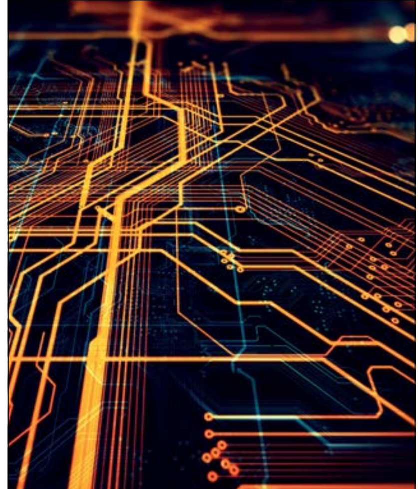
INSIGHT & ANALYSIS

The death of cash… again

Many experts have prophesied the death of cash for some time now. Yet, in 2018 paper notes and metal coins are used daily in every country in the world. In fact, statistics show that there is more cash in circulation today than ever before. Despite this, there is a clear drive from governments, banks, corporates and even individuals to move away from cash. Accelerating this is the wave of innovation sweeping over the payments space that is making storing and using digital cash cheaper and easier. And let's not forget about the cryptocurrency revolution.



TECHNOLOGY

Treasury on a budget

Every treasurer wants access to best in class technology to help them run their operations more efficiently and reduce risk. The problem is that this technology is not cheap, making it out of budget for treasury teams being asked to operate on a shoestring. This does not mean that these treasury teams cannot obtain many of the benefits offered by more advanced technology, however, it just requires a little more creativity. Treasury Today Asia tells you how you can build a best in class treasury technology stack on a budget.

INVESTING

Security, liquidity or yield

Managing surplus cash is a core function of any treasury team. As such, it should not be a static exercise and strategic treasury teams should be constantly re-evaluating their short-term investment options to ensure it matches the objectives of their organisation. In this article, Treasury Today Asia finds out how corporates around the region are investing their surplus cash and how this may evolve considering the changing regulatory and monetary forces.

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

Malcolm Andrews, Treasury Manager, SEEK; Amit Baraskar, Vice President & Head – Treasury, Thomas Cook (India); Tim Bartlett, Senior Liquidity Commercialisation Manager, HSBC; Aman Singh Chadha, Asia Pacific Technology, Media and Telecoms Sector Sales Head, Treasury and Trade Solutions, Citi; Allison Cheung, International Tax Partner, PwC Singapore; Vincent Couche, Asia Pacific Industrials Sector Sales Head, Treasury and Trade Solutions, Citi; Jeff Dart, Assistant Treasurer, SEEK; Shannan Fort, Cyber Product Development Leader, Aon; Paul Gruenwald, Chief Economist, S&P Global Ratings; Shirley Inscoe, Senior Analyst, Aite Group; Kojima Isao, Head of Transaction Services, Japan, J.P. Morgan; Kaoru Ito, Director, Deloitte Tohmatsu Consulting; Rohit Jamwal, Asia Pacific Consumer and Healthcare Sector Sales Head, Treasury and Trade Solutions, Citi Shveta Kapur, Associate Director, Treasury, IndiGo; Tony Kinnear, Managing Director, ASEAN and North Asia, Thomson Reuters; Rakesh Kochhar, Senior Vice President, Global Treasury and Global Sales Finance, Nissan; Louis Kuijs, Head of Asia Economics, Oxford Economics; Christopher Lee, Analyst, S&P Global Ratings; Todd McElhatton, CFO, SAP North America; Nikki Mullins, Senior Manager, PwC Singapore; Anthony Osentoski, Head of Corporate Treasury and Insurance, Asia Pacific, Solvay; Sandip Patil, Asia Pacific Global Liquidity and Investments Head, Treasury and Trade Solutions, Citi; Ernesto Pittaluga, Asia Pacific Sales, Head, Treasury and Trade Solutions, Citi; Carl Sharman, Director, Treasury Advisory, Deloitte; Tim Waggett, Asia Pacific Energy, Power and Chemicals Sector Sales Head, Treasury and Trade Solutions, Citi; Steve Wiley, Vice President, Treasury Solutions, FIS; Julia Wu, President of J.P. Morgan Chase Bank China and Head of Corporate Banking, J.P. Morgan China; Sam Xu, Head of Transaction Banking, China, Standard Chartered.

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