March/April 2024

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Sustainability in the cloud

Data centres try to cut emissions.

The Corporate View

Wee Teck Lim

Senior Treasury Manager

Women in Treasury

Michelle Ang

Group Treasurer

Mitsubishi Fuso Truck and Bus Corporation

Cash Management

Filling the gaps in cash and transaction consolidation

Funding & Investing

Asia's corporate indebtedness turns a corner

Payments

Challenges with payments data monetisation

Technology

Digital sovereignty moves up the agenda

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treasurytoday.com
Volume 12/Issue 2
March/April 2024

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© Treasury Today ISSN 1466-4224

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

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

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

Physical realities in a digital world

Digitalisation is a megatrend that cannot be ignored; we all live in a data-driven world where our lives are increasingly digital. The reality, however, is the digital carries physical consequences. Our data is in the cloud, but it isn't stored in some ethereal receptacle in the sky. Instead, massive data centres are having an impact on the environment. This issue looks at how data centres are trying to cut their emissions in the face of exponential growth in the sector.

The shift to a digital economy is also having an impact on physical national boundaries. In the past trade was in physical goods across clear borders. Now, however, nation states are finding it much harder to manage those boundaries – all of which has implications for taxation and economic protectionism, as well as cybersecurity.

The increase in data is also presenting opportunities for treasurers, who can do more with transaction data – and even monetise it. The reality, however, is that many corporate treasuries still need to focus on the basics and ensure that they have operational efficiencies in place first.

With the rise in data, there is also the opportunity to leverage artificial intelligence for analysis and forecasting. However, with this comes certain risks as there is always the possibility of a 'black swan' event on the horizon. In the Corporate View profile, Wee Teck Lim, a senior treasury manager, discusses how he keeps his mind open to the 'unknown unknowns' and how his approach to risk management has developed over his career.

Also in this issue, Michelle Ang, Group Treasurer at Mitsubishi Fuso Truck and Bus Corporation, shares how she built an international treasury career and gives some stellar career advice.

This issue also has regional pieces, including a feature on treasury in the Middle East and how cash management remains high on the agenda amid budgetary constraints and geopolitical tensions. And in Asia there is hope on the horizon for corporate indebtedness, which has been at concerning levels in recent months.

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Data centre operators say economies of scale, plugging into renewable energy sources and equipment efficiencies will increasingly drive down ballooning energy consumption in the sector. But a lack of awareness and exponential growth is hindering progress.

Michelle Ang

Group Treasurer

FUSO

Michelle Ang discusses her experiences of building an international treasury career at Daimler Group and shares some astute career advice.

Navigating treasury in the Middle East

Cash management remains high on the agenda for treasurers in the Middle East. Meanwhile, budgetary constraints arising from geopolitical tensions are making it more critical to demonstrate the ROI on technology solutions.

Treasurers turn to basics with data monetisation

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Wee Teck Lim

Senior Treasury Manager

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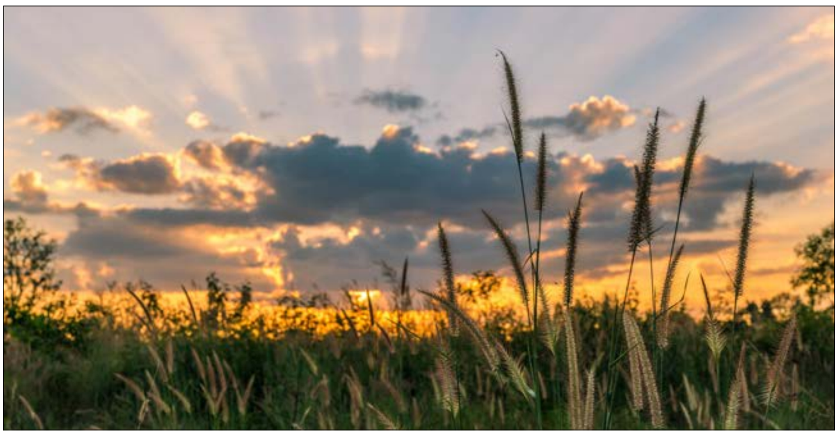

Hope on the horizon for Asia's indebtedness

Worries about the level of indebtedness among Asia's corporates have persisted in the face of higher interest rates and a gloomy macro environment. While concerns remain for the region, there are plenty of reasons to be more positive.

Sustainability in the cloud: how data centres are trying to cut their emissions

Data centre industry executives say economies of scale plugging into renewable energy sources and equipment efficiencies will increasingly drive down ballooning energy consumption in the sector. But exponential growth, a lack of awareness of the industry's carbon footprint and poor emissions reporting is hindering progress.

Remember the days when research involved going to the library to thumb through heavy tomes? Or you put photographs in an album instead of on Facebook – or didn't stream a movie? In a digital world, content is at our – and treasury's – fingertips, increasingly stored in outsourced data centres since the explosive growth of cloud computing. Add to this the fact AI means companies want even more data to crunch to provide the business insights of the future, and our digital footprint grows by the day.

Data centres have transformed productivity. But these giant buildings, densely packed with humming computers on racks, also have a high energy and water use. The IEA estimates that around 1-1.5% of global electricity production supplies data centres and data transmission networks. Other estimates are more worrying. Like energy consultants Baringa's prediction that Ireland's data centres, 75 and counting, could soak up 27% of the national electricity output by 2029.

The data centre ecosystem comprises different players spanning on-premises data centres that house companies own IT systems and hyperscalers, the giant cloud providers like Amazon Web Services (AWS) and Microsoft. Others include colocation facilities (colos) owned and operated by independent providers offering equipment, space and bandwidth for rent and off which cloud storage service providers can piggyback. Efforts are underway to shift the industry onto a sustainable footing, but critics warn many people don't realise it's a sector which uses so much energy.

"People are not aware of the detail," says Prof. Gordon Blair, Head of Environmental Digital Strategy at UKCEH and Distinguished Professor of Distributed Systems at Lancaster University. "From members of the public to captains of industry, they don't realise. When a plane takes off, we hear the roar and know it involves carbon emissions, but technology is ephemeral, and the metaphor of the cloud enhances that."

Sustainability in scale

Treasury Today interviewees argue that large data centres create an economy of scale that is making the industry more sustainable. Data centres use the metric Power Usage Effectiveness, PUE, to calculate the percentage of energy used to cool buildings and run the machines. It shows that most of the energy going into the buildings goes on running the IT. That means opportunities to save energy come from optimising IT infrastructure and the performance of servers, storage and network equipment.

"The best energy performance gains are achieved by consolidation of workload and operating the equipment at higher utilisation levels more of the time," explains Jay Dietrich, Research Director, Sustainability at Uptime Institute in Wisconsin, US. He says much of the growth in data centres is coming from companies moving their IT operations to the cloud and colocation facilities. These companies have typically run their own data centres and are migrating to cloud or colocation facilities because they can't reduce their PUE or they want to minimise capital expenditures.

One beneficiary of that trend is Boston-headquartered Wasabi Technologies, a leading provider of outsourced cloud storage to businesses and governments as well as distributors or channel partners, in turn with thousands of customers of their own. Because cloud systems pool resources, they can use every inch of slack in the system. Data centres pack in the storage and network equipment in efficiently designed cages that stops duplication and increases sustainability, explains Wasabi CFO Michael Bayer.

"It's better to share resources," he says. "Companies are increasingly aware of the costs around IT and systems infrastructure. It's not easy pushing IT out to the cloud, but it is easier than buying new boxes and keeping up investment in-house."

He says the cost of power is a pass through to customers and the benefits of economy of scale are instantly visible in lower bills. "People are thinking about their sustainability footprint," he continues. "Sustainability saves money and being more sustainable can help your bottom line."

Green energy

Singapore-headquartered ST Telemedia Global Data Centres, one of the world's fastest growing data centre providers, currently draws over 50% of its energy use from renewable sources, targeting 100% by 2030. Strategies include investing directly in renewable energy projects. For example, the company has invested in renewable projects in India, benefiting from a regulatory framework that allows it to draw cheap electricity from projects it has invested in. In another project in Berlin, the operator is located directly adjacent to a significant renewable energy project. "As data centres continue to expand, closer integration with green power generation and collaboration with other industries will undoubtedly gain momentum," predicts Jonathan King, Group Chief Strategy and Investment Officer at STT GDC.

Dietrich observers more data centre operators are developing inhouse energy buying teams who have the skills to evaluate energy contracts and are also working with consultants. "There has been an expansion of interest around this," he says. Strategies include operators buying renewable energy in one market and using the guarantee of origin to offset power from fossil fuels in another.

But as data centres become increasingly significant buyers of renewable energy, they are also attracting criticism for reducing the availability of renewable energy for others. Facebook is one of the largest corporate buyers of renewable energy, with contracts in place for more than six gigawatts (GW) of wind and solar energy located on the same electrical grids as the data centres they support.

Moreover, accounting and reporting emissions is challenging. Positively, King observes an increasing awareness amongst STT GDC's customers regarding what they are drawing from the grid versus actual utilisation, driven both by cost efficiency and the need to account for carbon emissions. However, he says the carbon accounting industry is still developing, and further, industry-wide progress will be an important step forward to effectively managing emissions in the data centre industry.

Identifying where the energy is coming from is a complex business for companies like Wasabi that don't own or operate their own premises. "We don't have visibility on the level of renewables in their energy mix because sourcing power is the remit of the co-lo. We can get some visibility, but it's hard to measure, and changes through the course of the day."

It reflects wider challenges for treasury teams that have outsourced their IT systems and data strategy, trying to get a handle on their Scope 3 cloud operations. Although regions like the EU are tightening reporting on Scope 3, it is complex and characterised by poor levels of reporting and transparency.

"One of the biggest challenges to reducing emissions from the cloud is the lack of transparency. Few companies properly count Scope 3, and the lack of transparency allows companies to make it up," says Blair who calls for speeding up the introduction of legislation that will standardise rules on the accounting and methodologies to assess carbon footprints as part of a company's accounts. "Every single large company has pledged net zero but are they confident they will achieve it or is it just a marketing slogan? We don't know because we don't have the numbers."

Sustainable investors

Wasabi's lender cohort are increasingly pushing sustainability. In 2022, the company completed its fourth round of capital raising, expanding its funding base from primarily family offices to more institutional finance and regulated lenders that are hiring consultants to ask deeper questions on sustainability, and Wasabi's carbon footprint.

Like requests for a breakdown in the energy bills the company is charged by the co-lo's it uses to get more visibility on emissions. Or investor requests to separate power bills, space bills and networking bills. "We've definitely started to get more questions. Carbon emissions are now part of the dialogue; it wasn't five years ago," says Bayer.

STT GDC has committed to be carbon neutral by 2030 and has developed a Sustainability-Linked Financing Framework allowing it to access green financing linked to KPIs like renewable energy usage, carbon intensity reduction and increasing the number of Green Data Centres.

To date, the company has raised US$500m through this facility, but King flags room for further growth in the green financing market. "While the industry is progressively embracing green finance, it has yet to reach its full potential. The market's evolution is ongoing; it entails more than just meeting key performance indicators to attract green funds at a lower cost," he says.

Dealing with waste

No conversation about a sustainable data industry can ignore the issue of waste. Data is the new gold and companies are afraid to throw it away. AI has made data more valuable on the premise it will feed the models that will drive innovation in the future. It means companies are holding onto data they were previously dropping on the floor, even if they have to pay to store it.

Executives say their job is to provide the efficient resources to drive our digital lives in the most sustainable way possible, not get behind the veil of what their customers choose to store. Like a car salesman asking a customer if they really want to buy a car, they say it's not their job to question how much data a client wants to store.

But it's possible we are storing far more data than we need, and this will increase in the future, warns Blair. "A lot of it may never be utilised," he says, citing the reams of satellite data that is being captured by the scientific and defence community that might never be used. "Most data that is accumulated will never be looked at. It's the same as keeping all this stuff in our cupboards that we don't need," he says.

Still, one area data centres are addressing the waste question is via recycling equipment when it is replaced at points in the cycle. This process also benefits from economies of scale, says Bayer who says Wasabi's hundreds and thousands of servers with a five-to-seven-year life can be recycled easier than a company with say, five servers. "It is much easier to work with vendors to retire that volume of equipment. We can do it more thoughtfully than just put it in landfill."

Innovations

Innovation in the industry is also set to improve sustainability. For example, King notes that the design of buildings can help limit water use, for example a closed loop system means it doesn't constantly draw water but uses a fixed volume that recirculates. "It is essential to recognise the water scarcity, which may be even more pronounced," he says. "We're also implementing liquid cooling strategies, including immersion cooling, to allow our data centres to support the increasing power density (and heat emissions) from AI/High Performance Computing workloads. These strategies are critical to deliver responsible digital infrastructure in a highly sustainable manner," explains King.

STT GDC is also using AI in its data centre operations to optimise cooling infrastructure and manage the heat generated from the servers. The smart processes include automatically adjusting the cooling infrastructure based on environmental factors to further improve PUE. "We have established an R&D team in Singapore exclusively dedicated to initiatives like this, ensuring that every precious kilowatt drawn from the grid is utilised with utmost efficiency."

Industry protagonists argue that data centres will get more efficient with every year of progress. Older generations of data centre assets operate at a PUE of around 2-2.5. "For every 1 MW of power required to power IT servers in a data centre, approximately 2.5 MW needs to be sourced from the grid for these older, less efficient assets," explains King. In a sign of increasing efficiencies, STT GDC has been continuing to lower its PUE even in more challenging climate markets like Singapore, achieving PUE factors in the 1.2-1.3 range.

They argue that the growth curve will flatten, driven particularly by ever more efficient equipment. The industry releases a new generation of products on average every three years that is steadily improving the work delivered per unit of energy consumed. "When these companies buy a new server, they can hopefully consolidate two to 12 existing servers into one new one. Best case, that means taking 11 machines off the floor and dropping the energy use by half or more to do the same amount of work," says Dietrich.

He also believes the gap between facilities groups that buy the power and pay for it, and the IT groups that plugs in and run, is closing. This disconnect, where IT groups have historically focused on reliability, resilience and availability rather than energy use is changing as operators realise they need to be more efficient with their equipment, and save on capital investment if they have to buy fewer servers, in an environmental and business win.

"The case for running systems at optimal levels and streamlining the amount of equipment needed has become a central sustainability. It's carbon emissions you don't have to account for," he says.

Still efficiency drives are also proving challenging. Like the fact servers have a power management capability whereby it's possible to idle parts or turn it off to reduce power. Dietrich notes a trade off with this approach because when operators begin turning off functions, it takes longer for the system to communicate at the speed it's meant to, impacting a variety of workloads.

And for all the efficiencies, Blair remains concerned about the 'Rebound Effect' where history tells us that continued efficiencies just continue to drive growth. "As soon as we save, we do more. We save, we invest, and the industry gets bigger. If you look at the statistics, carbon emissions from technology are not dropping. The world needs to slash carbon emissions over the next couple of decades and a gradual decrease won't halt the climate emergency," he concludes.

SHOEMAKER'S TREASURY TEAM HIT THEIR STRIDE

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Christian Louboutin has taken major steps to improve the efficiency of its treasury operations by centrally managing intercompany transactions.

With more than 150 boutiques in 30 countries across Europe, North America and Asia, Christian Louboutin has become synonymous with high-end women's and men's shoes as well as bags and other accessories over the last three decades.

Primary shipment flows are completed by the company's master distribution entity. That follows a specific process, but merchandise can be transferred between locations to meet customer demand, resulting in a web of intercompany invoices to account for the movement of goods.

As the company continued to expand, tracking the financial impact of these transfers manually became increasingly time-consuming. With each transfer, the sending entity would invoice the receiving entity and then wait to be paid. There were no standardised processes or procedures to manage intercompany settlements or to resolve (or escalate) disputes between the two parties and the treasury team didn't have sufficient visibility into the exact number and scale of all the transfers taking place each month.

"The time had come for us to gain more control over the impact of intercompany transfers," explains Annabella Lopes, Senior Treasury Manager Credit Risk & Netting. "With 150-plus stores it had become too inefficient to try to centralise – and rationalise – all these flows using manual systems."

Key objectives included implementing an automated reconciliation and settlement solution to alleviate friction and manual effort, eliminate neglected transactions, and gain full visibility into those processes.

The ability to implement an API interface with the company's ERP system was a strong factor in the solution selection process. The data is now automatically uploaded via an API for reconciliation and settlement for affiliates using the ERP system (for some entities not using this system, the upload is completed via CSV file).

"Even though we run monthly AR-driven netting, both AR and AP invoices are imported into the netting solution to facilitate the matching and reconciliation of intercompany transactions," says Lopes. "The treasury team defines a calendar at the beginning of each year that specifies cut-off dates for every step in the process from upload to discussion and dispute to settlement."

The automatic interface runs on these specific dates so everyone understands invoices need to be entered within that timeframe, or they will wait until the next cycle to be paid.

"In addition to matching virtually every invoice for quick and easy settlement, this modernisation has helped us save hundreds of thousands of euros for financial year 2023," says Lopes. "These savings are a result of a reduction in FX transactions, bank transaction fees and float – with a precise settlement schedule, float is no longer a factor in intercompany payments. On average, we are now converting more than 120 monthly gross flows into fewer than 25 net flows."

To date, 31 Christian Louboutin entities across the Americas and Europe are using the system to enter more than 3,500 invoices per month in eight different currencies, observes Emeline Marchand, Netting and Credit Manager. "Throughout this transformation and after a lot of clean-up of transactions backlog, we are now at nearly 100% matching during each settlement cycle," she adds.

The various accounting teams refer to how easy the system is to use, allowing precise prediction of settlement dates and easy reconciliation if there is a mismatch between entities.

"Coming from a manual process with a lack of visibility, we are now in a system where we have complete control," says Marchand. "We will be expanding it to Asian countries and adapting to local regulations and constraints to achieve even greater visibility of intercompany flows."

This much I know

Michelle Ang

Group Treasurer

FUSO

Part of Daimler Truck AG, Mitsubishi Fuso Truck and Bus Corporation (MFTBC) is headquartered in Kawasaki, Japan. The company, which has around 10,000 employees, manufactures trucks, buses and industrial engines for over 170 markets around the world. MFTBC also serves as a development centre for electric and autonomous drive technologies within the larger Daimler Truck Network.

How did you arrive in your current role?

I graduated with a degree in accounting and started off with what was then one of the big six accounting firms – but I was never really satisfied with just looking at financials historically and closing the books. I moved into other industries, like banking and securities, before I finally joined a management associate programme ran by the Daimler Group. It was a two-year programme which provided a holistic view on the industry, with exposure to different functions, and at the end you could decide which function you'd like to consider for your longer-term career.

What advice would you give women in terms of establishing a career in finance?

If you've just graduated and don't know which industry you'd like to join, my recommendation is to go to an organisation whose purpose shouts out to you, rather than zooming in on a particular role. Beyond whatever your degree or your education might be, it's about understanding where this company sees itself, and whether you identify with the values of that organisation.

Which factors are most important in helping women achieve their career goals?

It's really about the hunger you have, in terms of pushing yourself out of your comfort zone, as well as about flexibility – for example, if you had to relocate to gain a particular experience, would you do it? There's no right or wrong, but these two aspects have been a constant in my career. I've also had some great mentors who have helped me achieve my goals, so I've been very fortunate.

What is your favourite motto or greatest inspiration?

At the start of my career, it was 'never say never', or 'the best is yet to come'. But at this stage of my life and career, it's really 'lead with a position of love and kindness'.

Often in the boardroom, people have a mindset of 'winner takes all', but I believe any great leader has to come from a position of love – meaning you need to love what you do and love the people that you're trying to nurture to be the next leaders. You also need to have a love for your society, otherwise all these ESG goals are just more KPIs that you need to report on. When you come from this position, profits automatically follow because you're making decisions that have a long-term effect.

> "It really doesn't matter what role you get within the organisation – in a larger organisation, you have the chance to move around relatively easily."

ONLINE

To read all the interviews in this series go to treasurytoday.com/women-in-treasury

Finding the right fit

When it comes to creating a career plan, Michelle Ang believes a flexible approach is more important than focusing on specific roles. "I had a defined career plan, but none of it turned out the way I planned," she laughs.

While people's priorities are inevitably different at different life stages, Michelle says the most important career advice she can give to younger women is to find an organisation that aligns with their values. "I think it really doesn't matter what role you get within the organisation – in a larger organisation, you have the chance to move around relatively easily, and depending on the footprint of the organisation you may be able to build an international career," she reflects.

For Michelle, applying to a management associate programme at Daimler Group proved to be a defining moment in her career. Following a detailed assessment process for candidates around the world, she was awarded a place on the two-year programme. "I started my journey, and never looked back," she says. "Asia was very much a growth region, so I had the benefit of working there as the team grew. The programme really benefited me, as I felt that I was part of a bigger purpose at the company, and that I understood it from day one."

During Michelle's time at Daimler she has worked in Australia, China, Germany and Singapore. Then, in 2021, following the successful spin-off of Daimler Truck from Daimler AG (now Mercedes-Benz AG) she took up her role in Japan and worked on various corporate finance transactions for the Group.

Becoming a role model

Turning to the topic of inclusion and diversity, Michelle notes that her experiences have been very different across the five countries in which she's worked. "I think there are some places where it`s second nature to articulate your views, but there are also other locations where women need to feel safe that they can articulate their views," she adds.

> "People are attracted to individuals whose values, behaviour or path in career and life reflect their aspirations.

In Japan, Michelle observes that young female employees seek out female role models within the workplace or industry that they can identify with. "People are attracted to individuals whose values, behaviour or path in career and life reflect their aspirations. This attraction coupled with some curiosity is a great conversation starter for exchange of views and opinions and shaping a 'Speak Up' culture. At Daimler Truck Asia, we have various Human Resources led programmes that support inclusion and diversity."

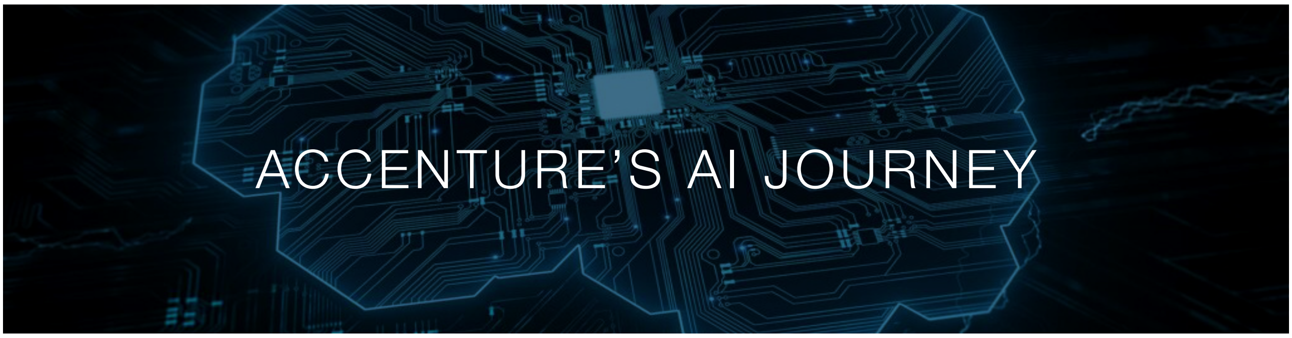
When it comes to helping others navigate challenging or uncomfortable situations in the workplace, Michelle has a further piece of advice to offer. "Approach criticisms received from a position of curiosity. Try to detach yourself from being the object of negative criticism. Use phrases such as – 'I'm sorry, what did you say? Could you help me understand what that meant?'"

While this approach can take some practice, Michelle says it provides a way for people to detach themselves from a particular issue, find out whether a comment has been misconstrued, and shape the dialogue in a constructive way. She adds, "You don't have to get personal about feedback, but you do need to understand why that feedback was given, and to do that in an open-minded way."

Profile

Michelle Ang has close to 25 years' experience working for the Daimler Group, and previously held leadership positions in Australia, China, Singapore and Germany before assuming her role as Group Treasurer, MFTBC in 2021, based out of Tokyo. In her current role, she is responsible for shaping the group's banking, financial markets and investment strategy across Japan, China, India, Australia, Singapore, South Korea, Taiwan, Indonesia and Thailand.

In 2023, Michelle was the Highly Commended Winner of Treasury Today's Woman of the Year APAC award.



ACCENTURE'S AI JOURNEY

Onkar Liddar, Assistant Treasurer & Managing Director at Accenture explains how the consulting group is integrating AI in its treasury function in step-by-step process.

Accenture's treasury is based on SAP which runs alongside the ERP of the organisation. This has been an important baseline in the company's digital journey because it has created a single instance data lake or source of truth the team can trust and has enabled it to leapfrog into using advanced technologies.

Accenture has begun by developing what it calls intelligent cash. This has three components, the first of which is a comprehensive dashboard, easily available to everyone in the finance function, which lays out where its cash is and in which currency; with which counterparty or if treasury has a cash holding that doesn't align with its guardrails.

The second element comprises forecasting. In the past, forecasting would involve taking historical data and streamlining it.

"Now we use sophisticated algorithms developed by our own data scientists and consultants applied to each individual cash flow around, say, accounts payable, receivables or tax. The machine learns and evolves its algorithms, and our latest GBP forecast was spot on for the short and medium term – it forecast what actually happened. The machine is so sophisticated it can forecast better than our people have historically been able to do," he says.

Forecasts lead to the third component where the technology is helping Accenture take business decisions and decide the best course of action. "For example, it tells us whether to reduce our holding in a particular currency, taking into consideration its own forecasts and external data sources like the FX rate. The machine does the grunt work and people can spend less time on operations and more on thinking about risks that could happen. It also speeds up the velocity of our cash, and treasurers always need money to move quickly and without friction," he explains.

There are already many companies that profess to sell the perfect intelligent cash tool but Liddar says he hasn't seen a fintech out there yet that can really do this.

"Tools like SAP can facilitate it, but the risk with using fintech is that treasury ends up tailoring its process to fit their model, rather than the other way around. Treasurers are also mindful of how much data they send to a third party to process on their behalf because fintech and technology like ChatGPT requires putting data in the public domain and this is not the right approach for a corporate treasurer. The technology is also developing so fast, tools are unlikely to keep pace with changes in the market. Still, treasurers can't integrate AI internally and in isolation because it is complex and they have such a busy day job, so the best approach is to use trusted advisors with a proven track record."

Treasury can't operate on systems alone; it is a context-based discipline and experts will always be required to make final decisions, he continues. What AI gives treasury is an opportunity to upskill people in an environment that is becoming increasingly challenging. "Take our growth for example, as the business grows, our exposure to currencies, bank accounts, partners and integration work (Accenture is very acquisitive) makes having the right money in the right place at the right time increasingly challenging."

Liddar says he envisages a point in time where the team can engage with the technology using prose. The machine will suggest courses of action and identify issues, and treasury will also be able to instruct it. "Once we have identified risk and interacted with it, we will be able to instruct it to exchange this currency; issue a bank guarantee, downsize debt, or increase a bond offering. The tool will carry out the transaction and manage the accounting in the background in a utopia for busy corporate treasurers."

He says treasurers need to determine where they stand in terms of technology, conscious it is fluid and changing so fast that they don't tie themselves in. "My advice is to set out a clear roadmap for how you want to operate in the future and start building towards that goal. AI is a fast-moving space; it will be as impactful to how we operate today as was the loom in the industrial revolution. It is transforming our industry," he concludes.

Navigating treasury in the Middle East

For treasurers in the Middle East, cash management continues to be high on the agenda. At the same time, budgetary constraints arising from geopolitical tensions are making it more critical for treasurers to be able to demonstrate the ROI on technology solutions.

Located at the intersection of Europe, Asia and Africa, the Middle East has a population of over 370 million people, with its largest economies including Saudi Arabia, UAE and Turkey. The region is famed for its rich cultural history, as well as for its modern architecture, low taxes and abundant oil and gas reserves.

In recent years, significant efforts have been made to diversify the region's economies away from hydrocarbons. In 2016, for example, Saudi Arabia launched its Saudi Vision 2030 roadmap, the goals of which include diversifying revenues and establishing Saudi Arabia as a global hub connecting three continents.

Meanwhile, the Middle East continues to be affected by geopolitical tensions and upheaval, including the Israel-Hamas war. Despite this, tourism in the Gulf Cooperation Council (GCC) – a political and economic alliance of six countries in the region – is experiencing robust growth, led by the UAE and Saudi Arabia.

Treasury landscape

For treasurers operating in the region, the region presents both challenges and opportunities. For one thing, the maturity level of treasury practices varies between countries, explains Irwin Medford, Director, Treasury Advisory at PwC in the Middle East.

"For example, in the UAE, and particularly in Dubai and Abu Dhabi, the markets are more mature," he says. "As well as focusing on cash and liquidity management, treasurers are becoming more sophisticated and are looking at centralisation structures such as payment factories. Many also have treasury systems in place."

In other countries, including Saudi Arabia and Oman, Medford observes that treasury practices are often in earlier stages of development. "Again, cash management is still high on the agenda, and some entities have dedicated treasury functions. But in some places, you see finance doing some treasury work."

The Middle East is also characterised by the variety of client profiles that can be found there, adds Sleiman El Homsi, Director – Treasury at PwC. On the one hand, the region has numerous family businesses across different sectors, which may be focusing on opportunities for centralisation and rationalisation. "Then in Saudi, specifically, there are 'giga-projects' that are in building mode, striving towards a self-sufficient model, but currently still under the auspices of the KSA central government and its leading sovereign wealth fund."

El Homsi says the relationship between holding companies and subsidiaries is not necessarily akin to a parent/child set up, "but more of a spousal relationship." Medford adds: "In family businesses, you find that some of the subsidiaries are more autonomous than you would probably see in a more international company with a high degree of centralisation."

Growing sophistication

As companies ramp up their activities, says El Homsi, "the sophistication of treasury grows, because it needs to cater not just for cash management, but also for improved bank connectivity, process automation, more effective internal business partnering, and coverage of ancillary activities like trade finance."

For capital intensive clients looking to execute their ambitious investment plans, he adds, "the right competencies need to be sourced or built internally to drive asset-backed financing, which entails more complexity."

Alongside family businesses and government-related entities, El Homsi notes the region also includes many international players, which often choose to set up their treasury operations in the region's two main free zones: Abu Dhabi Global Market (ADGM), and the Dubai International Financial Centre (DIFC).

"We're seeing a trend towards using places like Dubai and Abu Dhabi as regional centres," comments Medford. "The free trade zones are a key driver for companies setting up as regional treasury centres, because they can be a bit more sophisticated in terms of the work they do and the scale of their operations."

Treasury in the Middle East: challenges and opportunities

Nabeel Albloushi, Head of Markets & Securities Services, Middle East, North Africa and Türkiye (MENAT), HSBC Bank Middle East

How would you describe the landscape for corporate treasury in the Middle East?

As a region, the Middle East is witnessing more and more corporates focused on growing their footprint. We continue to see growth in the non-oil sector and positive demographics thanks to the youthful, regional population. Optimism remains strong that the region will continue to perform well in the medium and long-term which, in turn, provides abundant opportunities for corporates to expand or establish their treasury operations in the region.

What do you see as the most significant challenges for treasurers in the region?

Clearly one of the biggest challenges is managing the impact of geopolitical challenges. This variable is something to be aware of and prepared for. Other challenges include liquidity constraints as well as regulatory pressures in some countries in the region. Whilst these produce difficulties for treasurers, the complexity required in tackling them is something specialist treasurers understand.

What are treasurers in the Middle East doing to improve the efficiency of their cash management activities?

Treasurers have an abundance of options these days with regards to making the most of their cash. It could be through crystalising higher yields with excess cash or implementing effective, yet simple-to-use cash pooling structures across their regional entities. Investment in technology in this space is ever-increasing and treasurers will continue to gain access to new solutions that match their requirements and make their cash management activities more seamless. Full automation of their FX transactions can now even be applied to their payments and receivables flow, minimising the need for manual input and, therefore, the associated risk of human error.

Cash management and the role of technology

El Homsi says that while different clients have different levels of maturity, a major focus on cash and liquidity management is a common theme. The use of cash pooling is not often maximised, with structures such as cross-border pooling and notional pooling relatively uncommon. Nevertheless, different companies will have different ways of centralising cash.

"For example, we've seen one enterprise that has a regional treasury centre in the Netherlands, and an operating company in Saudi Arabia," he comments. "They include cash in the European cash pool by having that cash go to a local correspondent bank."

With many companies focusing specifically on cash and liquidity management, El Homsi says the way that treasuries approach system enablement "is increasingly becoming modular. They prefer a cost-effective, building block approach, ramping up capabilities in tandem with business requirements, allowing them to simultaneously de-risk the project while also showing some tangible wins along the way."

Indeed, there is a clear realisation that technology will drive significant gains, observes Rahul Daswani, founder of LHD Research in Dubai, who has previously held treasury roles at Microsoft and Nokia. "The challenge is being able to showcase the ROI, as currently budgets are being cut back due to conflict and the wider risk of geopolitical issues spilling over," he adds.

Challenges and risks

Treasurers operating in the Middle East also need to navigate a number of obstacles. For one thing, the availability of trained resources continues to be a challenge for treasurers, notes Daswani. At the same time, he argues that the greater complexity of technology systems and the rapid pace of change "is making it very difficult to make longer-term decisions."

Where financial risks are concerned, El Homsi says that foreign exchange (FX) risk management doesn't tend to be a major consideration, as many companies in the region operate domestically. He notes that the focus tends to be on plain vanilla forward hedging, and not so much on the use of options or other structured products. "It is not uncommon for formal policies on financial counterparty risk management to be absent," El Homsi adds, "while treasury involvement in managing commercial counterparty credit risk is a rarity."

Meanwhile, geopolitical tensions have brought interest rate risk management to the forefront for some companies, "particularly more heavily levered entities, or entities that have ambitious expansion or capex plans." But generally speaking, El Homsi says the decision to hedge interest rate risk is done on an ad hoc basis.

"For most companies, the typical approach is to have around 50-50 fixed to floating," he comments. "If you were to dig down and see how they manage interest rate risk – for example, whether they do the required sensitivities, and look at the impact on debt servicing – these things might be done, but probably not as rigorously as one would want." Likewise, he says that companies tend to focus on the impact of interest rates on debt, without placing much emphasis on the implications for commercial cash flows.

Growth vs efficiency

Despite the challenges presented by the region, Daswani notes that there is nevertheless a significant opportunity for growth. "Most companies are now busy with corporate governance, considering the strong growth seen in the last two years, and this requires them to organise the finance function and set up a dedicated treasury team that is equipped with systems and tools. This requires a lot of investment in treasury management systems (TMSs)."

Daswani says the addition of tax rules has made this even more important, "as intergroup financing now needs to be looked at from an arm's length perspective, and thus in-house bank capabilities become critical." But alongside the growth opportunity, Daswani notes that conflict in the Middle East is resulting in a significant sales impact for many consumer-facing companies, as spend has been pulled back.

"This has led to budgets being recalibrated, and 2024 is expected to be more of a year of efficiency vs growth," he says. "Thus the corporate treasurer and CFO's roles are becoming much harder, as they have to make tough decisions on investing."

Treasurers turn to basics with data monetisation

Opportunities abound for corporates – and their banks – to monetise payments data. For most treasury teams, however, there is a need to turn to the basics and focus on efficiencies and cost savings.

Sometimes it seems that Amazon knows more about you than you do; its analysis of previous purchases can now anticipate your future needs – and wants. Meanwhile, ads on Facebook have become more relevant, Netflix knows what you should watch, and Spotify has the best music you have never heard. Big Tech companies like these have become well-versed in putting customer data to use. And when it comes to payments data, merchants have long been analysing transaction data to reward, and increase, their customers' loyalty. For corporate treasuries, given the volume of transactions they – and their banks – have access to, surely they are also sitting on a treasure trove of data that can be monetised?

With the rise of artificial intelligence (AI) tools, the ISO 20022 payment format, as well as open banking, it is now possible to do a lot more with transaction data. However, the degree to which corporates are able to monetise payments data really depends on the kind of business they are in, says Toine van Beusekom, Strategy Director at Icon Solutions. If, for example, they are data-driven businesses – as with Big Tech companies like Google and Facebook – it is more likely they will be able to monetise their data effectively. "They can monetise data because their business model is selling advertising," Van Beusekom says of Facebook.

Also, Big Tech has been encroaching the space of traditional financial institutions and has been getting into the payments business itself. The approach towards payments, however, doesn't necessarily mean that the transactions will be directly monetised. Alistair Brown, Vice President, Global Head of Open Banking and Payments, at technology provider EPAM, highlights this in a blog about Apple's move into buy now pay later (BNPL) with its Apple Pay Later solution. Apple has also been moving into other financial services, but its motivations are different from traditional banks. With a company like Apple, Brown notes, payments are not a product to be monetised directly but rather a feature of its ecosystem. With payments, the main goal is to increase the reliance on Apple's other products and services and increase users' loyalty. The same goes for Google, where a payment via Google Pay may not directly bring revenue to the company, but if a purchase is made after using the search engine and finding a business on Google Maps, it reinforces the need for those companies to be part of Google's ecosystem and advertise on its platform.

This is just one approach that companies – particularly those that deal directly with consumers – can take with their payments data. For most treasurers, however, the priorities with payments are not what can be done with customer experience and making improvements on the front-end. Rather, the goal is to create efficiencies and make cash and liquidity management more effective.

When it comes to making use of payments data, Kieran Hines, Principal Analyst at Celent, comments that a priority for many corporates is operational efficiency and having visibility of cash. "You can make a lot of improvements with efficiency and managing payment flows if you know where the money is and where it is going to be required. It is far more efficient to have the right amount of money in the right currency, in the right country, when you need it rather than shuttling it around," says Hines.

Sending money across borders or short-term borrowing are not cost-effective ways to cover outgoing payments, especially if data analysis shows it is unnecessary. Take, for example, a treasurer who needs to pay a supplier in Toronto in Canadian dollars. If they have visibility of a Canadian dollar payment that is due soon, they can use these funds instead and avoid the more expensive options.

These issues were covered in a 2021 Celent report, which Hines authored, entitled 'Expectations Versus Reality for Payments Data Monetisation'. A survey of 217 treasurers and chief financial officers in Europe, North America and Asia showed the greatest pain points were the need for accuracy with cash balances and forecasting. Also, treasurers were often having to make decisions based on an incomplete, or out-of-date, picture.

The report showed that the greatest data opportunities for banks wishing to enhance their services to corporate clients lie in providing real-time balances, forecasts, improved security and visibility across bank providers. Rationalising the number of banking partners remains a priority for treasurers, although the average number still remains relatively high. According to Celent, the average number of bank relationships is 9.5, and this figure rises to 13 for corporates with group revenues of between US$5bn and US$10bn. "This creates complications, and it can be hard to manage in real-time how much cash the business has at any point in time," says Hines. Although multi-bank dashboards that provide a consolidated view are available, doing this in real time remains a challenge.

Van Beusekom tells Treasury Today that many of these challenges for treasurers are persistent and many are still focused on getting visibility of their current positions and managing reconciliations more effectively. Some corporates – as Treasury Today's readers will know – have undergone varying degrees of digital transformation, but many are still using Excel spreadsheets and spending their time on manual processes. There has been a lot of focus in the banking

> A corporate does not want an API for this and an API for that.
>
> Toine van Beusekom, Strategy Director, Icon Solutions

industry on real-time payments, notes Van Beusekom. However, what treasurers really want is real-time data.

This echoes what Treasury Today often hears from the treasury community. In a previous interview, Mark Sutton, Senior Manager at treasury and risk consulting firm Zanders, commented that having data-driven real-time vision is a key pillar of the digital transformation that many corporate treasuries are undergoing. Alexander Seelmann-Eggebert, Deputy Regional Treasurer, Asia Pacific at Nestlé commented that his digital aspirations were to reduce operational workflows, increase efficiencies and create data visibility. Meanwhile, Jason Teo, Head of Treasury, Southeast Asia (including Ventures in Korea, Data Centre and Renewables) has spoken of his desire to reduce manual processes and also to bring the treasury onto a single platform for cash visibility and forecasting.

Many banks are clamouring to support corporates in these goals, but when it comes to monetising payments data many financial institutions struggle. In fact, a 2019 report by Aite entitled 'The Payments Transformation Race: Criteria for Success' noted that only 9% of banks were able to monetise transaction data effectively. The report noted that the shift to open banking – where banking services are provided in partnership with others – and real-time payments were drivers of change for banks, and monetising payments data provides them with an opportunity to cement their relationship with their customers, or create new revenue streams.

The use of payments data has moved up the agenda, says Celent's Hines, because of the current migration to ISO 20022 and Swift's drive to adopt the new format. With this messaging format, there is an opportunity to do more with the richer data, says Hines.

With more financial institutions sending and receiving payment messages in the ISO 20022 format, more data can be included with a payment. Invoices can be batched and paid in a single payment, credit notes can be included in a transaction, purchase orders referred to and so on. And for sanctions and anti-money laundering screening, documents can be referred to that show a payment is for a legitimate transaction, for example. The opportunities are endless and corporates are expecting their financial institutions to help them navigate the possibilities. For many banks, providing ISO 20022 solutions is not necessarily a means for them to generate new revenue streams from payments. Rather, providing services related to ISO 20022 will become table stakes for banks, says Van Beusekom, and not doing so is a churn risk. If they don't do it, their competitors will.

There are many opportunities for banks to provide new solutions to corporates based on their transaction data, which in turn will give them a competitive advantage. If they don't make moves to monetise their payments data, they risk losing out. Christian Löw, Partner, Financial Services – Payments, EY-Parthenon Financial Services, in an article writes, "Payment providers that find ways to monetise their vast wealth of transaction data can seize a powerful opportunity to differentiate." He gives some examples, such as an online retailer credit scoring its customers based on payment data and using this to offer services such as BNPL. There are other opportunities for those who don't sell to consumers directly, as Andy Schmidt, Vice President and Global Industry Lead for Banking at CGI notes. He writes in a blog that much of the transaction data that banks have is left idle and could be used to serve customers better. For example, a corporate that is making certain cross-border payments may be overpaying for their foreign exchange. A bank could identify this from the data and alert the customer, offering them a cheaper alternative, for example.

Also, Celent's Hines comments, a closer analysis of transaction data can reveal where a corporate is exposed to certain countries that now carry a geopolitical risk, or the risk may be concentrated with certain banks. "The data is not just useful for cash management and payments – there might be other issues it can highlight such as risk and business continuity," Hines says.

How far corporates rely on banks to help them with their data depends on the size of the corporate. The largest, with around US$10bn in revenues are likely to develop their own solutions so they can access their payments data through APIs [application programming interfaces] offered by their bank partners. For these corporates, the Celent report notes, real-time cash forecasting and real-time cash balances are the greatest needs. For smaller corporates – with US$500m to US$1bn in revenue – they are more likely to expect their bank to provide the services, such as a real-time consolidated view across their accounts and positions.

In an era of open banking, where solutions are available via different parties, the integration of APIs is important, but even managing this can be complex and banks need to make it as simple as possible. "A corporate does not want an API for this and an API for that – it needs to be simplified – otherwise they will do it for themselves," says Van Beusekom.

Looking to the future, as the use of AI and analytics tools are on the rise, other areas also need to be simplified. This is one of the challenges that Zander's Sutton previously pointed to: "Data is the fuel that powers AI. However, most organisations remain heavily siloed, from a system, data and process perspective," he says. This view aligns with Van Beusekom's, who comments that corporates need to get their 'ducks in a row' when it comes to managing their data and have it in a single place. If the data is not well managed, he says, there is only so much that an AI mechanism on top of it can do.

Hope on the horizon for Asia's indebtedness

Worries about the level of indebtedness among Asia's corporates have persisted in the face of higher interest rates and a gloomy macro environment. While concerns remain for the region, there are plenty of reasons to be more positive about the months that lie ahead.

There are many things that seem like a good idea at the time, and being highly-leveraged is one of them. Corporates that gorged on cheap debt when rates were low continue to face an uncertain future as the macro environment, and higher interest rates, have turned against them. For some, with the benefit of hindsight, it now seems their pursuit of leverage was a risky strategy.

Concerns have persisted in Asia in recent months about the level of corporate indebtedness, and the impact that higher interest rates has had on companies' ability to make their repayments. This in turn has led to fears of defaults among Asian corporates. While those issues remain, there is some hope on the horizon and there are several reasons for observers to have a more positive outlook about the months ahead.

A number of economists have pointed out how Asia's corporates have been struggling to repay their debts in the face of rising interest rates. For example, companies, in the ASEAN+3 region [which comprises the Association of Southeast Asian Nations as well as China, Japan and South Korea], are more leveraged than their global counterparts.

In a briefing note on debt sustainability published in February 2023, the Organisation for Economic Cooperation and Development (OECD) noted that Asian corporate debt in 2022 comprised almost half of the outstanding debt on a global level. And Chinese corporates took up a large chunk of this, with 30% of global outstanding debt.

There are other measures that point to the concern around corporate indebtedness. The ASEAN+3 Macroeconomic Research Office (AMRO) points out that the ratio of corporate debt to GDP [global domestic product] for ASEAN was 80.7% while for China, Hong Kong, Japan and South Korea it was 171.6%. This is based on data from March 2023, and AMRO Group Head and Lead Economist, Dr. Kevin C. Cheng tells Treasury Today Asia that there has been no significant change in corporate debt size and maturity since. "The current data suggest ongoing concerns about corporate debt," he says.

The risks are higher for the companies that have shifted away from bank loans towards bond issuance, which leaves them exposed to market risk. As the macro environment has become less favourable, they face the uncertainty about whether they will be able to refinance in the future. "It is noteworthy that over 40% of corporate bonds in the ASEAN+3 region are slated to mature within the next three years," says Cheng.

Although there has been a recent let up in market conditions, there are still concerns that lie ahead. Cheng continues: "The financial market conditions have eased since Q323, but interest rates still remain elevated. As such, floating rate debt liabilities or maturing debts that need to roll over are expected to bear a higher interest burden."

Interest coverage ratios

There has been particular concern about low interest coverage ratios, or the ability of a corporate to cover its debt obligations with its earnings. When earnings are divided by interest expenses, a ratio of less than 2 is generally deemed by many analysts as the minimum level that is sustainable.

In a blog, International Monetary Fund (IMF) economists Thomas Helbling, Shanaka Peiris and Monica Petrescu noted that in the middle of 2022, 17% of Asia's corporate debt was held by companies with a level of below 1. Meanwhile, a third of corporates had interest coverage ratios of between 1 and 4.

A more favourable outlook

Now that corporates are already into 2024, the risk of default has diminished for the months ahead and ratings trends are becoming more positive. Christopher Lee, Managing Director in the Corporate Ratings group at S&P Global Ratings notes, for example, that the number of corporate defaults in Asia dropped from 12 in 2022 to two in 2023.

Regarding the outlook for the remainder of this year, Cheng at AMRO comments that the outlook for corporate indebtedness is influenced by a number of factors. "On the bright side, as private consumption remains resilient, domestic investment recovers and export rebounds, ASEAN+3 is expected to grow faster in 2024 than in 2023. The improving economic prospects will support corporate earnings growth in the region," says Cheng.

There are other reasons for corporates to be encouraged. As global commodity prices come down, inflationary pressures in Southeast Asia and China, Japan and South Korea are expected to ease.

Buddhika Piyasena, Fitch Ratings' Head of Asia-Pacific Corporates tells Treasury Today Asia that indebtedness per se is currently not a huge challenge. Although some sectors are facing headwinds, there are others that are bouncing back from the pandemic and have seen an improvement in their leverage.

"Compared to 2023, our expectations for 2024 and 2025 are very flattish," says Piyasena. He notes there are particular challenges in China's homebuilding sector, as well as the chemical sector. "All the other sectors generally have a stable leverage forecast," he comments.

The commercial real estate sector remains challenging, says Piyasena, although this is a trend that extends to other regions. He adds that in Asia, the issues are not as acute as they are in the US and Europe, for example.

Others point to the continued woes in the property sector as a cause for concern. Lee at S&P Global Ratings notes that developers are prominent defaulters, but it is not just China where this is a problem. Lee highlights Vietnam, Indonesia and also South Korea where there is a greater risk of corporate defaults.

In China, most of the defaults have occurred in the property sector and it is property developers that take up the bulk of negative outlooks. These developers account for 40% of Standard and Poor's corporate ratings that have a negative outlook.

Bright spots emerge

There are, however, some bright spots in the region and reasons to be cheerful. Several observers point to the positive outlook for India and Indonesia. Lee at S&P, for example, says that India has a solid outlook and expects a resilient performance for most of its rated companies. In India, Lee notes, most of the corporates that the ratings agency assesses have limited funding needs and refinancing risks, and also have relatively modest capital expenditure needs. "Balance sheet discipline and strong operating cash flows will likely keep the aggregate debt of rated companies broadly unchanged in 2024," states Lee.

Indonesia has also emerged as a bright spot. The outlook for Indonesian corporates is favourable and Lee notes there is ample banking and capital market liquidity available for larger firms, although this is not the case for corporates with weaker ratings as they struggle to access the offshore bond market. In terms of bank loans, there is plenty of liquidity onshore in Indonesia although the lenders are focusing on less risky loans to larger more stable companies, even though are lower margin, to keep their non-performing loans in check. Lee also notes that the domestic capital markets have become a more attractive venue for corporates.

Preference for local currencies

Fitch Ratings' Piyasena also notes the attractiveness of local markets. He comments that if dollar funding was the only avenue available for corporates, then the current environment would be a lot more challenging. "Thankfully what we have seen in markets like China, India and Indonesia is that the local currency liquidity has been very strong," and many in those countries have been switching to local currency debt, he says. "When companies switch to the local currency they do not have to worry about the currency swap costs."

Piyasena comments that the differential between dollar-denominated and local currency debt remains large. In India and Indonesia, however, he expects the differential to narrow. He also expects to see an improved level of activity in the dollar debt market in those countries – not just with high-grade corporates but also the high-yield segment.

Interest rate expectations

Many corporates were facing difficulties because of the monetary policies of central banks around the world to rein in inflation, and with rising rates, their ability to meet their debt repayments became more strained. Whether corporates can survive the current environment depends to some extent on what will happen to interest rates in the coming months.

Analysts have commented on what they expect to happen. Eunice Tan, Head of Credit Research Asia-Pacific at S&P Global Ratings, explains that the US Federal Reserve has made progress in tackling inflation. However, she does not expect the Fed to cut rates too quickly as consumer inflation is unlikely to fall sharply as economic momentum is strong and labour markets are still tight. She argues that the Federal Reserve will be cautious and other economies will follow this approach. "We expect central banks to take their time cutting rates. They will look at what the Fed is doing, with an eye on their currencies."

Piyasena comments that Fitch Ratings expects the US Federal Reserve to cut its rate in the middle of 2024, which may be followed by three further rate cuts.

Even though a reduction in interest rates is good news for corporates who have been grappling with a rising cost of debt, it is not necessarily the end to their worries. Even if rates do fall, AMRO's Cheng comments that the rates are unlikely to fall to the low levels that were seen in the past decade.

"Interest rates will likely remain higher for longer and though borrowing conditions may ease from current levels, they will stay tighter than those we have typically seen over the past decade," continues Cheng.

Investor expectations

As corporates are hoping for a more favourable interest-rate environment, this will have an impact in other ways. "On the other side, with dollar rates coming down, investors will have to search for yield," says Piyasena. As interest rates rose, there was more of a focus on money market funds, he comments, but as the rates outlook is changing – and rates are likely to fall – some of that activity may return to corporate fixed income.

That money will have to look for a home, and as rates come down investors may be willing to look at other kinds of corporates to invest in. They may not just invest in high-grade US corporates, for example, but may be willing to look at quality high-yield exposure. Corporates with a BB rating could be a sweet spot, adds Piyasena.

For fixed income investors, says Piyasena, there are certain markets that are attractive. China is a slow growth story with the main question being how quickly the government can stem the downside pressures on the economy. Meanwhile, the economies of India and Indonesia remain favourable. "India seems to be a darling for fixed income investors," concludes Piyasena.

With bright spots such as these, the landscape for Asian corporates is not all doom and gloom. While concerns about the level of indebtedness remain, there are still many reasons to be optimistic about the months ahead.

A healthy approach to risk

Wee Teck Lim
Senior Treasury Manager

Managing risk is an essential skill for any treasurer, and Wee Teck Lim has a healthy – and risk-averse – approach that has been developed from the earlier stages of his career. Whether it is protecting the family wealth of business tycoons, anticipating the impact of geopolitical events, or questioning the results of artificial intelligence, the application of sound riskmanagement principles has served him well in his career so far.

In 2002, when Donald Rumsfeld, the US Secretary of Defense, spoke of 'unknown unknowns' regarding Iraq's weapons of mass destruction, he was ridiculed in some quarters for speaking in garbled gobbledygook. He even earned a Foot in Mouth Award by the UK's Plain English Campaign. Others, however, such as psychologists, national security analysts, and riskmanagement professionals, had an appreciation for what he said. "There are known knowns; there are things we know we know. We also know there are known unknowns; that is to say we know there are some things we do not know. But there are also unknown unknowns – the ones we don't know we don't know," Rumsfeld said. To some, this might sound like nonsense, but to others it brings clarity and is a profound way of framing the challenges of risk management.

Over the course of his career, Wee Teck Lim has dealt with known knowns, the unknown ones, and is mindful that the unknown unknowns can wreak havoc on even the best financial forecasts. Lim's skills lie in analysing, forecasting and advising, which he has done in various environments through his career, which has sharpened his approach to risk management. He studied economics and mathematics at the National University of Singapore and, after graduating, he pursued a career in public service, using his numeracy skills in a government statistical research department. This role, however, didn't suit Lim and he felt the time was ripe to point his career in a different direction. "I was interested in banking and finance, and I was still young – in my early 20s – so I moved to a banking job where I learned about foreign exchange [FX] and cash management," he explains.

This job at a Japanese bank as a treasury dealer for financial institutions and corporate clients gave him his first taste of the treasury world. During this time, he became acutely aware of the importance of effective risk management.

From there Lim moved to a Singaporean bank and was an investment counsellor and relationship manager and provided investment advice to highnetworth clients in FX, fixed income and equities. He worked hard, and during this time he successfully acquired 100 new accounts in three months with total assets under management of SG$30m. He then moved to another Japanese bank and became a treasury trader, advising and executing FX spot, FX options, interest rate derivatives and money market instruments for major multinational corporations and regional banks. One of the accomplishments he is most proud of is achieving SG$1.5m profit and US$1.4bn volume in a single year.

An evolving career

Lim's career shifted gears when he moved to a family office and investment company that was founded by one of Asia's most well-known banking magnates. The family office has numerous interests, which includes being a major shareholder in a Singaporean bank as well as various investments in public and private equity, venture capital, hedge funds and fixed income credit.

Although there is a clear banking connection in this firm – with its founder also being the founder of a major bank in Asia – the overarching objectives for Lim in this role were quite different when he worked in a bank. For the family office, his main responsibilities were to provide specialist input on technical analysis for the firm's investments, managing and hedging the firm's equity, FX and fixed income investments. He also selected and oversaw hedge funds and other daily fixed income funds. Additionally, he ensured there was ample liquidity for the foundation's activities and its subsidiaries' businesses. In addition, he monitored the FX and equity markets on a daily basis and traded within risk limits.

The emphasis in Lim's family office role was different from what he has since experienced working for multinational corporations. Being in a treasury role, where major decisions can ultimately affect the survival of an organisation carries a weight of responsibility. Did Lim feel this burden – or stress – with this kind of responsibility working for the family office? Is it more or less stress working for a corporate?!

"The stress levels and expectations are different with a family office – you do not want to be the one responsible for losing the family's wealth," Lim says. He explains that the major key performance indicator (KPI) is on beating inflation and ensuring future generations can preserve and continue to use the family's wealth. In a corporate, he says, the emphasis is typically different and there would be a larger risk department to manage various risks. Still, there is a stress – and responsibility – that comes with corporate treasury roles. A misjudged hedge, for example, could leave a company massively exposed. Or a treasurer's FX decisions could lose the company millions, which could then impact the share price, Lim comments. While no one wants to be the one to lose a family's wealth, by the same token, no one wants to be the one to put a corporate out of business.

Lim crossed over to working for corporates when an opportunity came his way. After working for the family office since 2007, many years later, in 2016, he made his first foray into corporate treasury. He became a senior manager in FX, liquidity and fund management at a major Singaporean engineering firm and managed their alternative investments as well as their cash. From his previous family office role, he was well-versed in managing alternatives, which was experience the engineering firm found attractive. After five years in this first treasury job, Lim has pursued other corporate treasury roles and has remained in the industrial sector.

Reflections on risk

Now that he is working in a corporate environment, Lim has a chance to reflect on the different approaches to managing risk. When asked about the main lesson he has learned through his 20-year career – in working for banks, a family office, and multinational corporations – he says the main learning is related to risk management. "The main lesson I have learned is not to take risks unnecessarily – whether that is in the treasury department of a bank, or dealing with highnetworth clients or a family office – and it is never a good idea to put money in one basket. Being risk averse is something that is good for my day-to-day responsibilities," Lim tells Treasury Today Asia.

When it comes to being risk averse and being sensible with diversification, there is still the possibility that Donald Rumsfeld's unknown unknowns can cause a problem. Even though investors think they are diversifying, they could actually all be investing into the same underlying risks. During the global financial crisis, for example, credit default swaps seemed like a good way to insure against defaults, but there was concentrated risk in the market because AIG was the major provider of the swaps and underwriting the market. When they ran into trouble, the problems were systemic. How, then, does Lim ensure he has his eyes, ears and mind open to the possibility that there are risks emerging he doesn't know about? What about 'Black Swan' events – which were made famous by the theory of economist Nassim Nicholas Taleb who argued that rare and unpredictable events can have a disproportionate impact. Conventional methods cannot often see such events coming, even though hindsight can often rationalise and explain them.

> The stress levels and expectations are different with a family office – you do not want to be the one responsible for losing the family's wealth.

"I survived the global financial crisis and was quite lucky because we had invested in a fund that was dealing with US mortgages," Lim comments. One lesson he learned, he says, is that what is deemed 'safe' may not actually be safe if everyone decides to sell at the same time. Given the main motivation of a wealthy family is to preserve wealth, and to be prudent and risk-averse, working in this environment means there is a different kind of sensitivity to when the markets are turning for the worse. "My family office background has stood me in good stead because I have been exposed to different indicators about what the tell-tale signs of problems are," he says.

This kind of perspective is different from other corporate treasurers who typically come from an accounting and finance background, where the focus is on bookkeeping and the balance sheet. When these corporate treasurers hedge their foreign exchange exposure, Lim says, they typically rely on banks to do this for them. The problem with this approach, however, is the banks' motivations may differ from the corporates', and they may not always know when a suggested approach is more in the banks' interests than their own. Given his background, Lim is able to bring a different mindset to the table when assessing a bank's products and solutions and will often challenge the bank with a confident argument.

Keeping an eye on geopolitical risk

Now, in his current role as a senior treasury manager at a shipping and logistics company, Lim's priorities are in bringing improvements to how the treasury is run. One of his aims is to centralise the treasury, which is something he has worked on in his previous roles. Lim is also looking to digitalise the treasury, enhance the use of the treasury management system and automate the reporting as much as possible. Many treasuries, he comments, still rely on manual processes and it is not uncommon to see companies in Singapore still relying on Excel. "In one sense it's a good thing because it gives everyone lots of work to do," he jokes.

In his current role, there are many factors he needs to monitor because of the nature of the industry in which he is working. Geopolitical risk is a major risk he needs to have a handle on. With tensions in the Middle East, for example, any rise in the price of crude oil has an enormous impact on shipping costs. Meanwhile, the multinational needs to ensure any price increases to its customers are not too dramatic – otherwise they risk losing their business altogether. "Things can be quite volatile," says Lim of the current geopolitical environment.

With navigating such situations, it is necessary for various teams within a corporate to communicate effectively; no department can operate in a silo when deciding the best course of action with rising costs and prices. For this reason, says Lim, he has a close working relationship with the finance team as well as each of the business leaders of the company. One advantage of the nature of his industry, however, is that the pricing is done in advance based on the macroeconomic outlook at the beginning of the year, and the company's contracts have a relatively long timeframe. In this sense, the uncertainty in the markets doesn't have an immediate impact in the same way it would for a fast-moving consumer goods company, for example, which is always having to manage inventory – and the associated costs and pricing – on a shorter cycle.

From the treasury team, Lim is exposed to all aspects of his company and gets a front-row seat as major events unfold because of the strategic importance of the treasury function. Lim says he likes working in treasury because it is related to so many topics, and they can vary every day. "It's a good career to be in," he comments. "Corporate treasury is quite dynamic and can be quite different depending on the industry you are in – that's why I find it interesting," he adds.

Other interests and role models

When Lim isn't working in treasury, one of his interests is English Premier League, and he is a keen supporter of Liverpool football club, which has provided him with opportunities to reflect on his role models and the nature of leadership. In a recent post on LinkedIn, Lim referred to the announcement in January that Jorgen Klopp – the manager of Liverpool FC – would be retiring at the end of the season. Klopp has been widely lauded for building a team culture, treating people with respect, and effectively delegating. His departure after nine years comes at a good time and allows him to leave on a high. Lim has taken some lessons from this, which can also apply to his professional life. "His departure also shows one thing: nothing is permanent and if it is time to move on, leave with your head high and never burn bridges," he wrote in a LinkedIn post.

Building for the future

For now, Lim has his work cut out digitalising the treasury at his current company and moving it to real-time so the team can have up-to-date visibility of its cash positions. As is common with many others in the treasury community, Lim sees artificial intelligence (AI) as a major trend that will be useful for forecasting cash flow as well as the macro environment. "AI is here to stay and will go a long way in enabling us to do things we cannot do at the moment," says Lim. There are risks with relying on AI, and they pose myriad challenges to risk management professionals. However, Lim isn't getting carried away with his vision of how AI will be used. "You still need someone to stress test the results that AI has given you – you need to take it with a pinch of salt," he says. With AI on the horizon and set to become a mainstay of working treasurers' lives, it is good to know that Lim will still be keeping an eye on the known knowns, the known unknowns – and the unknown unknowns.

Digital sovereignty moves up the agenda

The rise of the digital economy – and the masses of data that accompanies it – is driving a push towards digital sovereignty where nation states seek to gain control over the production, storage and flow of data, and build their economic and cybersecurity defences.

If you take a photo of your dog, create a meme, and post it to social media, who has control over that data? Many jurisdictions could be involved: the software was likely created by a foreign company, as well as the social media platform. The data has been shared across borders and is now stored in the cloud, hosted by another company in a foreign land.

Nation states have long sought to protect their physical borders, but in the digital economy – where data proliferates – the boundaries are more difficult to define. Along with the rise of digital technologies, there has been a push towards digital sovereignty where nation states are seeking to put a fence around the production, storage and flow of data to assert their economic interests and bolster their cybersecurity.

The issue has implications for treasurers: cash and liquidity management, for example, is essentially data that is travelling across borders. And so are emails and Zoom calls where digital tools are facilitating the flow of data to other jurisdictions. Depending on how countries take action, the push for digital sovereignty could have implications for taxation, as well as an additional legal and compliance burden that comes with more data governance rules.

Simona Autolitano, a researcher and expert on the European Union's digital sovereignty at the Centre for Advanced Security, Strategic and Integration Studies (CASSIS) at the University of Bonn, comments that the understanding of digital sovereignty varies from country to country. In the EU, for example, it broadly covers how different member states want to control digital data on their territory, she explains. "It's not just about the flow of data, it's about creating and keeping the data on their territory," she adds.

Data is often described as the 'new oil', and Autolitano points out that data will be at the core of business in the future. Right now, however, many countries are missing out on the opportunities that the digital economy brings because other countries are benefitting from the flow of that data.

The EU's economic security

According to the World Economic Forum, as of 2021, 92% of data from the West is hosted in the United States, and there are no European companies among the world's Top 20 technology brands. Not surprisingly, the EU has taken issue with this and wants to do something about it. Back in 2021, the leaders of Denmark, Estonia, Finland and Germany wrote in an open letter, "Now is the time to be digitally sovereign. We have to foster the Digital Single Market in all its dimensions where innovation can thrive and data flow freely. We need to effectively safeguard competition and market access in a data-driven world. Critical infrastructures and technologies need to become resilient and secure."

There are two main aspects to digital sovereignty, explains Autolitano: economic progress and security. Given the shift to the digital economy, the EU needs to ensure that it is not missing out on the opportunities of the data-driven world. For example, European companies may want to compete with US companies in cloud technology and host some of the data that Europe produces themselves. By some estimates, Amazon Web Services currently hosts about one-third of the world's corporate data, with Microsoft and Google not far behind. In a paper by the Atlantic Council, entitled 'Digital Sovereignty in Practice: The EU's Push to Shape the New Global Economy', academics Kenneth Propp and Frances Burwell explain that under the leadership of Ursula von der Leyen, the EU has been boosting its support for homegrown technology, creating various regulations for the digital economy, as well as addressing the EU's vulnerabilities and threats from other countries.

A paper by the European Parliament states: "With a worldwide market for new digital technologies expected to reach €2.2trn by 2025, a large part of Europe's growth potential resides in digital markets." In line with this, the EU is asserting its digital independence and addressing concerns about the competition from other countries with innovations such as 5G, artificial intelligence, cloud computing and the internet of things, and how they are now major strategic assets for the EU economy. The EU has already invested heavily into research and development – to the tune of €80bn over seven years to 2020 – to keep the region at the forefront of such innovations.

Big Tech's threat to sovereignty

The European Parliament paper notes that the pandemic – when reliance on digital tools grew – accelerated the issues around digital sovereignty. The topic, however, has been rumbling in the background for a number of years. One of the drivers has been the rising dominance of Big Tech – both US and Chinese companies – whose influence extends beyond national borders and the efforts of governments to claw back control over their data.

One interviewee who works in government affairs, who wished to remain anonymous, told Treasury Today that many countries have felt aggrieved to be missing out on the tax revenue while technology companies have been profiting from the data that its citizens have been producing. France is one such country that took action with a digital services tax, which was targeted at the likes of Facebook. The French government's position was that the social media company, as an example, had been able to capture the attention of French citizens – and collect data on its user's behaviour and preferences – and then sell those insights to multinationals, and other companies, for the purposes of advertising. However, the French government had not been benefitting from the tax revenue from this economic transaction that involved its citizens. Now that economic activity is occurring beyond the traditional national boundaries, many countries around the world have taken action to ensure their economies are structured in a way that is relevant for the digital economy.

Tax in the digital world

Collecting taxes in the old-world economy was much easier when goods and services were traded within physical borders. Now things are much more complicated. Take digital nomads, who may be a national of one country, tax resident of another, yet are working on their laptop from a beach in Thailand, selling services to another country, and receiving the income into a bank account somewhere else. This is just one of the issues of the digital economy that national governments are now grappling with.

In theory every digital transaction could be taxed, but this taken to the extreme could cripple the global economy. For example, if every time data crosses a national border it is subject to tax, imagine what would happen if nation states took protectionism to the extreme and made all emails, or Zoom calls taxable or subject to tariffs. And for treasurers, given that moving money is essentially the transfer of data, if this was subject to taxation every time it occurred across national boundaries, this could be very difficult to manage. For now, however, there has been a moratorium on e-transaction data that crosses borders, according to a digital trade expert who spoke to Treasury Today. For now, while digital trade agreements are being negotiated, it doesn't look like that agreement will be broken, but if it is – it could wreak havoc on the way that the digital economy currently operates.

Most action has been taken in the form of digital services taxes, and there has been a shift in how governments treat companies that are selling digital goods and services from another jurisdiction. In a previous interview, Alan Lau, Partner and Head of Financial Services, Tax, KPMG in Singapore commented how there was a rising trend of seeking tax revenue for such transactions and various countries have been introducing additional taxes for foreign vendors. Singapore, for example, since 2020 has had a regime where such companies need to register under the Overseas Vendor Registration (OVR) and these rules were later extended to companies providing services from another jurisdiction whether they were digital or non-digital.

Digital sovereignty and cybersecurity

Taxation isn't the only reason that nations have been moving to assert their independence in the digital economy. As Autolitano already noted, digital sovereignty is also about cybersecurity and there has been a growing unease that many companies, individuals and government agencies are relying on foreign companies to host their data.

Autolitano explains that government ministries – given the amount of data they have to handle – are now putting that data in the cloud, but that could be problematic if the data is held offshore. This creates vulnerabilities about who can retrieve that data and could potentially lead to national security issues if other foreign governments have access to it.

From a cybersecurity point of view, there is also the potential for criminals to access the data without a national government having any control over it. "As long as you produce digital data, it will be interesting for criminals," says Autolitano. This is one of the reasons that many countries – such as China and Indonesia – have rules in place to store the data locally. Their moves towards data localisation on the one hand can be viewed as a prudent move for cybersecurity, although many observers criticise the approach as a form of economic protectionism.

Indonesia's data rules

Amid the trend toward digital sovereignty, Indonesia is a notable example of a country that has taken action and moved the topic up the national agenda in recent months. For example, in August 2023, Minister of Communication and Information, Budi Arie Setiadi was quoted as saying that Indonesian data must be protected: "Financial data must be in Indonesia because our financial data is vital." Later, in October 2023, President Joko Widodo spoke of the importance of Indonesia's digital sovereignty: "We have to protect our digital sovereignty and really defend our local content and local goods," he reportedly said.

Indonesia has also introduced a personal data protection (PDP) law that lays out how personal data should be handled. Gopul Shah, Director of Corporate Treasury and Structured Trade Finance at Golden Agri-Resources, which has a large presence in Indonesia, comments that the core of this law is about accountability and that organisations operating in Indonesia must be responsible for managing data. Organisations in both the public and the private sectors need to enhance their governance frameworks to ensure that personal data is protected, Shah explains. The PDP Law mostly aligns with the EU's GDPR [General Data Protection Regulation], says Shah, which means that the transition to these rules should be less onerous for multinationals who are already compliant with the European data regulation. There will, however, be an extra legal and compliance burden to bear. For treasurers, Shah says, "Banking, financial services and treasury activities will not see much impact except enhanced cost of legal, compliance and additional processes."

Range of trust issues

Historically, there has been a range of approaches from national governments regarding their digital trade, and how open they are to the free flow of data. While Indonesia has pushed for data localisation, there is a range of approaches that has been taken by the member countries in ASEAN [the Association of Southeast Asian Nations]. Anthony Toh Han Yang, Research Analyst at the S Rajaratnam School of International Studies, Nanyang Technical University in Singapore, previously told Treasury Today that countries like Singapore and the Philippines want a more liberalised cross-border data regime, whereas Malaysia, Vietnam, Indonesia and Cambodia have a more restrictive approach with their regulation.

When it comes to making digital trade agreements with other countries, one of the major issues is the degree to which data can flow with trust. This 'Data Free Flow with Trust' was a concept that was first introduced by the Japanese government, under the leadership of the then Prime Minister, Shinzo Abe. The idea is to facilitate the free flow of data while ensuring trust in privacy, security and intellectual property rights, and this has been taken up by the G7 member countries to turn the concept into reality, working on areas such as data localisation, regulatory cooperation, government access to data, and data sharing.

The European approach

The EU has already laid out its regulation for personal data with the GDPR, and is now taking the issue of digital sovereignty more seriously. In the past, it may have been correct to say that the EU was concerned with data from the perspective of human rights, and concerned about personal data and how it is handled – as is exemplified by the GDPR. Meanwhile other jurisdictions such as China were looking at data issues in terms of digital sovereignty. However, there has been a shift in the EU's stance under the presidency of Von der Leyen. Now, many of the EU's issues are framed in the context of geopolitics, explains Autolitano. There is a different concept of security – with a backdrop of conflicts in Ukraine and Israel, for example – and much of the EU's narrative is framed in terms of geopolitics and the need for security.

In terms of digital sovereignty, the EU is trying to set the rules of the game, with thousands of pages of legislation, says Autolitano. One target of the rules has been the financial sector, with regulation put in place to protect the region's financial infrastructure.

Treasury implications

Financial institutions are in the business of managing masses of sensitive data and so it is natural that they would be targeted with various rules and regulations, which will likely have an impact on the working lives of treasurers. This will become more apparent as treasuries become more and more digitalised, and treasury teams will increasingly rely on digital tools – likely produced by foreign companies – to manage their cash and liquidity. For those relying on fintech firms to assist with their digitalisation, this may create vulnerabilities if the data is not handled appropriately, points out Autolitano, and security will always be top of mind. Having said, the financial sector is well protected from cyber-attack because as an industry it has always been at the forefront of fighting cybercrime. "The financial sector is very well equipped – it has always been considered a critical sector," says Autolitano.

More to come from netting and pooling

Despite neither being a new concept, there is significant untapped potential for cash pooling and intercompany netting implementation among corporate treasurers.

Intercompany netting has been described as a relatively underappreciated treasury solution, particularly by international corporates who do a lot of business between linked entities in different locations.

Corporates that already have an in-house bank in place are fully aware of the possibility of using a netting process settled in the intercompany account and/or in a bank account, suggests Eric Aillet, Product Manager Enterprise Solutions at Finastra.

"Typically, those corporates that have not implemented cash pooling are less aware of the potential of an in-house bank because there has not been a history of structuring payment flows in this way within the group, or they are less sensitive to needing to centralise cash," he says.

Erik Smolders, a Deloitte Risk & Financial Advisory Managing Director in Treasury Management refers to significant interest in netting from smaller global companies, but acknowledges that the tools are not always in place to allow them to fully benefit from netting for a variety of reasons – including competing priorities and costs.

"The most successful netting implementations occur at organisations where the treasury and accounting teams are fully aligned on the benefits," he says.

Awareness is not a challenge, but rather internal buy-in from other finance teams – including tax – to commit to implementing a global netting structure. That is the view of Bob Stark, Head of Market Strategy at Kyriba, who cautions that netting programmes are not simple to construct as they require a dedicated effort, often originating from the CFO.

According to Justin Callaghan, CEO of FTI Treasury the financial benefits are generally well understood but often not well quantified at the business evaluation stage of implementing a netting process. Whilst these financial benefits are often the catalyst for introducing intercompany netting, the additional softer and knock on benefits are often only really understood after implementation.

These include the impact of balance sheet deflation by removing intercompany balances, systematic reduction of FX noise caused by these balances, the ability to settle third-party FX payments, and the dovetailing of the netting process with an internal FX hedging strategy.

"Besides the obvious benefits of saving on currency spreads, the main benefit that implementing an internal FX netting process brings is the structure and regiment imposed by such a process," he explains. "In a centralised ERP environment an automated process can be implemented. In a more decentralised environment the requirement to hedge exposures internally within agreed parameters and timelines can provide a focus for subsidiaries that may otherwise be less concerned with FX exposures."

Enterprise cloud communications company Bandwidth has derived numerous benefits from netting of FX and intercompany transactions, explains Treasurer, Scott Taylor.

"We have a large number of cross-border, cross-currency transactions and prior to netting we were settling these bilaterally," he says. "The first step in that process was similar to piecing together a puzzle where we would determine which subsidiaries had enough cash to settle their open payables balances. Then once subsidiary 'A' paid subsidiary 'B', we could proceed to 'B' paying 'C' and so forth."

This turned into three phases of settlements as the treasury team would enter the trades in its bank's FX portal and wait for settlement before moving on to the next group of transactions. Once all of that was finalised, the team made manual journal entries to record all the settlements.

Netting these transactions has reduced the processing time from weeks to days, reduced the notional amount of cross-currency trades by 90% and eliminated hundreds of manual journal entries, while the speed of settlement limits Bandwidth's exposure to FX volatility.

"The integration process was extremely easy," says Taylor. "Implementation only took a few weeks and most of the work was formatting the input file so that we could get the information back in a way that could be easily uploaded to our ERP system. We were able to get the process up and running with very little IT systems support."

Andy Schmidt, Vice-President & Global Industry Lead for Banking at CGI refers to two primary cost benefits from netting foreign currency exposure – lower transaction costs, and lower foreign exchange costs. "The transaction cost benefit will be easy to calculate because these transactions typically have a fixed fee, while the foreign exchange cost will vary depending on the currency pairs involved," he says.

Some corporates may not be fully aware of the potential benefits of intercompany netting, while others may face challenges in implementing it effectively due to internal complexities or limitations, suggests Jim Kessler, Vice President Global Treasury Solutions at Corpay.

"These challenges can include organisational silos, disparate systems and processes across subsidiaries, legal and tax complexities, and resistance to change from stakeholders accustomed to traditional payment practices," he continues.

Daniel Cugni, Manager Director GTreasury Netting observes that corporates without a cash flow hedging programme often don't have any visibility on intercompany flows.

"Intercompany payments are prepared by the accounts payable department and included (and hidden) in third-party payment runs," he explains. "Foreign currency payments are often settled from the main EUR or USD bank account with a very high spread. Intercompany reconciliation is done by accounting, and they don't always talk to their treasury colleagues."

In terms of numbers, Stark reckons that reducing the number of FX hedges needed to hedge intercompany exposures can lead to a reduction of up to 75% in trades and related costs – which for a multilateral netting programme could easily equate to a seven figure saving annually for larger treasury teams.

There are other advantages that are less visible, but also contribute to reducing the overall hedging cost. Having a single entity that is allowed to hedge on financial markets improves control, ensuring that all legal entities within the group are following the same hedging policy. Concentrating the bank relationship with a more restricted number of counterparties – and setting up forecasting processes to better predict future exposures – also helps ensure compliance with financial regulations and standards such as IFRS 9.

In addition, netting foreign currency exposures can help protect businesses from 'trading against themselves' by reducing trade volumes and managing staff costs, bank fees, hedging errors, and even the counterparty risk inherent to foreign exchange trading.

"However, it is important to remember that while the netting of corporate exposures prior to hedging those exposures can yield substantial advantages, any cost savings opportunities from netting should be evaluated on an after-tax basis as there could be tax or statutory reasons that would make this type of netting unattractive or impossible for some organisations," says Smolders.

The answer to the question of whether physical or notional pooling is the best option for the business depends on the liquidity structure of the business and local regulations. For example, some governments believe that notional pooling is co-mingling of funds from different entities.

"The physical pooling structure is a straightforward one and the concentration and management of cash centrally provides a feeling of control and security," says Callaghan. "The downside is that you then need to manage all of the resulting intercompany loans."

Notional pooling can allow for easily managed structures with no intercompany loan management required. However, it can also lead to over-inflated balance sheets, potential issues with net debt covenants, and credit issues with banks.

Banks are obviously keen to improve corporate access to services that can improve business performance by increasing the efficiency of internal liquidity management and the cash conversion cycle – services that include cash pooling programmes.

One of the most interesting aspects of demand for cash pooling is the extent to which it has been affected by higher interest rates. "CFOs recognise the opportunity cost of trapped cash and welcome programmes that increase cash utilisation while minimising the percentage of cash allocated for working capital," says Stark. "Cash forecasting has also increased in importance to help finance teams be more confident in investing cash for longer, within cash pools or externally."

There is no doubt that that there has been a much keener focus at board level on cash levels and visibility driven by both increased governance requirements and the higher cost of capital. Those organisations that have good liquidity structures can maximise yield on available cash and have also focused on finessing these structures by adding structures like multi-currency notional pools and intra bank sweeps, suggests Callaghan.

"Organisations which were a little bit behind the curve in terms of efficient pooling structures have had to react quickly to the increasing rate environment to ensure adequate control over non-earning cash assets that could achieve a good yield elsewhere," he adds.

Concentrating cash within an organisation provides similar benefits to netting foreign currency exposures. This becomes increasingly important in a higher interest rate environment, not only because of the savings inherent when balances in opposite directions are netted or when aggregation gives better conditions, but also for the improved monitoring and control it offers. "Large, listed corporates are used to working with a high degree of centralisation so for them the demand for cash pooling services is not interest rate sensitive," explains Aillet. "However, for medium sized corporates this is an area where demand has likely increased."

Cugni reckons demand for cash pooling has increased as decentralised companies started to realise that some of their subsidiaries were borrowing funds at a very high cost, while others had excess cash poorly invested. "Many companies have taken this opportunity to improve their liquidity structures and have started to centralise their treasury activities with physical or notional cash pooling by region and currency," he says.

Higher interest rates have clearly highlighted the opportunity cost of inefficient bank account and liquidity structures. In a near zero-rate environment it is difficult for many treasury organisations to make a business case for implementing a cash pooling structure due to the lack of monetary benefit.

"But there are benefits of cash pooling that exist whether interest rate levels are at zero, 5% or any other level," suggests Smolders. "These include access to liquidity, global visibility of cash, and the possibility to provide intercompany liquidity using notional pooling without currency risk. For this reason, many treasurers have maintained and in some cases expanded their cash pools even when the interest benefit of cash pooling has not necessarily been present."

Corporates are keenly aware of the impact that using pricier working capital lines of credit can have on their margins and net income and have been asking their banks for more efficient ways to manage liquidity and forecast cash flow according to Schmidt.

"Better liquidity management and cash flow forecasting services provides corporate banks with an opportunity to create stickier relationships and gain greater insights into their corporate clients' cash management needs while also creating additional recurring revenue streams," he concludes. "This type of partnership gives treasurers more time to focus on bigger issues, making these types of services well worth the additional investment."

The right time to tap the bond market

How do treasurers view the bond market in 2024?

Todd Yoder
EVP & CFO
Shikun & Binui, USA

Corporate finance has seen a lot just in the past 20 years, so I think most are well prepared to ensure resilience and not over correct as has been the case during certain turbulent periods in the same time horizon – some companies have adopted more conservative liquidity strategies, such as maintaining higher cash reserves and/or securing additional lines of credit, to buffer against additional unforeseen shocks.

Regulatory changes or updates, such as amendments to liquidity risk management regulations or capital adequacy requirements, may necessitate adjustments to how the corporate side manages liquidity. We need to ensure all the core items are covered – noting changing regulatory guidelines, capital requirements, and standards to ensure sufficient liquidity buffers are there to mitigate regulatory risks.

As I have said many times over the past 15 years, “hope is not a strategy;” instead, we closely monitor credit conditions and lending standards, tightening credit markets or reduced access to financing can restrict options. Many corporates I know are proactively engaging with lenders to secure favourable terms and explore alternative financing sources to ensure adequate liquidity is there if needed. Running scenario analysis and stress testing to assess the resilience of the company’s liquidity position under various economic scenarios. We model different outcomes and identify potential liquidity risks; we then develop contingency plans and adjust liquidity strategies accordingly to mitigate adverse effects on the business.

Capital allocation should always be top-of-mind not just when we see turbulence in the horizon, we weigh the trade-offs between deploying capital for growth initiatives, debt repayment, shareholder distributions and maintaining liquidity reserves. It’s important to set up favourable credit agreements when you don’t need them – ideally moving when opportunities in the market are present.

Many of the CFOs I’ve spoken with over the past few years (who were able to) pre-hedged and are seeing positions way in the money and also moved to renegotiate credit agreements when rates were far more favourable than what we see in the current market. Given what I know now, I think two scenarios could develop, one is we see the forecasted cuts much slower than the market has priced in for 2024, and the other is we see something break and rates come down much faster than the market has priced in – credit markets are smart, I think they are priced in the middle of each of those scenarios.

What I have seen in the market in the past couple of years is those that have needed to tap the capitals markets moved beyond traditional debt issuance to alternatives such as convertible bond offerings, equity issuance and structured financing transactions.

The best approach in the long run is to stay informed and when opportunities arise be agile and ready to layer into those opportunities, closely monitor developments in monetary policy, the regulatory environment (B3 endgame), and adapt and remain agile in navigating changing market conditions to effectively manage funding costs and maintain financial flexibility. I have had more colleagues from a variety of companies call me to ask about hedging IR risk in the past 18 months than my entire career combined – a lot of discussions about the risks – asset/liability alignment duration, repricing, spreads, slope change, liquidity, credit and regulatory. The only trend I’ve seen is an uptick in those getting more educated. I think we are in a wait-and-see while being prepared space right now, and if rates do begin to fall later this year, we see a lot layering into these opportunities.

Michael Booth
Portfolio Manager
Invesco

Treasurers time bond issuance by looking at value, especially market arbitrage opportunities around credit spreads and the all-in cost of financing on a currency hedge or a market hedge basis. UK businesses might find it cheaper to issue in sterling or euros after hedging back to sterling, for example. Treasury teams also look at natural hedging to offset assets in other geographies. This also allows corporates to open themselves up to different investors, prudent if one market is closed like sterling was during Truss’s mini budget.

Large corporates and investment grade companies, have well established credit curves and a good ladder of maturities. This means they can diversify their refinancing across that curve. They might sell a new issue to fill a gap in that curve to keep the spread of maturities well maintained.

We’ve seen a fair bit of interest in long dated sterling issuance tied to demand from defined benefit pension funds derisking.

We are seeing treasury come in and take advantage of that. The ECB is running off its corporate bond buying programme and institutional money is filling demand. It's testimony to these yields being attractive. In the US we have seen issuance at the front end because corporates think rates will fall and are unwilling to lock in for ten years.

Still, infrequent users of the capital markets and issuers with a lower credit rating, say in the mid to BBB, should make sure they have a strong investors story and robust communications when they come to issue. It's only solid investment grade issuers that can announce a deal in the morning and build the book through the day. Its important corporate treasurers at lower rated/weaker companies give the market time to get comfortable on the credit risks.

These treasurers should also be prepared for questions around net zero and the regulatory backdrop. Questions will be around the business risk, balance sheet leverage and free cash flows visibility. Some companies that built their balance sheet during QE are struggling with higher rates. For example, a highly levered high-yield issuer refinancing all its debt at 10% likely won't generate enough free cash flows to service that balance sheet and we are seeing pockets of stress emerge.

Over the last couple of years, we saw a jump in sustainability linked bond issuance and treasury teams seeking to tap ESG flows, but the issue volume has dropped off slightly. We believe some investors are less willing to get involved in these structures. One of the challenges is that the corporate pays a price for not meeting its target, but as an ESG investor you don't want to benefit from a company not meeting its environmental target. The green bond market is a simpler way to isolate demand in the ESG market.

Giulio Baratta

Head of Investment Grade Finance Debt Capital Markets

Now is a good entry point into fixed income from an investor perspective. We are entering a cycle where interest rates are set to stabilise or decrease, and supply is tightening because more bonds are set to expire than be issued meaning investors are concerned about a shortage. This will also support performance. We believe the first part of 2024 will be accommodative of companies; there is an opportunity for treasurers to take advantage of capital markets, they will receive oversubscribed books and improved pricing conditions, especially for long-term maturities.

In recent years, corporate treasurers have had to navigate the rapid increase in interest rates and funding costs. Now companies with capex and investment plans are in a position to prefund; there is less uncertainty in the economy and investors still have cash to deploy.

Moreover, the outcome for equities remains uncertain; there is no clear route ahead for equity valuations which means M&A will remain muted. If treasury has to fund less M&A, they can focus on optimising refinancing costs as opposed to increasing debt stacks.

Credit spreads are currently very low compared to historic levels and the market is pricing credit risk very tightly. One reason is because central banks might lower interest rates to boost the economy. As soon as this happens, credit spreads will widen in a reflection of the increased risk for investors. It means the yield, or what treasurers pay on their debt, may not go down further.

This is triggering interesting corporate behaviour. For example, we are seeing more European corporates use the debt capital markets for three to four year funding. Some corporates are switching from using bank loans and bank products for their short-term funding needs to tap the markets instead. Companies are also arbitraging term loans against the debt capital markets and commercial paper. This is bringing more liquidity for institutional investors and is a trend first seen in the US.

We are seeing more appetite from investors for maturity extensions. The most liquid space in the bond market is between five to ten years or seven to 12 year buckets. In Europe, we expect to see the resurfacing of a liquid benchmark of 20-year funding for investment grade issuance. The sterling market is also buoyant for the longer end (12-15 20 years) where we have seen reverse enquiries from investors.

Of course, treasurers are loath to extend maturities when rates are still high. But we would argue that the marginal cost of issuing ten-year rather than seven-year paper is limited.

Next question:

"What are the do's and don'ts when it comes to integrating a TMS?"

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