HSBC's Guide to Cash, Supply Chain and Treasury Management in Asia Pacific 2012

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HSBC

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Foreword

Welcome to the 15th edition of HSBC's Guide to Cash, Supply Chain and Treasury Management in Asia Pacific. As ever, the Guide delivers a valuable range of information on industry developments and best practice across the region via insightful contributions from leading industry professionals.

All three disciplines in the Guide's title have continued to evolve rapidly in various ways. However, a strand common to all of them – which is also the theme of this year's Guide – is connectivity.

In many ways this builds upon something I mentioned in the foreword to last year's Guide, which was the changing interaction among the world's economic regions. Emerging markets have been breaking away from the conventional wisdom that they are dependent upon OECD economies for their growth – instead, they are sourcing new customers and suppliers in other emerging economies and developing their growing domestic consumer economies, although the extent of this decoupling remains to be confirmed given recent Chinese economic data.

Apart from macroeconomic factors, in 2011, risks such as natural disasters have also been driving this diversification and counterbalancing the tendency to consolidate relationships to drive efficiencies and focus on trusted commercial and financial partners.

From a treasury perspective, this diversification has important implications. Together with bank consolidation and risk management considerations, diversification begets a need for open standards and industry-recognised systems integration with banks capable of delivering the flexibility required to fulfil these criteria. The good news is that more extensive yet open connectivity is already available. The common standards and neutral platforms that we have been promulgating across the industry for some time have now come into their own in a significant way. They can be used by corporate treasuries and finance functions to deliver the non-proprietary financial connectivity that businesses need to navigate and manage through demanding times.

As a result, you will find various articles in this issue that deal with connectivity. We hope that you will find these and the other articles and resources in the Guide a valuable reference, and of assistance in unlocking the potential of your commercial enterprises. As always, we welcome your comments and any suggestions you may have for the 2013 edition.

Finally, I would like to thank the various clients, industry colleagues and external experts whose valued editorial contributions make the Guide such a benchmark resource for the industry.

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Blaik Wilson is a Solutions Consultant and Vice Chairman of the Hedge Accounting Technical Taskforce (HATT) at Reval. He is a qualified Chartered Accountant and an international instructor and consultant specialising in financial instruments, hedge accounting and treasury policy. Mr Wilson's experience spans Asia Pacific, Europe and North America. Prior to Reval, he worked as a consultant assisting corporations and financial institutions with IAS 39/FAS 133 compliance. He is also credited with designing treasury systems for SunGard. In 2006, Mr Wilson was awarded the Northern Region Young Chartered Accountant of the Year Award for his work on IAS 39. He is a regular speaker at accounting and treasury conferences on compliance issues relating to international accounting standards.

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Pole Yu is IT2 Treasury Solutions' Regional General Manager for the Asia Pacific region. He is based in IT2's Hong Kong office. Since joining the company in 2004, he has managed projects for a range of corporate and financial institution clients. His experience includes systems development, consulting, banking product development and client relationship management. Mr Yu holds a Bachelor of Science degree with honours in Business Administration and Computer Science from Aston University, Birmingham, UK, and an MBA from the Hong Kong University of Science and Technology.

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The New Economic Landscape

Riding Out the Storm in Style

Peter Wong, Founding Chairman, International Association of CFOs and Corporate Treasurers (China) and Convenor, Hong Kong Association of Corporate Treasurers

- Treasury management practitioners in Asia are seeing a shift in focus from operations to strategy, with connectivity as the key enabler.
- There is also increasing governance oversight at the corporate board level with a view to ensuring liquidity and de-risking.
- As the global economy rebalances, investors continue to look to Asia for new opportunities, giving a boost to foreign direct investment and to the region's financial centres.
- All this demands a higher level of sophistication in developing a corporate financial management strategy that is mindful of the traps and taps the opportunities.

Introduction

Corporate treasurers are thrust centre stage whenever there is turmoil in the financial markets. Experience has shown that the impact of the recent crisis will be recurring in nature and global in its consequences. Asian economies will continue to adjust to sluggish demand in the US and European markets. On the other hand, the shifting of capital flows from the West to the East will sustain the growth in foreign direct investment (FDI) in Asia and promote the development of the financial services sector in Shanghai, Hong Kong and Singapore. All these factors will encourage a higher level of sophistication among treasury professionals in Asia and fundamentally change the role of Asian treasury centres within the corporate financial management strategy.

Focus Shift from Operations to Strategy

Historically, treasury management in Asia is about cash management. With the increase in market volatility and the scale-backed lending capacity of banks, corporate treasurers will have to devote more attention to the management of financial risks – including liquidity risk, counterparty risk and foreign exchange (FX) risk, and corporate finance – including strategic financing via initial public offerings (IPOs), spin-offs, off-balance sheet financing, mergers and acquisitions (M&A), capital structure review, etc. Treasurers are partnering with business units to devise a capital structure and long-term financing profile that support the strategic change of the business model and future sustainable growth.

Liquidity risk is not going to go away, thus the ability to have internal cash visibility, rolling cash forecasts that reflect each business unit's funding priority and real-time control of cash mobility are essential elements of running a business in good times and in bad. Increasing numbers of corporate treasurers in Asia are implementing new treasury management systems (TMSs) after the 2008 financial crisis. A good TMS is necessary but not sufficient.

"Liquidity risk is not going to go away, thus the ability to have internal cash visibility, rolling cash forecasts that reflect each business unit's funding priority and real-time control of cash mobility are essential elements of running a business in good times and in bad."

A key enabler of this changing focus is connectivity, supported by robust cash management systems and processes. In addition, corporate treasurers will also need to review and streamline their bank account structures, strengthen cash concentration and cash pooling arrangements as well as achieve a high degree of control in the deployment of cash against any contingency liquidity needs. Such operational cash management review can go hand in hand with a banking partner review or assessment.

New Paradigm in Choosing Banking Partners

Banking facilities are becoming scarce resources. On the other hand, deposits from corporate customers are valuable to banks to reduce dependence upon inter-bank funding. Fee businesses are attractive to banks also as they do not require expensive capital support. Corporate treasurers can review their banking arrangements and consider centralising their fee businesses and deposits with one or a few core banks. A network of supporting banking partners is, however, important to maintain the diversity of funding, to provide the counterparties required for risk management and to reduce concentration risk. This will be a fine balancing act requiring constant monitoring in light of market developments and periodic review considering the overall corporate development strategy.

Increasing Governance Oversight at the Board Level

Corporate boards are increasingly concerned whether companies have put in place robust processes to guard against the possible deteriorating credit profiles of banks and customers if double-dip recession becomes a reality. It is fair, therefore, for corporate treasurers to exhibit the behaviour of flight to quality and to keep a relatively higher level of cash balances to mitigate liquidity risk.

The efficiency of the cash management system will also be monitored closely to ensure liquidity flow is not trapped in times of need.

More importantly, boards will demand that treasurers devise corporate finance solutions for de-risking. For example, the capital markets will have to be tapped to reduce dependence on bank lending. The current low interest rate environment provides a window of opportunity to issue fixed rate bonds before the inflationary effect of quantitative easing begins to kick in during the upturn of the economic cycle. Hedging solutions will be needed to achieve cost averaging and to counter increased volatility in the FX and commodity markets. Inflation is temporarily halted but stubbornly high energy prices may reflect long-term worries about the inflationary effect of a weak US dollar (USD). Market risk remains difficult for a corporation to minimise.

Rebalancing of the Global Economy

The recent downgrade of the US's sovereign rating is a wake-up call to the global financial world of the vulnerability of dependence upon the USD when the US is the world's largest debtor nation. There is no easy or quick answer. While the last thing the market wants is another shock, we look forward to a gradual change for the better rather than a gradual degradation. If the trade receipts in the next 10-20 years are denominated less in USD but in other currencies such as the renminbi (RMB), then there is less reason to hold on to USD assets. The relatively low long-term US benchmark interest rates indicate that the markets still entrust their wealth to US treasuries. The day that another national currency will challenge the USD as a safe haven currency is still far away.

What has unfolded in the past 12 months in the financial markets has further weakened market confidence. The fiscal deficit and external borrowing in some European countries have reached unsustainable levels. The banks are the first to be hit. The downward adjustment in the equity markets and the bond rating downgrade make it difficult for banks to obtain new funds from the stock and the bond markets. Some of the banks have just started their deleveraging process, with loan-to-deposit ratios as high as 90-100%, and find their capacity to lend severely constrained. We expect there will be a shift of funding activities from the West to the East, as Asia maintains a healthy savings ratio as percentage of the gross domestic product (GDP) and the banking sector is fundamentally sound.

> **"A deepening of the recession in Europe and the jobless recovery in the US will drive investors to look to Asia for new market demand opportunities, in the service industry sector in particular, where there is immense growth potential in major emerging markets in the region."**

A deepening of the recession in Europe and the jobless recovery in the US will drive investors to look to Asia for new market demand opportunities, in the service industry sector in particular, where there is immense growth potential in major emerging markets in the region. Such investments will require new funding requirements, which are likely to be sourced from within Asia rather than outside the region. Continuous economic development in China is important as it is now the world's second largest economy ranked by GDP, has the world's highest level of FX reserves and is a major creditor nation.

Internationalisation of the RMB

The development of the offshore RMB market is an important step in the internationalisation of the RMB. The pool of offshore RMB is being built up rapidly – RMB is increasingly used as the invoicing currency for international trade and settlement, and a growing number of Chinese cities can remit RMB overseas to settle their trade obligations. Areas that require further attention are the breadth and depth of RMB offshore investment and the mechanism to repatriate funds for use within Mainland China. While such developments will take time to mature, the recent policy announcements by the Mainland government are steps in the right direction. For example, HSBC recently infused capital in RMB to HSBC (China). The development of the dim sum bond market in Hong Kong is taking shape. In time, the Hong Kong stock market will allow shares to be listed and traded in RMB as well.

> **"Areas that require further attention are the breadth and depth of RMB offshore investment and the mechanism to repatriate funds for use within Mainland China."**

As the liberalisation continues, the RMB may take a route of gradual, rather than sudden, appreciation. It may also experience short-term volatility. Therefore, there is a need for risk management tools to be further developed to hedge against such risk.

Asian Treasury Centre Choices

Singapore, Shanghai and Hong Kong are Asia's three most popular treasury centres.

Singapore will continue to be an attractive centre for multinational corporations (MNCs) due to its proximity to India and Southeast Asian markets and its successful track record in market development such as the derivative market and the fund management industry. The nation's English language proficiency remains its competitive advantage and its triple-A sovereign rating is an important selling point in its establishment as a wealth management centre. The government is strongly committed to high-end management education and actively encourages employment of expatriates to mitigate possible talent gaps and support future growth.

Shanghai has set a timetable to achieve international financial centre status by 2020. It is already the centre for the domestic RMB financial market in terms of the size of both the equity and bond markets. The volume of international cross-border flows is subject to the timetable of the liberalisation of the capital account. Currently the intermediation of capital outflow is through the Qualified Domestic Institutional Investors (QDII) scheme. Significant developments in the Shanghai financial markets are anticipated in the years to come.

Hong Kong has become the de facto offshore RMB centre because of its strong economic ties with the Mainland relating to trade and investment flows, its proven track record as an international financial centre in capital formation and by virtue of being a part of China. The internationalisation of RMB will further strengthen Hong Kong as an Asian treasury centre. The Hong Kong Monetary Authority (HKMA) and the Financial Services and the Treasury Bureau (FSTB) have contributed tremendously to a constructive working relationship with Mainland regulators, devising policies and administrative details that can facilitate the process of RMB internationalisation in a controlled manner, in alignment with the domestic financial and economic development priorities.

Much has been done to harmonise the professional institutional framework in the legal, accountancy and banking arenas, which facilitates mutual recognition and cooperation. For example, Chinese companies audited by Mainland-authorised audit firms under Chinese accounting standards can list in the Hong Kong Stock Exchange without separate filing using Hong Kong accounting standards. The move makes sense, as both China and Hong Kong are adopting international financial reporting standards (IFRS) and will gain market confidence over time.

Such changes will accelerate the use of Hong Kong by Chinese companies as their international financial centre. The rapid development of the service industry in China will provide immense opportunity to Hong Kong. International students – mainly from the Mainland – will soon account for one-fifth of Hong Kong's undergraduates. They can elect to work in Hong Kong after graduation and become local citizens after seven years. The government has introduced policies to support the development of private universities since 2009. Nurturing talented professionals with strong Chinese and English language capabilities with both global and China experience is a critical success factor for Hong Kong in its drive to maintain its role as an international financial centre.

Be Mindful of the Traps, Tap the Opportunities

The overall risk profile of doing business has increased and success in this volatile environment calls for strong leadership and professionalism. Smart management will be rewarded. The costs associated with leaving cash idle are high and free cash from banks is a thing of the past. Corporate treasurers are able to improve the profitability and sustainability of businesses by controlling treasury operations through improved connectivity and by moving up the value chain by participating in strategic decision making. The financial landscape in Asia is undergoing fundamental changes with the speeding up of the internationalisation of the RMB and the readiness of Asia's financial centres to increase their depth and breadth, riding on the region's healthy savings and robust banking sector.

Connectivity: Make or Break in a Global Market

Simon Constantinides, Regional Head of Trade and Supply Chain, Asia Pacific (ex Hong Kong/Macau), **Richard Jaggard**, Regional Head of Sales, Global Payments and Cash Management, Asia Pacific, and **Caroline Lacocque**, Head of Client Integration Consulting, Global Transaction Banking, Hong Kong, HSBC

- As buyer/supplier relationships continue to diversify globally and become more complex, so do associated transaction patterns in the physical and financial supply chains.
- While physical supply chains have changed substantially in recent years to accommodate these changes, financial supply chains have not always kept pace.
- The situation has improved for those corporations capable of exploiting new connectivity opportunities and technology by deploying the right strategy.
- Achieving this requires a flexible mindset with a focus on maximising partnerships – with banks, infrastructure providers and technology vendors, and within the supply chain.

The traditional model of East/West economic flows was already starting to look a little *passé* even before 2008, but since then it has begun to look positively outdated. The original concept of globalisation was based upon the expansion of large corporations from developed economies in North America, Europe and Japan selling products into developing markets. By contrast, a new concept of "globality" is replacing this whereby companies from rapidly evolving economies are operating in a completely new business environment where knowledge, materials, people, suppliers and customers can be located anywhere globally and transaction flows are similarly omni-directional.

The New World Ahead

New World, New Order

One consequence of this new environment is that companies that many in the West had barely heard of 20 years ago now hold prominent positions in developed markets. For example, through its holdings in companies such as Jaguar and Corus, Tata is now the UK's largest manufacturing company. Elsewhere, companies from emerging markets (such as Samsung and LG) have become global multinationals in a fraction of the time it took far longer established Western corporations to achieve the same status.

> **"In 2010, Asia's stock markets represented the largest share of global market capitalisation (32%), ahead of both the US (30%) and Europe (25%)."**

This shift is not just confined to a few prominent emerging market corporations; the combined effect of these markets is similarly impressive. In 2010, Asia's stock markets represented the largest share of global market capitalisation (32%), ahead of both the US (30%) and Europe (25%). These figures are perhaps not so surprising when one considers how attractive many emerging markets have made themselves in the context of foreign direct investment (FDI). A.T. Kearney's 2010 Foreign Direct Investment Confidence Index highlighted this, with China, India and Brazil in the top five, while emerging consumer markets (such as Indonesia and Vietnam), also ranked highly. The nature of the consumer markets in some of these countries makes their FDI popularity entirely understandable, with the developing world's share of gross domestic product (GDP) in purchasing power parity terms increasing from 33.7% in 1980 to 43.4% in 2010.

New Links

The economic doldrums that many developed economies lapsed into during the financial crisis further accelerated the expansion of trade links among developing economies ("South-South" trade) that is now driving many of the changes outlined above. The scale of these linkages is already impressive, but is likely to become truly remarkable over the next few decades. In the case of China, India and Brazil, South-South trade accounts for 47%, 58% and 58% respectively of their current total exports.[1] But by 2050, these figures are expected to jump to 75%, 83% and 83% respectively.[2]

These links are already translating into activity that supersedes that conducted with developed Western economies. During the Chinese premier's December 2010 visit to India, USD16bn of trade deals were signed – comfortably surpassing the USD10bn of deals signed during the US president's visit the previous month. The relative importance of emerging market infrastructure through which all this new trade activity will flow is similarly impressive. Today, five of the world's ten largest container ports are Chinese; 20 years ago, none were even in the top 20.

> **"Today, five of the world's ten largest container ports are Chinese; 20 years ago, none were even in the top 20."**

Furthermore, these South-South links now go much further than just everyday trade activity and extend into long-term strategic investment and acquisition. The second largest Brazilian mergers and acquisitions (M&A) deal of 2010 was Sinopec's acquisition of a major stake in Repsol-YPF, while in Argentina the USD3.1bn investment in Bridas Corp by CNOOC was the largest M&A deal of 2010. Furthermore, this sort of activity increasingly involves both direct and indirect investment in the huge pool of natural resources that is Africa. For example, Riversdale, the Australian-listed company developing coalfields in Mozambique, is nearly 50% owned by three companies from China, India and Brazil (Wuhan Iron and Steel, Tata and CSN).

1 *IMF Direction of Trade Statistics.*
2 *HSBC estimates.*

New Complexity, New Risk

The proliferation of these South-South links has become a prominent feature of world trade in its own right, but it has also been a major element in another rapidly developing trend – complexity. The need for a competitive edge in tough economic conditions has seen an increasing number of companies breaking down their manufacturing processes into more granular elements in order to obtain best value and efficiencies. In doing so, they have opened up access to a larger pool of smaller suppliers capable of handling these smaller individual tasks/stages in the manufacturing process at competitive cost.

Furthermore, subject to the constraint of transportation costs, these suppliers may be geographically diverse. It is no longer just a case of invest in Asia, manufacture in Asia and ship to Western Europe or the US. Depending upon the value of the finished product, it may be a case of dealing with multiple suppliers in Africa and Latin America for raw materials, shipping to multiple Asian locations for manufacture of sub-assemblies, shipping to Eastern Europe for further manufacture, before shipping to the US for final assembly and testing. In some cases, the geographical patterns involved may even be considerably more complex than this.

> **“A similar pattern can apply on the sales side, with (multiple new) markets emerging as new consumer classes develop and start to move up the value chain from generic white-label items to global brands.”**

A similar pattern can apply on the sales side, with (multiple new) markets emerging as new consumer classes develop and start to move up the value chain from generic white-label items to global brands. In some cases, the supply side begets new business on the sales side – as larger companies look to new, smaller suppliers with niche technology or expertise to improve their manufacturing efficiencies, those suppliers in turn invest in more advanced technology and tooling (perhaps in turn purchased from new overseas suppliers) to fulfil these orders.

Another motivation for supply chain diversification/fragmentation has been risk: long-standing suppliers in developed markets may now be financially pressured due to the reduced availability and higher cost of working capital funding from external sources. For example, a high-tech company with key suppliers in Europe may be concerned that these suppliers are financially stressed and as a prudent operational risk management measure may also start sourcing similar components from an alternative supplier in a less financially pressured location, such as Taiwan.

The bottom line is that there is now more complexity in the way that global trade is conducted because trade flows have become inherently more diverse.

New Connectivity

While this diversification of trade flows may bring efficiencies, reduced risk and new sales opportunities, the corollary is increasing complexity in financial supply/sales chains. New transactions in the physical supply chain beget new transactions in the financial supply chain.

This has implications on several levels. On the cash management side, there is a need for better connectivity solutions capable of making/receiving payments in a wider range of locations and, just as importantly, accessing and managing the information associated with these payments.

The financial risks involved in increasingly diverse supply/sales chains are also more complex. Trading counterparties that were once in the next town are now on the next continent or far beyond, so where will the credit information necessary to understand how financially strong or weak they are come from? Who will provide the market intelligence on suppliers and customers who may be thousands of miles away and whom you have never seen? How can that intelligence be managed to assist in delivering supply/sales chain solutions for these suppliers/customers should they be needed?

> **"Remote new locations may necessitate new bank relationships in order to achieve coverage, but how will the connectivity required to communicate efficiently with these new banks work?"**

A further related consideration is banking relationships. Remote new locations may necessitate new bank relationships in order to achieve coverage, but how will the connectivity required to communicate efficiently with these new banks work? Can your lead bank provide robust third-party bank connectivity? How will you manage the day-to-day operation and reporting of these new accounts without a ballooning time/process overhead? By the same token, how will you manage the administration of matters such as changing signatories on accounts? How will you maintain a suitable level of security across new banks and accounts without a massive proliferation of identity tokens and security keys?

There is also the question of project management to consider. As new commercial relationships proliferate, new processes, technology and business structures are required to support them. To maintain efficiency, a degree of centralisation, such as the implementation of a regional treasury centre (RTC) or shared service centre (SSC) will often be required. That, in turn, raises the issues around effective project management. If a new RTC or SSC is being implemented, this will require hooking up in-house systems to potentially multiple external connections, so how can this process be made transparent so that it can be remotely as well as locally managed? For instance, how will senior treasury personnel in a head office location perhaps thousands of miles away be able to monitor project progress effectively?

Connectivity and the Supply Chain

Connecting the Financing Dots

As supply and sales chains continue to fragment and proliferate globally, so does the need to finance them. New suppliers and distributors in emerging markets may be highly efficient in a manufacturing cost or profitability sense, but they may lack the working capital capacity to afford the credit terms a larger corporation may expect.

While supply/sales chain financing can fill this gap by leveraging the credit rating differential between a large customer/supplier and smaller suppliers/distributors, connectivity is again a critical component. Pre- and post-shipment financing structures are always provided with ultimate recourse to the supplier, because however creditworthy the buyer is, that buyer can always say no. Therefore, the financing bank has to be able to underwrite the supplier, so the supplier still has to be bankable.

In the current global environment, this means that financing banks that cannot physically reach out and touch both the supplier and buyer ends of the supply chain are of limited use. This connectivity is essential because rising compliance and regulatory requirements (such as those relating to money laundering and terrorism) are putting increasing pressure on banks to conduct rigorous due diligence on each participant in the supply/sales chains they finance.

That requires high quality bank connectivity in two areas. Firstly, in terms of the technology needed to support the day-to-day operation of increasingly complex supply chains. Secondly, as regards connectivity and networks in disparate global markets to deliver the requisite local intelligence to satisfy regulatory/compliance requirements. The bank should also be able to leverage this local intelligence and deliver it in a manner that makes it easy for its clients to stay abreast of regulation that may affect their own business in existing and new markets.

Neutral Connectivity

As larger corporations look to leverage their supplier base in order to meet their own working capital targets, this is raising the need for neutral connectivity. This situation arises as a result of increasing supply chain fragmentation and diversity. As companies look to tap a wider range of suppliers in the interests of cost, risk and efficiency they reach into new territories where the attitude of smaller companies to technology differs from developed markets. These smaller companies are not investing in the technology often associated with supply chain processes: a small company in Vietnam is unlikely to invest in a full-blown enterprise resource planning (ERP) system to oblige even the largest Western multinational customer.

As a consequence, large corporations now place heavy emphasis on single-stream, neutral technology. The functionality of bank platforms was a competitive differentiator 10 or 15 years ago; today the neutrality of the bank technology is the key selling point as corporations look for technology that will facilitate the onboarding of new and diverse trading partners.

Pragmatic Connectivity

While neutral connectivity goes a long way towards facilitating the extension of new and more complex global supply chains, there are some practical limitations. In most developed markets, technology is part of everyday consciousness, so there is a natural tendency to default to technology as a means of improving efficiency and reducing cost. However, in many developing markets the drivers are very different. In a country where the majority of an individual’s income is spent on food, there is a pressing need to maintain the fullest possible employment. Labour rates are also low, so the need to reduce costs through technology and automation is less pressing.

> **“In some cases, the local infrastructure makes mainstream technology impractical: for example, parts of certain countries in Asia do not have a complete electricity grid.”**

For example, in Vietnam a small percentage of the letters of credit that HSBC currently issues are requested electronically, the vast majority of requests come via fax or in the post, because that is the approach the market and clients prefer rather than using the latest technology. In some cases, the local infrastructure makes mainstream technology impractical: for example, parts of certain countries in Asia do not have a complete electricity grid.

As a result, there is a need when dealing in many emerging markets to avoid the trap of automatically mapping across developed market approaches to technology. This applies to both corporates and banks; ultimately, the corporation needs a banking partner that can deliver the greatest possible efficiency and automation that local conditions allow, not some unrealistic utopian ideal that doesn't work.

Connecting Through Technology: The Client Experience

Integration and Centralisation

The liquidity pressures arising from the financial crisis have seen many treasurers looking for technology-driven solutions that can provide future-proof platforms for cash and treasury management. Important aspects of this future-proofing include integration, centralisation and automation.

- Integration: Any technology that is future-proof with regard to integration will reduce costs and disruption by allowing new data feeds, transaction channels and banking partners to be easily added. This was one of the reasons that some corporates took a new interest in SWIFT during and after the financial crisis. While they had previously devoted considerable effort to rationalising bank relationships, they realised that this carried a concentration risk when certain of their core banks were no longer able to provide sufficient liquidity. SWIFT therefore looked attractive as a fast and efficient way to connect to new banks to access the necessary credit.

- Centralisation: The crisis also meant that many treasuries and boardrooms became acutely aware of the need to maximise their use of internal liquidity to reduce dependence upon external sources that might no longer be available. As a result, centralised bank account visibility and control became a key focus in order to minimise the incidence of invisible and idle cash, as well as to improve cash forecasting.

- Automation: While automation obviously reduces cost and minimises the scope for manual errors, there is a growing appreciation that it can also support a faster sales cycle. In accounts receivable, automated reconciliation can expedite the freeing up of available credit limits on customer accounts, thereby allowing faster rotation of sales and shipments.

The Demise of Proprietary Standards

Most treasuries are now aware that the use of proprietary banking standards and technology is a major barrier to better connectivity. As the number of bank relationships increase due to more complex and diverse trading relationships, so does the number of bank interfaces and formats that corporate personnel have to master, which increases the data management workload as well as the risk of errors.

A related issue is that multiple relationships have historically required multiple log-on details and security tokens. This can easily result in convenience overriding security, such as when security credentials are written on slips of paper. It also creates significant upheaval when personnel leave a company and multiple sets of their security credentials have to be revoked and new ones requested for their replacement.

This has driven greater corporate interest in SWIFT as a means of avoiding the overhead of proprietary banking standards and technology. It provides a single neutral gateway to potentially any bank connected to SWIFT, which improves efficiency and convenience – especially when coupled with a common standard such as ISO20022. This single point of access also makes contingency planning seamless, in that it becomes relatively straightforward to route transactions via a secondary provider if the primary bank is temporarily unable to process transactions.

> **"SWIFT's neutral technology also offers advantages when it comes to the management of security credentials."**

SWIFT's neutral technology also offers advantages when it comes to the management of security credentials. Its 3SKey concept opens the door to multi-bank, multi-application, multi-network and multi-country secure identification using just a single device. A corporate using 3SKey can obtain an inactive token from any participating bank and then authorise this token on SWIFT's 3SKey portal. The same token can then be associated (registered) with multiple banks and used to sign messages relating to transactions with those banks. Each bank then individually verifies the resulting electronic signature and its revocation status. Apart from streamlining day-to-day transactions, this model also means that should an individual leave the corporation, all their security credentials across multiple banks can be revoked in a single step by cancelling their token, which can also be done if a 3SKey is stolen or otherwise compromised.

eBAM and Electronic Trade

This sort of technology is an important component in the progress towards electronic bank account management (eBAM) via SWIFT. As supply chains become more complex and geographically diverse, so can bank relationships – hence the need for the most efficient and practicable way of managing them.

Some global banks already support eBAM using SWIFT so, for instance, much of the preliminary information gathering and requests for additional data that are part of the process of opening new bank accounts can be conducted electronically. In comparison with multiple iterations/versions of paper documents circulating by post, this represents an appreciable efficiency and speed gain. One caveat is that eBAM also depends upon technology vendors as well as banks in order to function properly and while some major ERP/treasury providers already support it, not all do – so some manual amendments and patching may still be required.

> **"As supply chains become more complex and geographically diverse, so can bank relationships – hence the need for the most efficient and practicable way of managing them."**

A similar situation applies to electronic trade. SWIFT MT798 messages already provide the necessary electronic envelope for documentation and guarantees. A number of major banks also already support SWIFT for trade transactions and there is strong pent-up demand for the concept in regions such as Asia. However, as with eBAM, comprehensive support from vendors of multi-bank trade platforms is also required in order to complete the picture.

ERP Integration and Project Management

ERP system implementations and upgrades represent some of the most labour-intensive projects any corporation will undertake. From a treasury perspective, the same has also held good for ERP integration with banks. Fortunately, this situation has improved recently, with a select group of major banks collaborating with major ERP vendors and SWIFT to develop a toolkit that vastly simplifies and expedites this integration process.

However, the wider implications of any changes made to an ERP system's financial module for the company as a whole means that any bank providing such a toolkit also needs to offer specialist consultants for the ERP system concerned who can flag up such implications. This is vital if needless disruption elsewhere in the organisation is to be avoided – a seemingly innocuous change to a finance module may inadvertently cause complete mayhem in another ERP module or business area. The same applies to SWIFT expertise – any bank purporting to offer a streamlined route to ERP/SWIFT/bank integration also needs to be able to deliver SWIFT consultants of the same calibre.

“... the right technology can play a role here by providing a project management platform that is remotely accessible and allows both reporting and interaction far more quickly and comprehensively than telephone or email.”

The availability of this range of expertise is clearly essential to the success of any project involving ERP/SWIFT/bank integration, but it still leaves open the matters of oversight and management. In a commercial environment that now spans multiple time zones and where much new activity may be in remote emerging markets, those ultimately responsible for a project may be thousands of miles from its epicentre. Again, the right technology can play a role here by providing a project management platform that is remotely accessible and allows both reporting and interaction far more quickly and comprehensively than telephone or email.

Mobile Technology, the Way Ahead?

As mentioned earlier, there is a need for pragmatism when it comes to connectivity – especially when dealing with new trading partners in countries where technology may not be the default option. Yet in some of these countries, a different slant on technology may be highly appropriate. In many Asian countries, communication has taken a shortcut; the migration from fixed line telecoms to mobile never happened because fixed line infrastructure never really existed in the first place. Instead, these countries leapt straight to the latest mobile technology and progressed from there. As a result, countries such as Malaysia are already advertising 4G mobile telephone coverage in certain areas.

The SME that can offer a major corporation on the other side of the planet highly competitive pricing on certain components may never invest in an ERP system, but it may already be an active user of mobile technology. Corporations and banks that respond to that by deploying interfaces and applications for tablets and other mobile devices may find that the technology circle can actually be commercially squared.

Conclusion

In a world where trading relationships are becoming ever more intricate, the connectivity required to support them obviously has to keep pace. Achieving this requires a combination of partnerships and flexibility. At one level, banks, infrastructure providers and technology vendors that collaborate effectively can hugely improve the connectivity experience and efficiency of corporations. At another, these same entities, together with corporations of a suitably pragmatic mindset, may find ways to tap the best opportunities in the supply chain – even to the level of the smallest SME.

Achieving this requires the rapid circulation of information in a consistent format that encourages the widest possible adoption. This is a role that the standards supported by SWIFT are ideally suited to fulfil because they act as a common touch point for corporations and financial institutions alike. In doing so, they will facilitate the expansion of global trade both geographically and demographically.

Fortified Against Future Financial Crises?

- Now, post the financial crisis of 2008-2009, it might be the right time to ask what has been learned from this experience to help prepare for the future.
- While large corporates withstood the crisis better than smaller ones, all companies have faced surprises and problems and would do well to assess their mistakes to avoid repeating them.
- Some fundamental lessons that are worth reiterating include simple, basic things that are sometimes overlooked.
- All companies will recognise at least one area – maybe more – that can be fortified to prepare for the next crisis.

Damian Glendinning, Vice President and Treasurer, Lenovo and President, Association of Corporate Treasurers, Singapore

It is widely believed that humans learn from past mistakes. Yet there is nothing in history to suggest this is the case – why else do people build houses on the sides of volcanoes, or in floodplains? Surely cold, rational finance types are more logical and will always make future systems more robust, thanks to lessons learned? Apparently not.

You only have to look back to the Dutch Tulip Mania of the 1630s to realise that speculative asset bubbles fuelled by excessive leverage are nothing new – nor is the way in which they collapse. Tulips were introduced in Holland in the early 1600s, and people liked them so much, that a speculative craze developed. At one point, the rarest tulip bulbs sold for over 10 times the annual salary of a skilled craftsman. People borrowed to invest in tulips – then lost everything when the market collapsed. The cause of the collapse? The usual problem – people starting to worry whether the trend could continue.

Now that the world has emerged from the crisis of 2008-2009 – the most severe since the Great Depression – it might be the right time to ask what has been learned from this experience. Now that the global economy is stronger, have businesses taken advantage of the better times to make sure that they are prepared for the next storm? Because one thing is certain – there will be future storms.

The Crisis of 2008-2009

The simplified explanation of the crisis is that several years of easy lending policies had led to the creation of asset bubbles, particularly in US real estate. Thanks to complex financial engineering, mortgages were given to buyers who had no hope of ever repaying the loans, and the resulting debt instruments were widely marketed as high quality credits. At the same time, asset booms were taking place around the world, fuelled by cheap and plentiful cash.

The Authorities' Reaction

Fortunately, the central bankers had learned from the Great Depression. They had not prevented the bubble from forming, but when it burst, they were prepared – they knew what to do. Though they have been heavily criticised, there can be little doubt that the measures taken to provide the markets with liquidity were effective in preventing much more serious and longer lasting damage.

However, as recent events have demonstrated, they have not been able to cure the underlying problems. Providing unlimited additional liquidity to keep markets moving was necessary – but it is unlikely to be an effective long-term cure for excessive debt levels and over-leverage. More importantly, there is little reason to be optimistic about the legal and regulatory reforms that finally are being made by the politicians to avoid a repeat.

How Did Corporates Fare?

Generally, larger corporates entered the crisis with stronger balance sheets than usual, and most survived surprisingly well. There was no major, large-scale liquidation – the bankruptcies of two major US car manufacturers were the confirmation of problems that had existed for a long time, and both companies emerged from bankruptcy quickly.

Things were not so rosy for the smaller companies – a reminder that life is much tougher for small companies.

So, What Are the Lessons?

The crisis brought home the need to perform basic tasks, diligently and well. In summary:

- Excessive leverage is dangerous.
- If you need to borrow, match your liabilities to your assets.
- Markets may be here today, but they can be gone tomorrow.
- Read the fine print in your loan agreements.
- Maintain good relationships with your banks – you never know when you might need them.
- Currencies are volatile and stability is an illusion.
- Manage your counterparty risk carefully.
- If you do not fully understand it and cannot model it, do not buy it.
- Do your funding in good times not once the crisis has hit.
- If something seems too good to be true – it usually is.

Excessive Leverage is Dangerous

Debt is a necessary part of doing business. A good balance sheet structure will include some, but every business must ask itself the question: how much debt is too much? It may be easy to obtain debt in a favourable market, but this can become life threatening if the market tightens.

During periods of economic growth, there is a lot of pressure to return cash to shareholders, to improve return on equity (ROE). Conservatism is often frowned on, especially by some of the more active shareholders or aggressive analysts, but when the sources of funding dry up overnight, as they did in the case, for example, of the US commercial paper (CP) market, a highly leveraged business can quickly find itself struggling.

What is the right level of debt? It is not easy to say, but when deciding, it is essential to ask what will happen if access to funding suddenly dries up.

Today, interest rates are exceptionally low. How many companies with floating rate debt are looking at what will happen to their interest coverage if we return to "normal" rates (for example, one month LIBOR at 5%)?

Another lesson that needs to be learned from the crisis is not to assume it cannot happen, no matter how unlikely it looks now.

Match Your Liabilities to Your Assets

Matching liabilities to assets may seem obvious, but it is something that many companies fail to do well. The crisis exposed at least one major conglomerate with a significant financing arm that was funding long-term financial assets with very short-term borrowing. This is attractive – charging customers higher, long-term, rates, but access funding from the short end of the yield curve.

Of course, it is difficult to persuade any business to accept the higher funding cost that goes with long-term, fixed-rate funding. However, if assets are long-term assets, producing returns that are essentially fixed, this is the right approach.

This notion does not only apply to financial institutions. A company building a large factory with a lot of capital equipment should use long-term and fixed rate funding to ensure the business model covers the ongoing cost of funding the assets.

Many companies continue to fund this kind of investment with floating rate debt, on the grounds it is cheaper, sure that interest rates will not rise any time soon and that they can successfully time the market and move to fixed rates before it is too late.

Markets Are Fickle

The most dangerous assumptions are the subconscious ones. Below are a few assumptions that have long been automatically accepted – until recent events:

- The US CP market is always deep and liquid.
- The US government will always be rated AAA.
- Being downgraded makes the cost of debt go up (the US government's has gone down).
- LIBOR means the rate at which banks actually lend to each other.

The point is that many companies and institutions found themselves with a problem in 2008-2009 because they had assumed one or another market or source of funding would always be there and available for them.

Understand Your Loan Agreements

The accepted covenants and clauses when negotiating loan agreements may seem reasonable at the time. Financial covenants are an inevitable part of bank loan agreements. However, during the crisis, even covenants that had seemed very remote became tripwires. Therefore, it is important to have a good understanding of what will cause a breach and be ready to communicate early with lenders.

The clause that caused several companies significant problems was something few would normally pay a lot of attention to: the market disruption clause. When invoked, this caused companies to go from a LIBOR-based rate to paying the bank's cost of funds, which it was impossible to verify.

Maintain Good Relationships With Your Banks

While there is much discussion about the merits of relationship banking, there can be no doubt about the truth of the old adage: it is in difficult times that you find out who your real friends are. It is always important for companies to make sure that relationship banks understand their business, and what makes it work. When faced with a crisis, banks are forced to trim their exposures due to the constraints they face, and companies need to ensure that they are on the list of relationships the bank wants to preserve.

Equally important is ongoing communication. Problems identified and communicated in advance are easier to deal with – and the company is recognised as being competent and professionally managed. No matter how good a company's relationship with its bank, it is not helpful to demand help at short notice, as many companies did in 2009.

Currencies Are Volatile

Currency hedging generates significant debates in most companies, and is too large a topic to cover comprehensively in this article. One of the biggest problems is that most companies have many currency experts – unfortunately, most of them do not work in treasury.

It is true that a good hedging programme costs money, in terms of the actual cost of hedging, opportunity costs if potential gains are lost, and, above all, in the administrative effort required to gather data and monitor exposures.

Manage Counterparty Risks

Managing counterparty risk is another thing everyone agrees is necessary, but which encounters a lot of resistance in practice.

Again, the crisis showed that it was important to have processes already in place for looking at all counterparties, and understanding all risks, even those that were not immediately obvious. While some changes are needed, it is much easier to adapt existing processes than to start from scratch in the middle of a crisis.

Now that the crisis has passed, it may seem tempting to lower the level of vigilance.

If You Cannot Model It, Do Not Buy It!

Low interest rates are good if you are borrowing. Unfortunately, they also reduce returns on excess cash. This increases the pressure to take more risk to enhance yields, including various forms of structured products.

Unfortunately, the laws of investing do not change. Just as there is no free lunch, so there is no high yield without risk. Enhanced yield money market funds and auction rate securities are just two examples of apparently safe investments that burned investors who prided themselves on being prudent.

Do Not Wait for a Crisis to Organise Funding

One of a treasurer's bigger challenges is persuading the business to incur fees and interest expense when times are good, and when the need for funds is not pressing. However, this is nothing compared to the challenge – or the cost – of raising funding when times are bad.

Conclusion

This is not meant to be an all-encompassing list of what can, and did, go wrong. It is also not meant to be an endorsement of arch conservatism, or a pessimistic assessment of the world and its economy. Taking risk is an essential part of business. Without risk, there is no reward, and no profit.

This does not take away the fact that one of the treasurer's key roles is to be aware of risk, and to manage it. This should not be confused with avoiding risk. However, we cannot get away from the fact that a key aspect of the role is to be the critical eye, be the person who asks what happens if things go wrong. While the aforementioned list of problems and errors may seem simplistic, the majority of companies will recognise at least one area in their own organisation where things did not turn out as well as expected.

There has been a period of nearly two years of relative calm in the markets when treasurers should have been examining the problems they experienced in 2008-2009 and looking at ways to avoid experiencing those problems again. There is considerable evidence to indicate that the world is entering a new crisis. This time, treasurers cannot say they have not been warned.

Three Phases of Treasury Evolution

David Blair, Independent Treasury Consultant, Singapore

- Usually, at an early phase in its evolution, treasury is inward looking, concerned with optimising its own efficiency.
- In the next phase, treasury looks outwards to the rest of the company, to optimise treasury-related processes at a company-wide level.
- In the final phase, treasury looks to optimise the company's entire supply chain, as the focus shifts from department to enterprise to customer.
- There are various dimensions of treasury evolution – such as demand chain management, risk or technology – and each expresses itself uniquely according to the underlying needs of a business.

Treasury suffers from the intrinsic problem of being non-core to the commercial enterprises that it serves. Treasury is thus condemned to the role of a back office department. In this role, it can be hard for treasury to connect with the core objectives of the business. This in turn can cause treasurers to focus on professional efficiency and optimising the treasury department rather than to look at the wider picture.

Treasurers understand that their role is critical to their enterprises' health and even survival. Simply ask sales people if they want to be paid in sales – or even profits – or in cash! However, even treasury-relevant goals like cash flow can seem remote from the day-to-day focus on cash planning, funding, investment and foreign exchange (FX).

Of course, the basics – the sometimes conflicting goals of risk and cost reduction – will always be crucial to successful treasury, especially the key risk of liquidity, of ensuring sufficient cash for operations. Unfortunately, these are negative successes. The exceptions are enterprises that have experienced near-death cash flow deficits. If they survive, senior management tends to place serious emphasis on cash flow.

To a large extent, treasury is a hygiene function, whose role is to make sure that:

- there is cash where and when needed (liquidity risk and cash management in the short term and corporate finance and capital structure in the long term);

- there are no surprises (risk management); and
- there are no losses or bad press (operational risk management).

Phase One – Efficient Treasury

Because the enterprise needs healthy cash flow to survive, it is crucial that treasury operates efficiently. Just because it is underappreciated does not mean it is unimportant to get the foundations right. The basic requirements for an efficient treasury are:

- a treasury management system (TMS) to ensure operational efficiency and risk visibility;
- straight-through processing (STP) to reduce operational risks and costs;
- visibility over cash to optimise use of cash and reduce cost of liquidity;
- cash planning to support optimum use of cash;
- sufficient resources (both quantity and quality) to reduce risks and costs; and
- other treasury basics.

Looking through this list immediately reveals that even basic treasury cannot happen in a vacuum. Treasurers often struggle with issues such as:

- no budget to implement TMS or hire appropriate staff, because treasury is underappreciated;
- no visibility over cash because subsidiaries consider it to be "their cash"; and
- weak cash planning because cash flow is not on other people's list of objectives – e.g. sales plans are based on sales volumes not cash collection, production planning is based on units without taking into account currency, value or timing.

Even in this first phase, treasury is heavily dependent on the rest of the business to achieve its goals. This is as it should be because, after all, treasury is a support function and not a core business. It is rightly incumbent on the support function to adapt and to be sensitive to the needs of the core business.

> **"Even in this first phase, treasury is heavily dependent on the rest of the business to achieve its goals ... the upside of this challenge is that building the connections required for this first phase of efficient treasury prepares the treasury team for future integration work."**

The upside of this challenge is that building the connections required for this first phase of efficient treasury prepares the treasury team for future integration work. Indeed, the first phase flows naturally into the second phase in the sense that as treasury resolves some of the issues listed above, it inevitably becomes closer to the underlying business.

This closeness to the business or business intimacy can develop in different ways depending on the nature of the business. If the business is highly integrated, treasury will focus on finding the right touch points to plug into the relevant data streams. In a diversified business, treasury will focus on discovering and exploiting needs that are common across the different parts of the business.

Listening is key to business intimacy. Listening provides treasurers the opportunity to learn about the underlying business and, perhaps even more importantly, to learn about pain points that can provide opportunities for treasury to bring solutions that can help the underlying business while hopefully improving the company's performance and growing treasury's business intimacy. For example, in the context of a multilateral payment netting rollout, if a business has a problem with intercompany reconciliations, invoice level netting could provide the solution; or if the business has a problem with cross-border vendor payments (and bank solutions like payment outsourcing are too expensive and cumbersome), including third-party payments into the netting process could solve the problem.

Sometimes, if there is a misalignment of objectives – for example, a focus on sales rather than cash flow or a lack of appreciation of risk – then it may be necessary to focus on pushing for metric changes. Most best-practice metrics encourage cash awareness; for instance, the importance of the capital denominator in return on capital (ROC) and economic value added (EVA).

A Note About Liquidity – Manual Sweeps, Controlled Disbursement, Sweeping Pooling Overlay and In-house Bank

Basic liquidity management may look like a simple issue and one belonging clearly to treasury, but problems with ownership of cash and legacy processes can quickly complicate matters. As treasury progresses from controlled disbursements and manual sweeps to automated sweeping and pooling and overlays, new bank partners and bank account rationalisation can mean changes in working practices that may not be well received by colleagues and, in some circumstances, even customers and suppliers.

Typical key performance indicators (KPIs) for this phase include:

- operational efficiency metrics like fully loaded cost per transaction;
- cash efficiency metrics like percentage of accessible cash; and
- balance sheet metrics like leverage.

In a company that has not learnt the hard way about the importance of cash flow (i.e. through a cash flow near-death experience), treasury has to promote cash flow awareness throughout the company in the hope that colleagues never have to learn the lesson the hard way.

Phase Two – Efficient Enterprise

Once sufficient foundations of efficient treasury are in place, the second phase is to look at enterprise cash flow efficiency. As stated above, there is inevitably overlap with the first phase of treasury efficiency, since treasury does not exist in a vacuum and depends on the business in an integral way. To make core treasury activities efficient, it becomes clear that there is a need for data streams from, and close cooperation with, the underlying business.

It can help tremendously with cash flow reporting if treasury can move away from being a passive recipient and consolidator, or worse, trying to cobble together a cash flow forecast from other colleagues' dustbins (so to speak), towards a participatory dialogue with colleagues about expected cash flows. Since the only certainty about any forecast is that it will be wrong (to some extent), getting flavour or colour for the numbers can greatly reduce the risk of wrong transactions.

Many treasury techniques that are no longer considered leading edge – like controlled disbursements, sweeping and pooling and multilateral netting – have significant impacts on processes and results in the underlying business. Implementation of such techniques will raise the profile and visibility of treasury, but will require buy-in from different parts of the enterprise.

For example, in this phase treasury will need intimate familiarity and close working relationships with the enterprise partners responsible for accounts receivable (A/R) and accounts payable (A/P) – typically sales and procurement departments. A specific example might be the impact of a payment factory operating model on vendors – efficiency measures may change payment frequency (typically to reduce it) and aggregation may change the flows for vendors. Treasury will have to ensure vendor buy-in – directly or indirectly through procurement colleagues – if they want the new process to be successful; this is normally achieved by explaining the process efficiency on the vendor side due to lower collection volumes, better reconciliation, more consistent collections, and better predictability of collections.

Another area for development, adjacent to core treasury, is supply chain financing. Different techniques for supply chain financing can be used to support suppliers and/or customers and distributors depending on the industry constellation as well as to manage the balance sheet of the enterprise itself. In any case, such arrangements cannot work without close cooperation with procurement and sales colleagues respectively.

“Developing supply chain financing is moving a step closer to the third phase – an efficient supply chain; the difference is that, in the second phase, treasury is looking at these techniques with an inward enterprise focus rather than an outward focus.”

Developing supply chain financing is moving a step closer to the third phase – an efficient supply chain; the difference is that, in the second phase, treasury is looking at these techniques with an inward enterprise focus rather than an outward focus.

Another key aspect of the second phase would be promoting enterprise-wide cash consciousness, assuming the organisation is not already cash conscious. This may involve education to raise awareness. Ultimately, this effort must bring cash consciousness into performance metrics. Examples include moving towards a focus on the capital denominator in various ROC metrics and in EVA or adopting cash conversion cycle (CCC) or net working capital (NWC) ratios directly. For example, sales people who are rewarded exclusively or predominantly on sales or order flow rather than cash flow will not demonstrate strong cash consciousness – even if they understand intellectually that they want to be paid in cash rather than in revenue.

In this second phase of enterprise efficiency, treasury can add significantly more value to the whole enterprise in terms of lower costs, reduced risk, potentially enhanced customer satisfaction and higher profitability.

Phase Three – Efficient Supply Chain

After reaching beyond the treasury department to look for enterprise-wide efficiencies, the next natural step is to look beyond the enterprise to the whole supply chain with a view to optimising the end customer experience. Clearly this is a stretch in a world where few companies – let alone treasury departments – actively manage their supply chain in a holistic manner. However, it is clear that this is what the best companies do and this must be the goal of companies that combine complex supply chains with customer ownership.

Enterprises that do not necessarily fit the complex supply chain with customer ownership models will inevitably rely on some kind of ecosystem that has to be nurtured. Business nurturing involves cash. Cash involves treasury. Companies that have been through the second phase and attained enterprise efficiency will have a deep understanding of their underlying business and how treasury can enhance their enterprise's ecosystem.

> **"Companies that have been through the second phase and attained enterprise efficiency will have a deep understanding of their underlying business and how treasury can enhance their enterprise's ecosystem."**

In classic supply chains, two obvious and pertinent areas that are often inefficient are use of capital in the supply chain and process efficiency in the supply chain.

Capital is an obvious and core concern of treasury – and many supply chains use capital very inefficiently. Studies have shown that funding required can be two to four times the end user sales price of the end product because of overlapping funding needs of successive parties in the supply chain.

These can be resolved by ensuring visibility across the supply chain to the funding entity, which might be a bank or a bank panel or even a dominant company in the supply chain. Such visibility is hard or impossible to achieve with a paper-based supply chain but easy in an electronic or digital supply chain. This brings us to the area of supply chain process efficiency.

Obviously, supply chain per se is not normally a core competence of treasury. However, after successfully delivering STP across treasury in phase one and across the enterprise in phase two, treasury may be well positioned to add value in improving supply chain efficiency with relevant electronic platforms or e-workflow and STP across the supply chain.

Metrics for this kind of work might include capital used across the supply chain as well as operational effectiveness metrics relating to supply chain-wide STP, which will reduce costs and operational errors. Most companies find they waste considerable time and effort on invoicing errors and reconciliation of A/R and A/P with partners. This effort does nothing for profits and it does not contribute to customer satisfaction.

With these two steps in place, treasury can work with colleagues within the enterprise and with supply chain partners to drive down working capital tied up in the supply chain (effectively improving net working capital rotation across the whole supply chain and lowering supply chain-wide funding costs), and thereby reduce costs, increase profits, grow market share, etc.

Corporate Diversity

A key point that needs to be reiterated is that the three phases can overlap. Treasury evolution may not be linear in the manner described above; the linear description is primarily for illustrative purposes.

For some treasuries, certain second and third phase skills will be early focus areas because of their criticality to the business. For instance, enterprises involved in long-term project or solution sales often develop deep customer financing skills from the start because this is such a critical component of the sales process. Another example might be trading companies that are often very skilled at managing long supply chains – traditionally through letters of credit. A third example might be the ingenuity of firms in regulated markets where scarce capital forces supply chain sophistication – an example is the use of corporate and bank acceptance notes in the People's Republic of China.

Multiple Dimensions

The dimension discussed above – moving from inward to outward focus – is just one of many dimensions of treasury evolution. Others would include:

- Corporate finance and capital structure: Focusing on well diversified funding and investor base, optimal weighted average cost of capital (WACC), etc. and liquidity gapping.
- Risk management: Dealing with market risk, especially in FX, interest rates, commodities, etc.
- Operational effectiveness: Tackling areas such as headcount, costs, operational risk management and sustainability.

Arguably, most of these are done within treasury; even so, an outward focus is a sign of treasury sophistication.

Working Capital Management

New Regulation: The Impact on Corporate Liquidity Management

- The backdrop to global liquidity management has changed significantly in two specific areas since the financial crisis – international banking standards and local regulation.
- New regulations such as Basel III have important ramifications for corporates across many aspects of their liquidity management.
- Corporates will face a range of challenges and potentially conflicting objectives in their attempts to optimise liquidity.
- More extensive and consultative terms of engagement with banks will be the key to facilitating the evaluation and recalibration of the liquidity management arrangements in an evolving environment.

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One of the many consequences of the global financial crisis has been a major shift in the nature of regulation. While some corporations may assume that macro-level regulatory changes, such as Basel III, are a matter purely for banks, the consequences are, in fact, far more pervasive. As this article explains, imminent regulatory initiatives will have a significant impact on corporate liquidity management.

A Holistic Approach

The ongoing need to improve the efficiency of liquidity management is currently driving some fundamental changes in the approaches being adopted. One of the emerging changes is the move away from the traditional regional approach to liquidity management. Instead, corporations are now examining their individual flows and trying to determine the best bank to use in managing a particular group of currencies or liquidity corridors. Geographical network footprint is no longer the only consideration; international connectivity quality has also become a primary factor. Opportunely, this more holistic approach is likely to pay dividends in a regulatory environment in the throes of significant change.

Centralisation

Centralisation of functions that affect liquidity management – and centralised visibility over their operation – has been an important theme for treasury in recent years. At an internal operational control level, this might consist of moving finance or treasury processes such as accounts payable, accounts receivable, investment and funding away from local business units and into a shared service centre or a group treasury. At a visibility and oversight level, a variety of information and workflow management systems, including specialised cash management applications provided by banks, are available to provide regional and central treasury with a consolidated view of liquidity-related activities. Finally, at an execution level, a range of services are offered by banks to support the domestic and international transactional and financial needs of global enterprises.

In combination, these changes are typically associated with the following specific objectives:

- improved treasury control of sources and uses of cash within an efficient working capital management framework;
- free movement of available liquidity across legal entities and geographies; and
- optimisation of expenses and returns, while mitigating financial and liquidity risks.

In the aftermath of the global financial crisis, where it has become far more challenging to source external liquidity economically, the validity of these objectives has been reconfirmed. Therefore, centralisation understandably remains a major priority for many treasuries.

However, a more recent objective underlying centralisation has been future-proofing; corporate treasuries are keen to avoid the risk of compromising future global opportunities as a result of earlier regionally- or domestically-focused decisions. As a result, some of them are re-evaluating their existing liquidity structures and providers. In many cases, the underlying intent is to move all liquidity (subject to regulatory constraints) to a single global point, which obviously allows liquidity to be distributed across the organisation efficiently.

Another driver for these reviews has been the rapid growth in intra-regional trade – particularly, but not exclusively, in Asia – which has given rise to new or larger liquidity flows that were perhaps not anticipated. This has led to a need to devise ways of optimising these new liquidity corridors, which in turn requires the reassessment of optimal commercial practices and of existing bank account structures in the interests of efficiency.

The reason behind such re-evaluation of the centralisation of liquidity is that it will further improve the maximum possible access to internal sources of cash. In view of the probable consequences of future banking regulation, the cost differential between internal and external liquidity is only likely to increase. Therefore, centralisation of liquidity to a single global focal point will not only minimise borrowing costs and maximise investment return, but also improve the management of liquidity risk and the usage of external credit facilities.

As with the more holistic approaches to liquidity management now being adopted, this re-evaluation is also particularly timely given the regulatory changes taking place over the next few years, which will drive significant changes among bank providers.

Multi-currency Exposure Management

One important facilitator of the centralisation trend is the wider availability and flexibility of multi-currency liquidity structures, particularly as regards multi-currency notional pooling. Liquidity can now be extracted and delivered globally to the most appropriate places in the most appropriate currency. Furthermore, this can be achieved without incurring the frictional costs of physical conversion or where conversion is required it can provide additional flexibility in managing its timing. The locations and range of currencies that can be incorporated in such a liquidity structure also continue to increase, with in excess of 30 currencies potentially participating at any single location.

These developments are especially timely in view of the internationalisation of the Chinese yuan (CNY), also known as the renminbi (RMB). China's importance as a manufacturing hub and consumer market has resulted in an increasing number of foreign corporations having substantial commercial flows with China. The recent deregulation of certain trade flows has opened up a number of opportunities to create a significant and growing off-shoring of the RMB. Once offshore, the RMB can be integrated into an international liquidity structure.

However, while some RMB-denominated investment products are increasingly available in Hong Kong, the choice is still very limited and returns are low at this stage in the development of the offshore RMB interbank and money markets. Liquidity supply and demand in the offshore markets remain tightly controlled by the Chinese authorities.

This combination of circumstances represents an important opportunity. As it is already commercially possible to include RMB in a multicurrency notional pool, for many corporations this will be a more attractive option than the limited range of offshore RMB investment offerings currently available. Essentially, the marginal rate of return on RMB participating in a multicurrency pool (versus being on overnight deposit) is likely to be considerably better due to the current, and probably expanding, spread between internal and external liquidity costs that will be increasingly driven by regulatory change. Moreover, a multicurrency pool permits the management of long and short positions across different currencies, simulating currency hedges that can be operated according to the specific hedging policy in place.

Changing Landscape

The backdrop to global liquidity management has changed significantly since the financial crisis in two specific areas – international banking standards and local regulation. Furthermore, neither is likely to prove static and neither is likely to be globally consistent in terms of application. This is obviously intrinsic in the case of local regulation, but in the case of Basel III, local regulators are already making their own interpretations and rulings (e.g. Dodd-Frank and flexible spending account cap requirements/thresholds), which adds local variation to overall principles. Both will have important liquidity management implications for corporate treasuries that will need to be addressed.

Basel III

In response to the 2008-2009 financial crisis, the Basel Committee on Banking Supervision has issued updates to its guidelines for capital and banking regulations, which will undergo phased implementation between 2015 and 2018 (with an observation and control period starting in 2012). They add another round to the substantive changes to bank regulation seen recently and are intended to improve the banking sector's ability to absorb financial and economic shocks, thereby minimising the risk of these spilling over into and damaging the "real" economy. A major element in the regulations is the focus on containing the systemic risk exposure created by systemically important financial institutions (SIFI). These are institutions – such as the major global banks – that through their size, pervasiveness or both could potentially cause major market disruption if they failed.

Basel III introduces some new capital, leverage and liquidity standards to strengthen regulation, supervision and risk management of the banking sector. The capital standards and new capital buffers will require banks to hold more capital – and of a higher quality – than under current Basel II rules. The new leverage and liquidity ratios introduce a non risk-based measure to supplement the risk-based minimum capital requirements and other additional measures to ensure that adequate funding is maintained in case of a crisis.

While the measures are a logical response to the events of 2008-2009, the critical point to emphasise is that by their very nature they will have major repercussions for corporations' liquidity management and working capital financing activities.

Local Regulation

At present, most local regulatory activity that directly affects corporates falls into two very distinct categories. Regulations relating to international trade activities and foreign direct investment (particularly inwards but also outwards in certain markets such as China) are generally being relaxed. By contrast, regulations on other forms of capital mobility and foreign exchange (FX) conversion remain tight in many countries in Asia Pacific. This second category of regulatory attitude is similar to Basel III's intended suppression of systemic risk in that it aims to protect local markets from external shocks or market forces (including speculation) that might be the result of too rapid a move to complete deregulation.

However, the attitude of local regulators regarding banking regulation also has important indirect implications for corporations. For instance, some regulators are becoming increasingly demanding about the localisation of balance sheets and are applying pressure to banks to ring-fence onshore balance sheets. This potentially creates challenges for some international and foreign banks that do not have a material local presence and a developed or diversified domestic balance sheet. Therefore, by necessity these banks have to rely upon and exploit their international network for the funding of their local operations. They may consequently be affected as regards the liquidity pricing – for both deposits and overdrafts – that they can offer corporate clients, thus influencing the conventional domestic pricing dynamics.

Implications for International Cash Management

Many of the changes outlined above might superficially appear to be issues purely for the banking industry. In practice, nothing could be further from the truth. They will all have important ramifications for corporations across many aspects of their liquidity management, including provider selection, choice of liquidity structure and the need to achieve even greater liquidity efficiencies.

While major international cash management banks have the technical ability to offer services that are increasingly sophisticated and genuinely global, various aspects of regulatory change will have a major influence on which of their liquidity services are actually commercially viable:

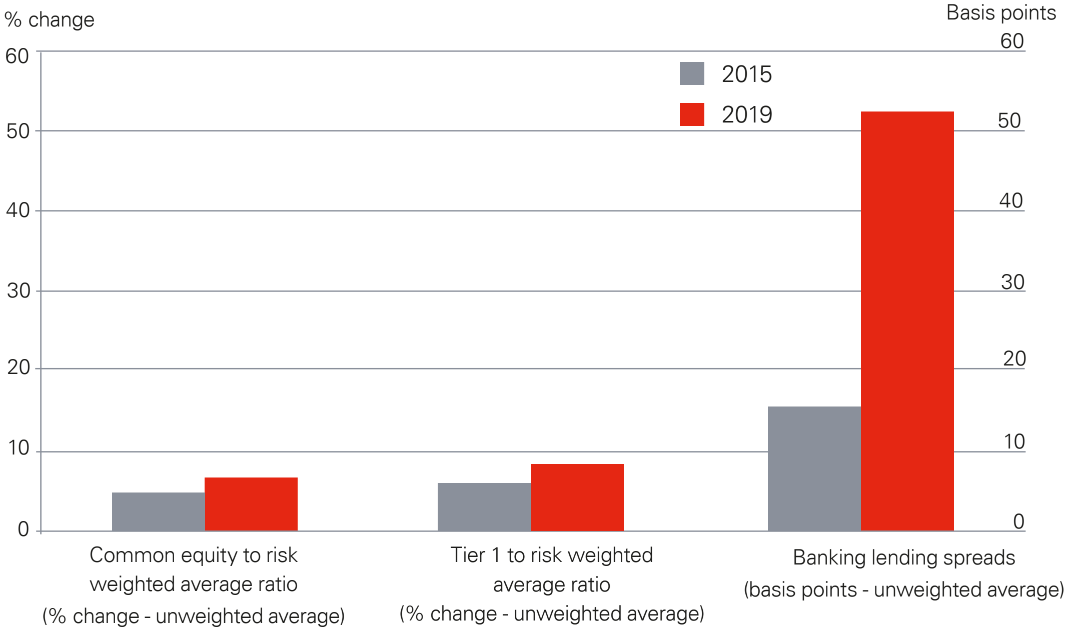
Higher Cost of Credit

Post Basel III implementation, the cost of extending credit is going to increase. An OECD study released in early 2011[1] estimated the negative medium-term impact of Basel III implementation on bank lending spreads and by implication also on gross domestic product (GDP) growth. This is illustrated in Figure 1,

1 *P. Slovik and B. Cournède (2011), "Macroeconomic Impact of Basel III", OECD Economics Department Working Papers, No. 844, OECD Publishing. http://dx.doi.org/10.1787/5kghwnhkkjs8-en.*

which shows the effect of the percentage increase in the ratio of bank capital to risk-weighted assets (RWA) on bank lending spreads. The OECD study projected the impact across three main OECD economies (the US, the euro area and Japan) taking into account how much on average the new capital requirements have already been met by the increase in capital ratios over the past few years and the remaining gaps to be addressed. It is also expected that increases in lending spreads will be larger than the projected average in economic areas such as the US and the euro area because banks in these economies tend to require a higher return on equity, on what is a larger proportion of RWAs on their balance sheets in comparison with other economies.

Figure 1: Estimated Medium-term Impact of Increasing Basel III Capital Requirements on Bank Lending Spreads (US, Euro Area and Japan)



Source: OECD

The study estimated that in order to meet the Basel III capital requirements that will apply in 2015, banks will have to increase their lending spreads by an average of approximately 15 basis points. Furthermore, the additional conservation buffer that will be required in 2019 could force bank lending spreads up by an average of 50 basis points in the three areas considered, with similar effects on the rest of the world.

This change will inevitably also increase the opportunity cost of corporates' internal versus external liquidity sources, so the need to maximise availability and utilisation of internal liquidity will become even more pressing.

Core/Stable Deposit Base Treatment

Basel III will also apply more stringent liquidity standards for internationally active banks, particularly with regard to the funding of their balance sheets and commercial deficits. The tighter risk framework, with its additional requirements for stress testing scenarios, forward-looking provisions, stricter definitions, minimum liquidity coverage and structural liquidity ratios, will result in a different approach to determining the core and non-core portions of the deposit base.

Those banks that have not already adopted higher standards will find themselves facing substantially different capital categorisation and associated stress scenarios. These, in conjunction with increased emphasis on balance sheet funding by currency, tenor and location (plus the required mix of core/stable deposits held) will affect the pricing characteristics of the deposit and lending products they can offer, including liquidity management services.

An important additional consideration is that a bank's strength of balance sheet has to be considered not just at a consolidated enterprise-wide level, but also on a per location basis. A potential implication of this is that the type and depth of business a bank has in a particular market becomes very important. If, for example, a bank only has limited wholesale or retail banking activities in a location then this might be disadvantageous if its balance sheet is consequently of insufficient size and quality. This may in turn constrain the terms of the services it will be able to offer under the new standards.

Regulatory Alignment with International Standards

Currently there are a number of situations in Asia where international and local regulatory standards are not fully aligned, which can necessitate adjustments to liquidity management structures in order to ensure compliance. Typically this situation tends to arise in smaller emerging and developing markets, where financial and banking systems are evolving and becoming more open to foreign flows. In these situations, domestic balance sheet treatment and the regulations associated with liquidity management techniques often deviate from their equivalents in more developed markets. A typical example is a bank's balance sheet treatment pertaining to notional pooling when it comes to net or gross reporting of exposures for capital adequacy purposes.

Specific Changes to Structures and Techniques

In addition to general considerations for corporates that will arise from the consequences of Basel III and local regulation on banks, there are some more specific points to be aware of relating to liquidity structures and techniques:

Single Versus Multi-location Structures

As already mentioned, the value of internal liquidity will increase as a result of higher credit costs. This will reinforce the value proposition of liquidity techniques that offer interest optimisation and enhancement at a centralised level, be that global, regional or sub-regional. However, in order to maximise the benefits, the most efficient structures are likely to remain those domiciled in a single location where the regulations are clear, flexible and in full alignment with international standards (for example Singapore, Hong Kong, or London – which will remain amongst the most popular). Using these locations will make it easier to achieve the most efficient bank balance sheet treatment and for the structure to generate the optimal benefit.

This may run counter to some corporates' desire for a cross-border multi-currency pool with balances held in multiple locations, but with the same benefits as if they were held in one location. However, this is simply not feasible from a regulatory perspective today and this is highly unlikely to change in the near future. Therefore the efficient location of bank accounts involved in an international liquidity structure will become increasingly important, with the most logical choice being in liquidity corridors where liquidity movement is unconstrained.

Single Versus Multi-entity Structures

From a regulatory and tax perspective, single entity structures are generally treated more consistently across jurisdictions in terms of set-off rights, balance sheet treatment and taxation. Nevertheless, multi-entity structures (particularly multi-currency ones) remain in strong demand. These need to be established in the appropriate location, under the correct regulatory framework and with efficient credit support that minimises the size and number of credit facilities.

The regulatory criteria that a bank must comply with when offering multi-entity structures occasionally change over time and it is essential that the bank prepares for, rather than just responds to, these changes. Without a forward-looking approach, all other things being equal, the cost to the corporate client of maintaining the structure will increase without the opportunity to adjust and possibly mitigate some of the impact.

Network Versus Liquidity Overlay Bank

The new regulatory standards are likely to favour the value proposition of a network bank's ability to offer a fully integrated solution. On the one hand, the credit relationship aspect will become more important in view of the rising cost of credit. On the other, the depth of the relationship will also have a material impact on the treatment of deposits under the new standards, thereby influencing access to and pricing of liquidity management solutions for corporates. Unless the breadth of services offered under cash management is material, it will be more difficult to continue to operate pure overlay structures without significant changes to the overall arrangement.

Challenges and Competing Objectives

In view of the forthcoming regulatory changes, corporations will face a range of challenges and potentially conflicting objectives in their attempts to optimise liquidity:

Cash Accumulation and Fee for Credit

A demanding balancing act for corporations in the new regulatory environment will be striking the right balance between optimal accumulation of liquidity to maximise returns and complying with boardroom emphasis on diversifying counterparty exposure. The new complication is that as the cost of credit provision for banks increases, providers of credit will be looking for additional fee business. This will be needed to compensate for reduced interest income due to the increase in their mandatory capital provisioning against any credit extended. Essentially the old "fee for credit" conundrum arises again, but in a more concentrated form.

Another element in the decision is that as the value of internal liquidity continues to rise, the breakeven point for the next liquidity management project shifts accordingly. This in turn should ideally lead to greater consolidation of liquidity, but also further accentuates the importance of selecting the right bank partner in view of the increased counterparty risks. The most likely outcome is a reduction in the number of key relationships and a change in the selection criteria.

Efficient Structure Versus Maintenance Costs

Another balancing act for corporate treasuries is finding the point of equilibrium between the need for an efficient liquidity structure and the associated maintenance costs. An obstacle to this is the need on both sides for a better understanding of service differentiation and respective business value propositions. Common points of confusion today include assumptions made about how banks operate their services and how they compare on cost and quality of service delivery.

Simple price comparisons between individual bank products can be misleading and should not be used to construct a "best price" service offering by cherry picking the lowest cost offering across multiple banks, unless such a comparison is performed at an overall aggregate service proposition level. Banks' service costing and associated pricing differ for a number of reasons, and their proposition evaluation needs to take into account the full array of services they have included in their pricing against the expected level of business considered. In other words, the comparison should be performed by considering and contrasting the full service proposition and benefits against the proposed pricing, without breaking it down into arbitrary components that will introduce additional distortion into the analysis. Liquidity services cannot and should not be evaluated in isolation since they will reflect the nature of transactional banking services that support them.

Structural Adjustment

The liquidity management techniques commonly used today – physical cash concentration, notional pooling, and interest enhancement – will not be materially affected by the new regulatory standards or local regulation. However, these regulatory changes will impose tighter criteria for their establishment, particularly as regards location, credit requirements and pricing conditions. Account structures, including location of operating accounts and cross-border linkages among them, will need to be designed in a very efficient manner in order to facilitate the operation of liquidity management techniques.

Regulatory changes are also likely to increase the maintenance costs of liquidity structures and/or reduce the potential returns. This, in conjunction with the increasing value of internal liquidity, means that corporations will have the strongest possible motivation to make their liquidity structures work harder by maximising liquidity throughput.

Banks: Those Who Can and Those Who Can't

At the same time, a clearer delineation will emerge between two categories of bank. In one category will be the international cash management banks that already have a sophisticated, comprehensive and prudent methodology to manage their balance sheets under an effective risk policy framework that is already broadly in line with the new regulatory standards. In the other will be those that are attempting to belatedly play catch-up.

From a corporate perspective, there will be various practical consequences of this delineation. Banks in the first category will already be able to offer the most credit-efficient structures that also comply with regulation. They will additionally be able to offer optimised international connectivity, which will become an increasingly important competitive differentiator, as it will require high quality balance sheets to sustain the rising regulatory costs of being an active international bank. Unlike the second category, international cash management banks that have prepared in advance for regulatory changes have also been investing in methodologies that will allow corporates greater transparency over what is practically achievable in terms of liquidity management. For example, they should be able to provide sophisticated benefit modelling techniques so corporates will be able to take decisions about liquidity management strategy on a more informed basis than was previously possible.

Conclusion

The new regulatory environment is most definitely not just a matter for banks; there will be important consequences for corporate liquidity that will need to be addressed by treasuries. The changes will make certain liquidity services, such as multicurrency liquidity management, increasingly essential. However, delivering this type of service in isolation will be insufficient. More extensive and consultative terms of engagement between corporations and banks will be the key to facilitating the evaluation and recalibration of the liquidity management arrangements in an evolving environment.

Finally, the credit implications of the regulatory changes will also drive the need for the efficiencies inherent in an integrated service offered by a network bank with extensive footprint and appropriate credit support. By the same token, the potential risk and growing inefficiency implicit in a pure overlay liquidity structure will become ever more apparent.

Liquidity Management: Leveraging Technology to Improve Cash Forecasting

- Managing liquidity requires having accurate information regarding current cash positions and making accurate forecasts of impending inflows and outflows.
- Companies that excel in managing cash, payables and receivables have greater control over the elements of liquidity.
- Some companies are leading the way towards all-electronic processing, alongside the implementation of workflow, analytics and dashboard solutions to boost visibility.
- Effective management of these processes is fundamental to successfully managing enterprise liquidity, driving down costs and improving visibility and forecasting.

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Enterprise liquidity management is a perfect example of a process that is simple in concept, yet complex in application. The true challenge is in gaining an accurate forecast of future cash positions, which requires visibility into impending inflows and outflows that are mired in paperwork, creating silos of information. This article offers insight into how cash management, supply chain finance (SCF), accounts payable (A/P) and accounts receivable (A/R) processes can improve visibility into and control over a central element of liquidity management: cash flows from operations.

The Starting Point: Cash Management

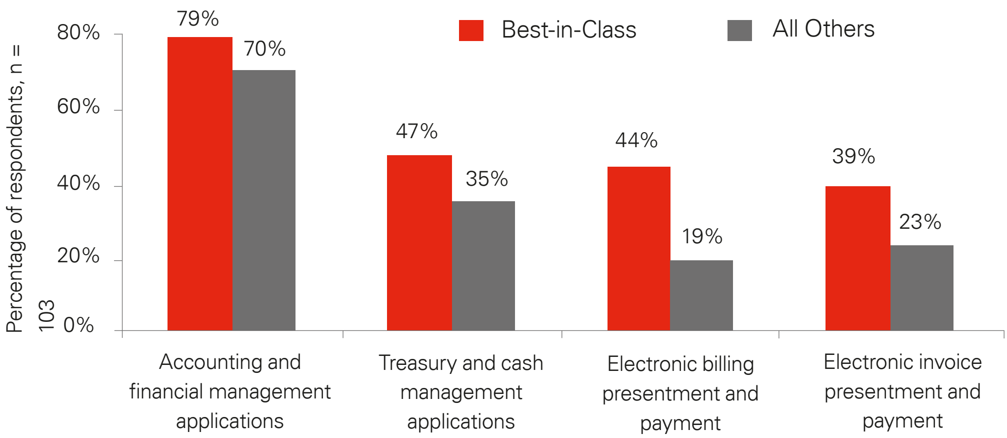
Aberdeen Group's November 2010 study, "Operational Cash Management: Streamlining Processes to Unlock Liquidity", brought to the forefront the role and impact of automation on cash reporting and forecasting. It is not necessarily the difficulty in gaining visibility of *current* positions, but rather of *future* states that are dependent on accurate appraisals of expected sources and uses of cash. The dominant pressure of a no-growth economic environment (cited by 51% of all respondents) also put cash flows from operations front-and-centre for responding financial professionals.

Leading companies were 47% more likely than their competitors to automate reporting of cash held and forecasted. This provided them with access to more accurate and timely information, enabling them to gauge their cash position and assess liquidity requirements on a regular basis. In fact, these top-performers were also found to be 25% more likely to be able to provide a clear assessment of liquidity over their peers. This theme of cash reporting and visibility (which depends on the efficient management of accurate data) was a common element in the discussions of A/P, A/R and SCF as well.

When looking to efficiently manage information, accessibility can be as important as the underlying accuracy of the data. With multiple bank relationships to manage, the processes used to interact with these partners can affect an organisation's ability to obtain a comprehensive view of current positions across the board. Top-performing companies were found to be 33% more likely to have standardised banking processes, enabling them to handle interactions with different banking partners on an identical basis.

Most organisations begin with a base of an enterprise resource planning (ERP) system, or a financial management solution to assess their liquidity position. The difference between top performers and all others lies in the level of adoption of supplemental technology solutions such as electronic billing presentment and payment (EBPP) to manage receivables from consumer transactions and electronic invoice presentment and payment (EIPP), which can apply to both A/R and A/P.

Figure 1: Leveraging of Enterprise-wide Applications



Source: Aberdeen Group, November 2010

The Big Picture: Putting Liquidity in Context

The operational cash flows that underlie liquidity forecasts are not passive elements. Companies are actively looking to manage these pieces by speeding up collections and reducing days sales outstanding (DSO), streamlining their inventory management practices and reducing days inventory outstanding (DIO), and *optimising* their payables to balance timing of outflows with the potential benefits of discounts. Companies favour optimisation (rather than maximisation) of their days payable outstanding (DPO), as

Figure 2: Financial Performance Comparision

	DSO +	DSO –	DPO =	CCC
Current	46.19	40.51	44.72	41.98
Target	33.63	26.73	42.01	18.35
Difference	-37%	-52%	-6%	-56%

Source: Aberdeen Group, January 2011

higher DPO does not necessarily correlate to better performance in other metrics such as DSO, accuracy of forecast, higher levels of discounts taken or lower fees. These changes, taken together, can drastically reduce targets for the cash conversion cycle (CCC).

Optimising DPO: Strategic Accounts Payable

The strategic value of A/P is centred on the ability to process invoices efficiently, providing companies with flexibility in scheduling external disbursements. While cost cutting is one of the top pressures driving A/P improvement efforts, the benefits of streamlined operations go far beyond labour costs. Those cost differences (which are 85% lower per invoice for the leading companies than for others) are driven by process efficiencies – most notably the 71% receipt-to-approval cycle advantage top performers boast over other respondents (3.8 days versus 13.3). In the liquidity discussion, this efficiency is paramount because it allows invoices to be processed within traditional discount windows, and affords the company flexibility to choose whether to pay early or hold onto their cash.

Another key pressure driving A/P improvement that is equally important to the liquidity discussion was the lack of visibility into invoice documents and approval status. Visibility is critical for gauging the health of a business and assessing liquidity needs of various units, so that executives can define objectives and/or ensure course correction in a timely manner. In addition to the technologies mentioned, which create and manage critical A/P data, leading companies were also 75% more likely than laggards to have dashboards in place summarising current A/P status and performance. Therefore, leading companies not only collect A/P-related data as part of their electronic processing, but also provide tools to expose this data to interested stakeholders.

Minimising DSO: Effective Accounts Receivable

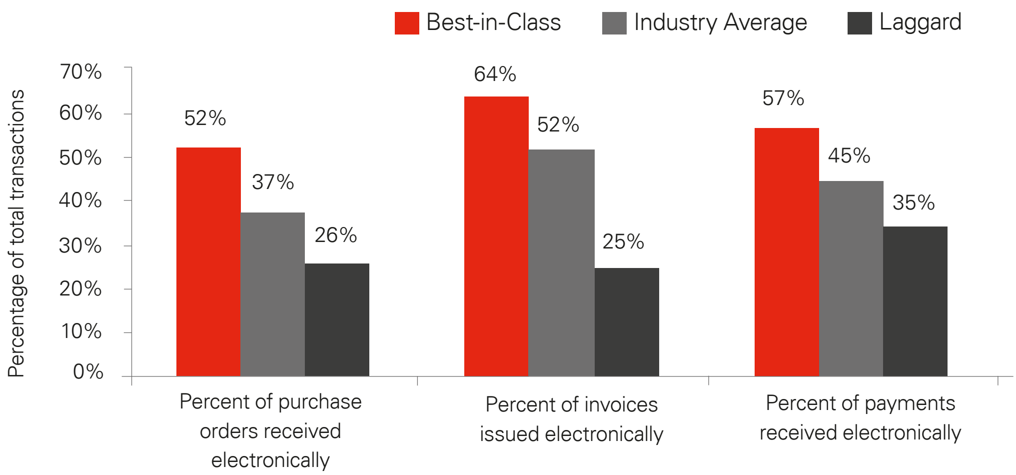
The aim of A/R is straightforward: accelerate the receipt of payment for goods sold and services rendered (thereby reducing DSO) and improve cash flow forecasting. The top strategies for improving A/R operations were the same: streamline processes to reduce complexity, increase the use of e-invoicing to aid customers' ability to process payments, and automate A/R to better manage and gain visibility into cash inflows.

Leading companies were 60% more likely to ensure collaboration between finance, credit and sales to optimise sales transactions based on collectability. This approach reduces the risk profile of the A/R portfolio by avoiding sales that are unlikely to be paid within required timelines. Risk assessments do not stop after credit is granted; leading companies were also far more likely to regularly score their entire A/R portfolio, using statistical and judgmental techniques to identify potential repayment problems on an on-going basis.

As with A/P, the ability to keep apprised of ongoing changes is intimately tied to accurate and timely reporting. There are two key components in this equation: electronic data, and the technologies that manage it. As illustrated in Figure 3, Best-in-Class companies (defined as the top 20% of all surveyed by

Aberdeen) are leading the way towards all-electronic processing – though there is still quite a bit of room for improvement. These volumes are complemented by the implementation of workflow, analytics and dashboard solutions to boost visibility.

Figure 3: Usage of Electronic Transactions by Maturity Class



Source: Aberdeen Group, June 2011

Key Takeaways

Managing liquidity requires accurate information regarding current cash positions and accurate forecasts of impending inflows and outflows. Cash flow from operations plays a large part in this arena, and companies that have excelled in cash, A/P and A/R management not only have greater visibility into the elements of liquidity, but also have greater control over them. There are many options to weigh when looking to improve liquidity management. A few key recommendations are to:

- standardise liquidity-related processes and policies across the finance function;
- automate processes to reduce review and approval cycles;
- continue growing electronic volumes of purchase orders, invoices and payments; and
- derive insight from existing data by employing solutions to actively monitor balances and cash flows from operations.

Cash flows from operations are not the only piece of the puzzle, but effective management of these processes is fundamental to successful management of enterprise liquidity, driving down costs, improving visibility and forecasting, and offering opportunities for additional enterprise benefits through discount capture.

Please note that while Aberdeen Group targets a global audience, the majority of respondents who took part in this study were based in North America.

New Roles and Tools for Optimising Treasury Operations

Jason Torgler, Vice President of Strategy, and **Blaik Wilson**, Solutions Consultant, APAC, Reval

- Since the global financial crisis, treasurers worldwide have taken on new responsibilities as they work towards optimising their treasury organisations.
- Amid an onslaught of new regulations rolling out globally, companies are adopting a new risk mindset and the treasury function is playing a vital role.
- Treasurers are demanding better visibility into cash and risk to better manage exposures and fulfil their expanding duties.
- A single, integrated, software as a service (SaaS) based treasury management system could hold the key to operating more efficiently in an interconnected world.

Since the collapse of US-based Lehman Brothers sparked a global financial crisis in 2008, chief financial officers (CFOs) and treasurers worldwide have been working diligently to assess how well their organisations responded, where their shortcomings were, and how they can fundamentally improve the way they operate in this interconnected world.

In 2011, Reval conducted a series of international interviews with financial executives at a number of public and private companies, and with other industry observers, such as consultants and journalists. Reval's goal was to collect and disseminate the views of CFOs and treasury executives on the future of treasury management in a post-crisis world. What were their responses to the global financial crisis? What changes are they now considering to improve operations in this new financial environment?

In short, the crisis exposed inadequacies experienced by many treasury organisations, leaving executives to close gaps discovered in cash management and risk management. Today, these executives are seeking integrated treasury technology solutions and deep domain expertise in an effort to optimise their treasury operations in a way that will enable them to meet the requirements of a world forever changed.

A look at how some treasury organisations are accomplishing key goals can help inform others who may be in different stages of progress.

Goals for the Way Forward

Many CFOs and treasurers are busy applying the lessons learned from the crisis, dealing with the deluge of new regulations enacted in its wake. They are striving to make changes to critical, day-to-day treasury functions, such as cash and liquidity management, funding, and counterparty credit risk management, which became problematic as credit markets seized up. But some financial executives are making more progress than others in accomplishing some important goals. These include:

- Identifying low-visibility but potentially high-impact risks. This requires businesses to move on from the numerous existing processes they currently use, the inaccurate forecasts they can produce and the labour intensive reporting techniques that are required. Instead, CFOs and treasurers are looking for integrated tools that can help them identify and mitigate financial risk, make strategic decisions and meet evolving regulatory requirements.
- Monitoring, accessing and managing financial assets. Financial executives need to be able to confidently manage and forecast their derivatives, cash and other positions, globally.
- Understanding and forecasting the risks – both individual and aggregate – inherent in the company's business. This requires effective ways to handle enterprise treasury and risk management.

New Attitude Toward Risk

One of the key focus areas among the CFOs and treasurers Reval spoke with is risk. Now more than ever, CFOs and their treasurers worry about many different types of risk, leading to the adoption of a new risk mindset with treasury playing a vital role. Today the treasury group must not only deal with such issues as liquidity and funding risk, it must also have an understanding of risks that are not readily apparent and that have a potential for contagion. Executives to whom Reval spoke explained that they must comprehend a company's risk appetite from the top down and evaluate many different risks for their potential impact on a company's cash positions. They must also have a complete understanding of their hedging strategies and the impacts of each region's over-the-counter (OTC) derivative reform and accounting changes.

> **"... the treasury group is one of the few areas of a large company that can see many of an organisation's risks."**

These executives have a heightened awareness that the treasury group is one of the few areas of a large company that can see many of an organisation's risks. In this respect, they can have a hand in identifying and managing risks from a holistic point of view, both in daily planning and long-term decision making, and also in assessing interconnected risks.

Expanding Roles of the CFO and Treasurer

This new risk mindset is forcing CFOs and treasurers to grow in their jobs and to perform new tasks on a regular basis. Today, treasurers are being asked to take on added or brand-new requirements, particularly when it comes to tasks around managing cash and managing regulatory compliance. Issues that previously were relevant to only a small number of treasurers are now the "new normal" for most treasurers.

For example, cash held in global subsidiaries is becoming an increasingly important issue. In the past, many treasurers just accepted that this cash was trapped in various locales and attached little strategic importance to these assets. Today, most treasurers must know how much cash exists and where, the institutions in which it is held and how they can repatriate it if needed.

> **Today, most treasurers must know how much cash exists and where, the institutions in which it is held and how they can repatriate it if needed.**

Treasurers are also dealing with the increased importance of funding diversification and relationship management, as they need to secure lines of credit well in advance and need to examine their counterparty risk exposure. They now have more focus on contingent and diversified funding sources, especially those that serve them in the short term.

When it comes to compliance, treasurers are challenged with an increasing array of new regulations. For example, the Reserve Bank of India released guidelines in February 2011 limiting the scope of allowable hedging instruments to be traded and requiring specific disclosures in the risk management policy. The ultimate responsibility for gathering and reporting the data to comply with this new regulation lies with the treasurer. This is, of course, just one example among many of how compliance with regulations following the global financial crisis is one of the main drivers expanding the roles of treasurers and CFOs.

CFO–Treasurer Dynamic

Reval also set out to explore the dynamic between CFOs and treasurers to ascertain how the effects of the global financial crisis have changed CFOs' expectations. Interestingly, Reval found that CFOs' concerns run the gamut. Some need their treasurers to continue to focus on core competencies, while others are asking for their treasurers to be even more strategic in the new tasks they are taking on. For some treasurers, these new tasks include developing a keen understanding of the organisation's current and projected liquidity position; understanding and securing access to short- and long-term funding; establishing a more active risk management discipline during periods of volatility; managing tax implications across cash movement and intercompany lending; partnering with the business side to work across departments and across business units on the creation and execution of financial plans; managing compliance; and managing staff resources and technology.

Some CFOs noted that the financial crisis exposed a lack of controls in some organisations. Because good controls help lay the foundation for good corporate governance, treasurers must maintain and monitor processes, risks and controls first – before branching out into expanded roles.

On the other hand, some CFOs need their treasurers to be more strategic, over and above the day-to-day activities they perform. Reval found this sentiment to be readily apparent within Asia, where some economies are growing more rapidly. Treasurers are being asked to consider the business impacts of globalisation, including factors such as foreign exchange rates and interest rates. Likewise, as multinational companies expand globally and become more decentralised, treasurers are asked to gather disparate sets of information and synthesise them to paint a bigger picture of capital investments.

Gaining Better Visibility

Now that they are aware of the need to consider more risks than they did in the past, the financial executives Reval spoke with stressed that the key to understanding and hedging these risks is gaining better visibility. They want a means to better visualise the entire treasury function in a comprehensive manner. A holistic view of their positions and risks will give them the ability to create more accurate forecasts and will lead to smoother operations and greater efficiencies. Ultimately, such visibility will give their organisations the information needed to make the right strategic decisions.

Many financial executives bemoan the fact that they lack complete visibility of all cash flows on a global basis. They also point to the lack of a central repository to view business risks across asset classes. In fact, financial executives said that too many treasury groups continue to rely on error-prone spreadsheets and are missing out on the advantages of straight-through processing.

Despite the continued prevalence of spreadsheets, advanced software has certainly been an important enabler for treasurers over the past decade. But financial executives are looking for the next generation of solutions. They need software to be much more interconnected than it has been, leading to a demand for horizontal, integrated treasury management software. Treasurers in particular want an enterprise-wide treasury management solution (TMS) that brings together various treasury workstation and risk management applications to give them a full view of their entire organisation in order to meet all the demands placed on them – a system that can handle cash management, hedge accounting and risk management.

“**... too many treasury groups continue to rely on error-prone spreadsheets and are missing out on the advantages of straight-through processing.**”

Is Software as a Service the Answer?

Reval's research shows that today's financial executives have a better understanding of web-based software than they did just a few years ago. Almost every TMS vendor has launched or will launch some sort of offering based on software as a service (SaaS) delivery.

Most of the individuals interviewed see the benefits of adopting an SaaS-based solution. In fact, some said that their IT staff prefer solutions that are maintained off premises as they see the promised benefits of cost savings and outsourcing support, and they can always use the latest iteration of the software.

By streamlining workflow and outsourcing support with SaaS-based TMS, treasurers can realise efficiency gains of integrated TMS, such as time savings. For example, treasurers will have more opportunity to be analytical and strategic. Previously, 80% of treasury time could be spent on processing, with the remaining 20% available for analysis and strategy. SaaS-based TMS can reverse this, to enable 80% of time to be devoted to analysis and strategy of issues such as liquidity positions, funding, risk management and compliance. In addition, by creating efficiencies, these systems enable treasurers to spend more time managing their staff and working with third-party experts to plan and execute over the long term.

Measuring Potential Benefits

CFOs and treasurers are certainly justified in asking TMS providers to show a clear path to return on their technology investments. While exact figures will, of course, vary for each successful implementation, many of the potential benefits of a SaaS-based TMS can be spelled out, based on real-world deployments:

- productivity gains as individual employees become more efficient and experience higher job satisfaction based on value-added work shift;
- increased rate of return based on better liquidity management such as elimination of trapped cash, investing earlier in the day and investing for longer time horizons;
- decreased cost of borrowing through improved borrowing decisions and pay-down practices;
- reduced internal IT costs from eliminating the need for hardware support, disaster recovery, backup, upgrades and integration;
- reduced internal audit costs, as an SaaS-based TMS delivers better audit and control features and reporting as compared to a manual, Excel-based environment; and
- bank fees reductions, coming from improved bank polling and data distribution practices, improved trading, payment and money movement practices and lower bank platform costs.

Supporting Change is Ongoing

The technical advantages for SaaS delivery are numerous, but for CFOs and treasurers, software architecture takes a backseat to functionality and the operational benefits that a truly integrated solution for enterprise-wide treasury and risk management can offer. Our research suggests that financial executives and thought leaders who influence buying decisions will gravitate toward those players in the marketplace who understand the regulatory landscape as it continues to take shape.

Compliance with these regulations and understanding their impacts, while all the time monitoring for developments that can threaten a business, is particularly challenging using a patchwork of technology solutions. But as many CFOs and treasurers have indicated, a single technology solution that provides total visibility throughout an organisation is both a preference and a necessity in their new world.
With the financial crisis still fresh in the minds of so many, it is reasonable to expect that the industry will continue to move toward such integrated technology solutions to support an optimised treasury organisation.

Concentrating and Integrating Chinese Liquidity

- Anti-inflationary measures in China have had a negative impact on the cost and availability of external sources of liquidity.
- The time is ripe for corporate treasuries to implement in-country liquidity management structures that maximise the use of internal liquidity sources.
- The corollary to this is the integration of liquidity arising from this into existing or new pan-Asian liquidity structures.
- While regulatory restrictions make some common liquidity management techniques unfeasible, there are alternative methods – such as entrusted loans – to deliver flexible and effective solutions.

Lewis L Sun, Head of Sales, Global Payments and Cash Management, HSBC, China

The interest setting regime operated by the People's Bank of China (PBOC) consists of mandatory limits for both deposits and borrowing. At present, these limits are widely spaced and the cost of bank borrowing is high. This provides a strong incentive to maximise the use of internal corporate liquidity, but there are certain regulatory restrictions that make some liquidity techniques commonly used in mature Western markets unfeasible. For example, direct intercompany loans are not permitted, so alternative methods have to be used, one of the most popular being the entrusted loan. Depending upon the banking provider used, these can be adapted in a variety of ways to deliver a flexible and effective liquidity management solution.

Liquidity Management in China

Entrusted Loans – Basics

An entrusted loan is indirectly made by a cash rich corporate entity to a cash poor one. The key point is that a bank must be involved as an entrustment agent that takes the deposit from the cash rich corporate entity and lends it on to the cash poor counterparty. Under this arrangement, the agent bank is assuming no credit risk, so this process is most commonly used for intra-corporate transactions. Both the corporation and the bank must book the transaction as an entrusted loan; in the bank's case it must be periodically recorded on a consolidated basis to the central bank as an off-balance sheet item.

The interest rate charged upon a renminbi (RMB) entrusted loan is freely negotiable under current Chinese regulations. However, it is advisable to establish the loan on an arm's-length basis to avoid any possibility of a challenge from the tax bureau.

The main benefit of an entrusted loan structure is apparent; the corporation can use its own internal liquidity to finance entities in deficit, thereby avoiding incurring the high costs of external bank borrowing.

The cost difference is significant; based upon the current interest rate environment in China, a corporation can probably save around 400 basis points by using an entrusted loan rather than borrowing from a bank. In addition to cost saving, a further benefit is that corporates can use entrusted loans as a risk control measure by consolidating all their cash into an entity of which they have control.

Entrusted Loans – Costs

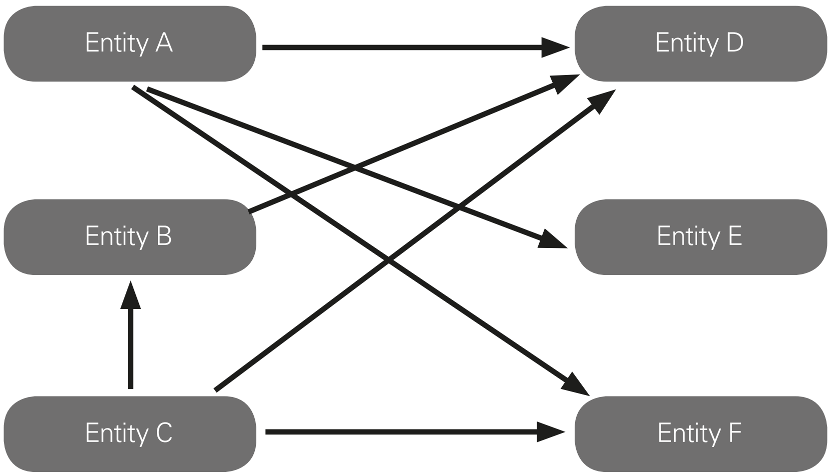
There are a number of costs associated with establishing an entrusted loan:

- Local withholding tax: Levied on the interest income of the loan and charged to the lending entity, the exact rate varies from city to city within China, but is typically around 5%. So if the inter-company interest rate is set at 2%, the tax burden will be around 10 basis points.
- Stamp duty: This is levied on a one-off basis on the principal of the loan at a rate of 0.005%.
- Bank commission: For acting as entrustment agent, the bank charges a commission. The percentage is negotiable depending upon the size and the frequency of the loans, but rates typically range between 0.1% and 0.3% per annum.

Entrusted Loans – Streamlining

While RMB entrusted loans have much to offer, they can quickly become unwieldy to manage once the number of loans within a corporation starts to rise. Figure 1 illustrates how this situation arises because of the need for a tripartite agreement for every individual entrusted loan. This situation can easily occur because it is difficult to find an ideal bilateral match in terms of tenor and amount, so multiple entities are often involved. As it can take anything from a couple of days to perhaps weeks to conclude each tripartite agreement, the workload can quickly become unmanageable.

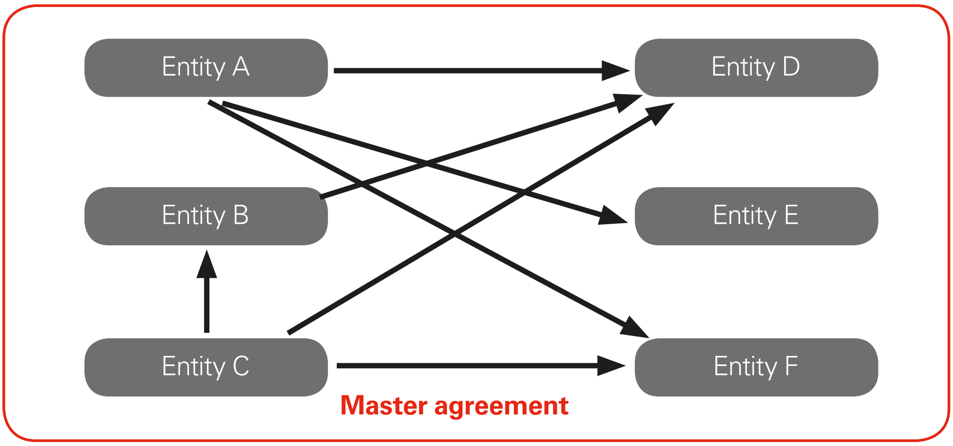
Figure 1: Proliferation of Tripartite Agreements with Multiple Entrusted Loans



Source: HSBC

One way of simplifying the process is to have a group entrusted loan with documentation that consists of a master agreement covering all participants and that has generic terms and conditions. Then each new loan only necessitates issuing a drawdown notice to the bank, which can then transfer the funds immediately (see Figure 2).

Figure 2: Streamlining Entrusted Loan Structures with a Master Agreement



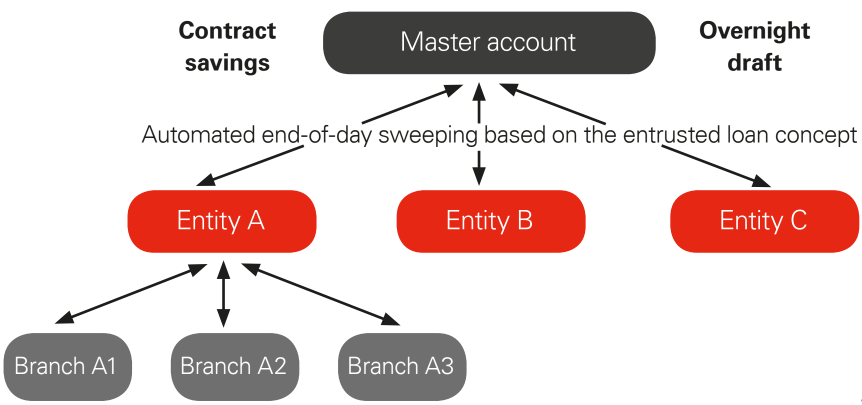
Source: HSBC

This method of managing entrusted loans dramatically reduces the administrative overhead and expedites matters, but does not alter the fact that the process is still essentially bilateral in nature. It is therefore still subject to the problem of precisely matching up lending and borrowing entities' requirements as regards tenor and amount. Furthermore, if the debtor entity is unable to repay on the due date, then external borrowing will be needed to cover the gap. Apart from the question of cost, this can quickly become messy from an audit perspective.

A further refinement of the entrusted loan concept that addresses these issues is a fully automated RMB cash pool (see Figure 3). This minimises the need for external borrowing, while simultaneously improving return on surplus cash and visibility/control.

This concept, which effectively provides an end-of-day zero balance structure, has been available as a product for about six years and is therefore tried and tested in the Chinese market. In addition to the benefits outlined above, different interest rates can be supported within the structure. This can be a valuable tool with which central treasury can influence corporate entities' behaviour. For example, an entity with sound treasury policies and risk control can be permitted to borrow RMB at preferential rates,

Figure 3: Fully Automated RMB Cash Pool



Source: HSBC

while a delinquent entity (such as one that ignores cash flow planning requests) can be penalised with higher rates to deter it from borrowing.

This structure is also available on a without reversal basis, which means that all entities will be running on a zero balance basis by using the intraday overdraft offered by the bank, which is free of charge. The structure is extremely flexible; entities can easily be added or removed and all parties are dealing with just one central counterparty, namely the entity holding the master account. Finally, it is worth noting the branches at the very bottom of the structure in Figure 3; sweeping RMB from branch offices to the main legal entity is completely possible and doesn't cost anything.

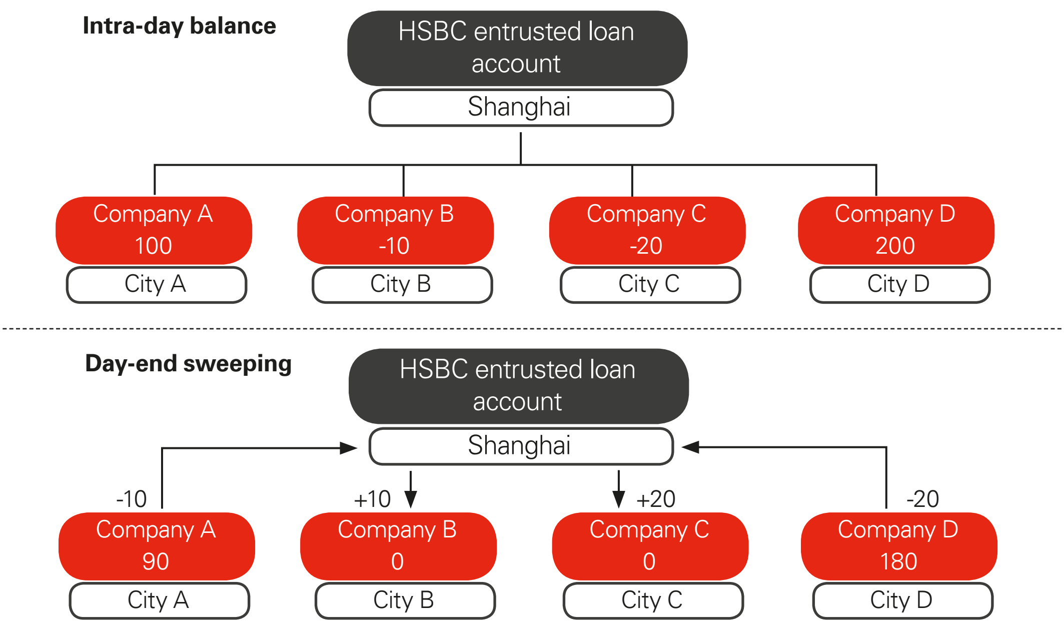
Entrusted Loans – Tax

Despite the advantages of the structure shown in Figure 3, there are some tax implications to consider. One obvious issue is that a loan from a cash rich to a cash poor entity under this model actually consists of two loans – one from the cash rich entity to the header account and one from the header account to the borrowing entity, thereby doubling the tax charge.

Another consideration is that if all entities in the structure are cash rich then the aggregated balance will not benefit from the tiered interest rates usually available in such a structure because of the maximum permissible onshore RMB deposit rates specified by the PBOC.

If the provider bank has the necessary capability, then one way around this issue is for sweeping to happen only on demand (see Figure 4). At the end of each day the bank system will calculate the collective cash deficit of entities requiring funding and only this exact amount will be swept. By minimising any unnecessary sweeping in this way, tax charges are kept to the minimum.

Figure 4: On-demand Sweeping to Optimise Tax Position



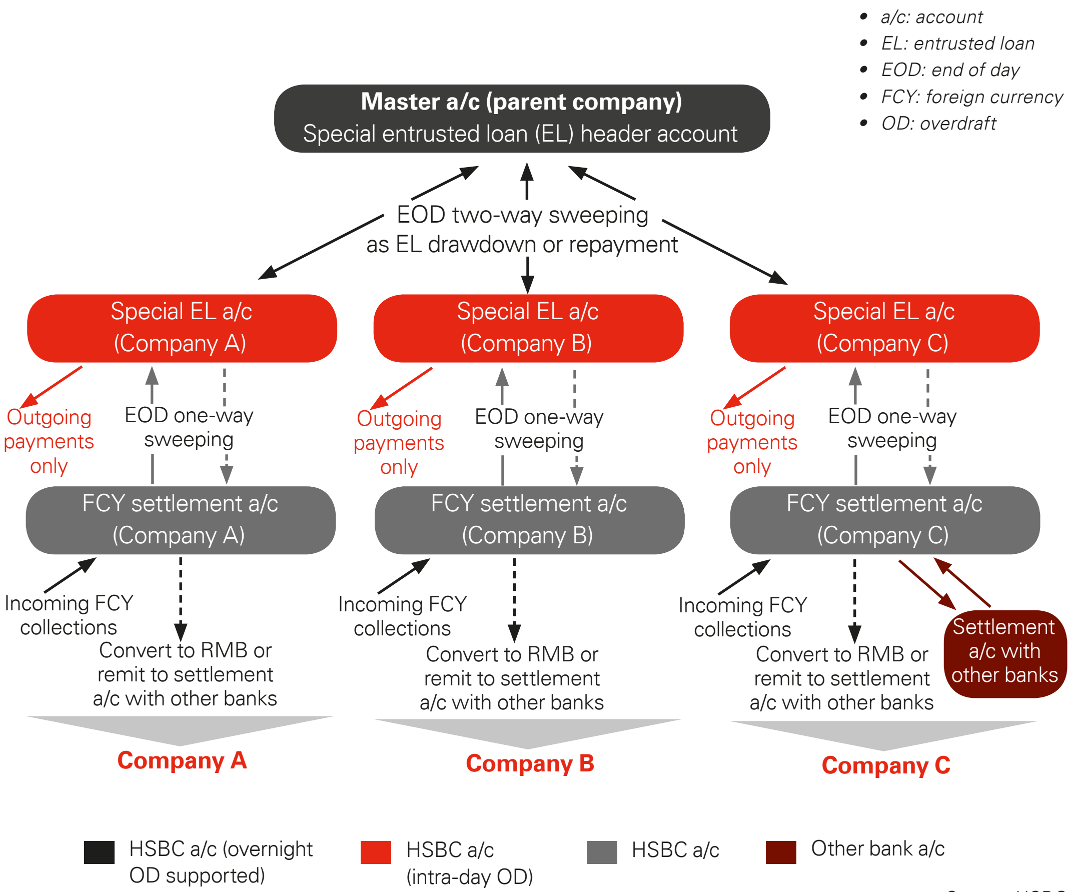
Source: HSBC

Another improvement is for the header account to be an Asian account belonging to the bank, not the corporation. This means that there is only one entrusted loan involved between the two corporate entities via the intermediary account, which avoids the duplication of tax charges. For companies that have substantial RMB cash flow fluctuations across their entities in China, the potential tax savings of this approach can be very substantial.

Foreign Currency Cash Concentration

The situation for cash concentration of foreign currency differs significantly from that for RMB because of China's foreign exchange (FX) controls. These make it extremely complicated to establish (for example) a US dollar pooling structure, but it is nevertheless possible to do this completely automatically. Figure 5 shows how this can be accomplished; as can be seen, the structure is very different from the two-layer structure used for RMB. Every company has to open at least one additional special entrusted loan account (the red boxes in Figure 5) because one of China's key foreign currency control requirements is that money that is different in nature (e.g. current account as opposed to capital account transactions) cannot be mingled. (This is because unlike current account transactions relating to approved trade

Figure 5: Foreign Currency Cash Concentration Structure



Source: HSBC

activity, capital account items that consist of capital borrowed on or offshore from shareholders is not freely convertible and requires case-by-case approval from the regulator before each conversion.)

Although it is more complex, this type of structure is compliant with China's current FX control measures and has been certified as such by China's State Administration of Foreign Exchange (SAFE) for a number of HSBC clients.

Another important difference between RMB and foreign currency pooling is that the spread between borrowing and deposit rates for foreign currencies may not be as wide as they are for RMB, which will obviously affect the possible level of pooling benefit. It is therefore advisable to conduct a thorough cost benefit analysis in advance, which includes an allowance for the time and costs involved in obtaining the necessary case-by-case approval from the regulator. The granting of such approval depends heavily on whether the corporation can prove to the regulator's satisfaction that the structure is intended as a purely working capital management measure and is definitely not for currency speculation.

Integrating China with an Asia Liquidity Structure

Onshore cash concentration in China is now perfectly achievable, but for maximum liquidity benefit, corporations with multiple business entities in Asia will be looking for a more holistic solution. Achieving this is still quite a demanding task because of the fragmented nature of regulation and exchange controls in the region. Countries such as Australia, Hong Kong, Japan, Singapore and New Zealand have freely convertible currency, transparent tax regimes and little in the way of foreign currency controls. Therefore, all the standard liquidity management techniques are typically available in these countries.

Countries such as Indonesia and the Philippines sit in the middle of the regulatory spectrum in that they have FX controls but are not otherwise especially onerous. At the most highly regulated end of the spectrum are countries such as China, India, Korea, Malaysia, Taiwan and Thailand. In addition to FX regulations, international corporations may find that in these countries they are unable to repatriate cash, or to pool cash between subsidiaries. There are also regulations governing onshore and offshore accounts to consider; many countries in this group do not allow resident incorporated entities to hold offshore foreign currency accounts.

This regulatory position makes it laborious to include this last group of countries in cross-border sweeping or notional pooling activities. For example, in China moving funds in or out of the country may only be done for bona fide business reasons, such as trade transactions, so certain documentation must be delivered to the bank before these fund movements can be processed – which obviously makes the process extremely manual.

However, a number of recent developments suggest that this situation may improve in due course. The RMB cross-border trade settlement programme has been appreciably extended in the past year or so. As part of this, there is now an active offshore market for RMB in Hong Kong (where it is referred to as CNH). Furthermore, with SAFE approval, export proceeds can now be kept overseas in an offshore account. This could potentially be a vehicle for onshore companies to join regional liquidity schemes, but there are certain points that need to be clarified before establishing such a structure. For example, it is not yet absolutely certain how SAFE will conduct its monitoring process of these offshore accounts. If, as appears likely, it opts to do this by checking monthly bank statements (as opposed to checking every individual transaction) then it should be possible to incorporate this type of offshore account in a regional sweeping structure.

Other Possibilities

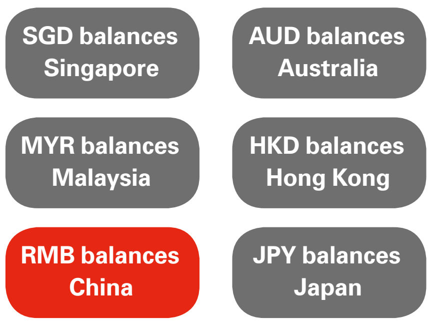
One valuable alternative to attempting to incorporate RMB liquidity into a conventional liquidity structure is to use an interest enhancement facility (see Figure 6), which aggregates account balances for the purposes of determining interest compensation. This process consists of four stages:

- Stage 1: The notional conversion of all credit balances in the scheme into a base currency (e.g. USD).
- Stage 2: The calculation of the total aggregate balance in the base currency.
- Stage 3: The determination of the applicable interest tier for all currency accounts based upon this aggregate balance.
- Stage 4: The calculation and settlement of enhanced account interest at a local level.

An interest enhancement facility is particularly useful for regulated countries where cash cannot be moved out of the country. Furthermore, in countries such as China domestic balances cannot earn deposit interest rates greater than the specified maximum set by the central bank. However, these

Figure 6: Interest Enhancement Facility

Currency	Tier	Credit interest rate
	Singapore interest conditions	
CCY1	Tier 1	HSBC O/N bid rate – 0.5%
	Tier 2	HSBC O/N bid rate – 0.3%
	Tier 3	HSBC O/N bid rate – 0.2%
CCY2	Tier 1	HSBC O/N bid rate – 0.3%
	Tier 2	HSBC O/N bid rate – 0.2%
	Tier 3	HSBC O/N bid rate – 0.1%
	Australia interest conditions	
CCY3	Tier 1	HSBC O/N bid rate – 1.5%
	Tier 2	HSBC O/N bid rate – 1.25%
	Tier 3	HSBC O/N bid rate – 1.00%
CCY2	Tier 1	HSBC O/N bid rate – 0.3%
	Tier 2	HSBC O/N bid rate – 0.2%
	Tier 3	HSBC O/N bid rate – 0.1%



Aggregate pool balance = USD75m, entitles a higher credit interest tier

Lower bound (USD)	Upper bound (USD)	Tier
(9,999,999,999)	50,000,000	Tier 1
50,000,001	100,000,000	Tier 2
100,000,001	9,999,999,999	Tier 3

The rates in this example are purely for illustrative purposes.

Source: HSBC

balances can be included in the interest enhancement scheme where they will contribute to achieving higher interest rates for the free markets by pushing the total aggregate balance into a higher tier.

Another alternative is to move RMB liquidity offshore; once in a free market such as Hong Kong, there are no limitations and physical or notional pooling is possible, so an offshore RMB credit balance can be used to offset debit balances in other countries.

Conclusion

The Chinese government clearly has very serious intentions as regards controlling inflation. The measures it is adopting to achieve this, such as lending control and interest rate policies, have made external sources of liquidity far more difficult to obtain and more expensive than previously. The inevitable conclusion is that maximising the use of existing internal liquidity is now essential. The good news is that onshore cash concentration is now relatively straightforward. Furthermore, there are also a number of ways in which this liquidity can be used to enhance overall corporate liquidity returns. Finally, the opportunity to keep the proceeds of current account transactions in offshore accounts potentially opens up a whole range of established liquidity management techniques for RMB balances.

Given various regulatory constraints and technical requirements, corporates in China will also be playing an active role in assessing their business nature and choosing a partner bank to achieve their business objectives. Flexible structure, clear reporting capabilities and a proven track record are the key elements to focus on when selecting a bank.

Efficient Accounts Payable Process: A Challenge to Overcome

- While there is a strong treasury focus on accounts receivable (A/R) to help meet the goal of effective cash management, a similar focus is needed on accounts payable (A/P).
- Several internal and external challenges must be dealt with to make the process more efficient, which can be addressed by various A/P management strategies.
- The key to a more effective A/P process may lie in building a strategic partnership among corporates, banks and vendors.
- Value-added services from banks to help corporates manage their A/P would streamline the process while maximising value and minimising cost.

Amit Lohani, Lead Consultant, Financial Services and Insurance Practice, and **Balwant C Surti**, Industry Principal, Finacle Group, Infosys Limited

Corporate treasurers consider accounts payable (A/P) and accounts receivable (A/R) core partner departments. The primary task for a treasurer is the effective utilisation of surplus cash – in other words, effective cash management to improve operations. Treasurers focus on various ways to improve cash value by considering various investment mechanisms such as fixed deposits. While there is a strong focus on A/R to help meet this goal, a similar focus is needed on A/P to make the process more efficient and cost effective. As corporates expand their business operations from one vertical industry to another, it is essential that they look at possible ways to streamline their processes and create strategic partnerships with banks and vendors. This article examines how the A/P process can be made more effective by building a strategic partnership among vendors, banks and corporates.

The Need for Streamlining A/P

The corporate A/P department expends considerable effort to accomplish tasks such as receiving, entering, validating and processing invoices. These distinct steps increase maintenance costs while making organisations lose out on the benefits of early payment to vendors. This can be attributed to several factors such as heavy paper invoice management, lack of standardisation across invoices provided by vendors and loose integration of internal systems. While e-invoicing helps significantly in modernising the process, there are areas that can be streamlined to avoid process gaps and minimise late fees and processing costs. As organisations expand their operations and adapt to changing market conditions to remain competitive, the areas of financial controls and compliance require attention.

There are numerous roadblocks hindering the effectiveness of A/P, within the organisation and in its dealings with vendors and banking partners.

Challenges Within the Organisation

- The A/P department receives inputs from various key departments such as infrastructure, payroll and internal tax teams. A lack of system integration might enable these departments to report A/P information at their convenience, an inefficiency that leads to improper cash flow analysis by the treasury department. Non-integrated systems also add to the complexity of the process and the unavailability of cash information from multiple departments negatively affects the A/P department's ability to report expected payment information to treasury in a timely manner.
- If streamlining of internal processes is not a priority for management, this impacts the effectiveness of A/P as well.
- Often, too much time is spent on processes such as matching invoices with purchase orders (POs) to identify payments that don't relate to any PO or user department, causing an approval delay for invoices.
- Sometimes defective goods and short supplies are paid for in advance, or an outage in supply occurs because of unintentional non-payment.

Disconnect Between Corporates and Vendors

- Most organisations pay vendors by advising their banks about payment dates and payment amounts to be made via wire transfers. Not many efforts are made by organisations or banks to analyse the incentives provided by vendors for early payments, charges for late payments or the cost of using cash for other investments.
- Multiple departments of the organisation may be sending data to the same vendor using multiple invoices, resulting in the loss of volume pricing benefits.

Banking Inefficiencies

The lack of offerings provided by partner banks can be a limitation to look into for improving the A/P process. To deal with these challenges, it is crucial that organisations take measures to strategically standardise their processes. From an A/P perspective, the focus areas could be:

- Internal department alignment: Alignment of departments reporting to A/P so that expected payments or the pipeline created by them can be visible to A/P and treasury in real-time.
- Process optimisation and automation: Breaking down business processes into sub-processes for each department with all personnel involved to help identify time-consuming procedures. It could then be considered whether outsourcing is a viable option, such as opting for electronic invoice storage.
- Matrix-driven system: Developing a clear-cut view about the input and output of each department in terms of attributes could help to build suitable monitoring solutions, which might lead to the consideration of alternative payment options.

The Solution: A Strategic Approach

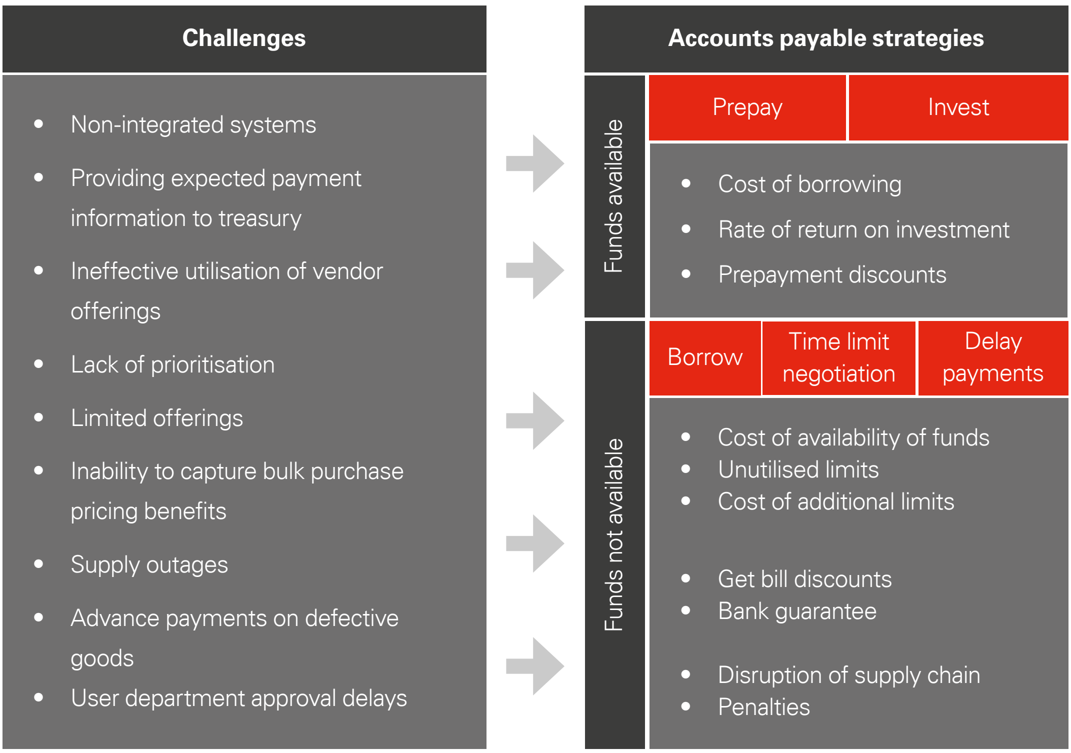
With the growing number of vendor options to choose from, corporates might be interested in various tools to manage their A/P process more smoothly. They could look to third-party vendors or to their partner banks to provide these services on top of existing offerings. To improve the A/P process, corporates might also look for services that facilitate decision-making or offer advice with regard to certain kinds of payments. The need for streamlining A/P functions varies from organisation to organisation. Some of the factors to be considered are:

- Sufficient cash for payments: A corporate may be in a situation where it has excess cash that can be used either to settle payables or to invest in the short term. The returns on short-term investment versus prepayment benefits would be a top consideration in this case.

- Insufficient cash for payments: If the corporate's cash flow is inadequate to settle payables, the alternative is to borrow to cover the shortfall or to delay payment, else incur a penalty, and even the risk of being blacklisted. Much will depend on considering the cost of funds, conducting a penalty analysis, and reviewing the long-term implications of delaying payments on the supply chain.

- Looking at receivables: Sometimes vendors' limited offerings can prevent corporates from benefiting from the most effective solutions. An alternative may be to increase early payment discounts for current A/R to encourage additional cash flow and bridge the gap.

Figure 1: Accounts Payable Management Strategies



Source: Infosys Limited

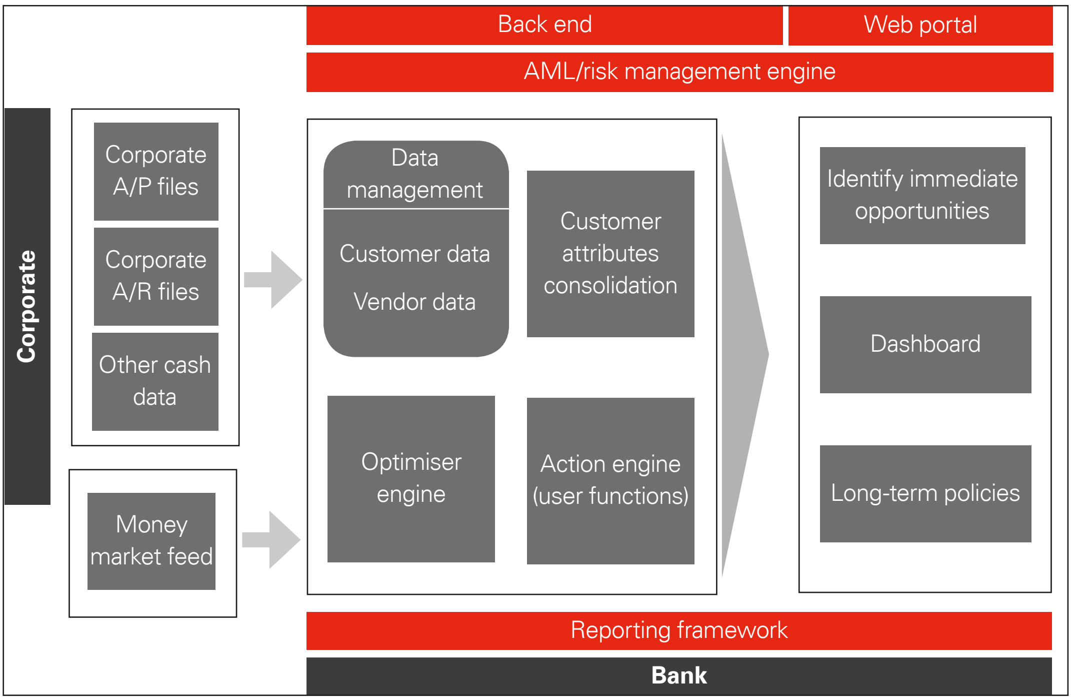
Figure 1 shows various options and recommended approaches that can be considered while deciding on a particular course of action. All the alternatives need to be examined to arrive at an optimal solution that will help maximise value and minimise cost for the corporate in its attempt to manage payables.

These offerings can be built by the organisation itself as in-house tools or they can be purchased from a third party. Another option is for banks to provide these services as a focused offering in a more sophisticated manner. One reason for this is that much of the information needed for optimising the management of payables (apart from information about the account itself) is easily available to banks. If organisations wish to use services based on their specific needs following a "use and pay" method, there is a strong possibility that they will be interested in receiving these services from a partner bank as part of their other existing offerings.

How Banks Can Help

Banks that are interested in providing such services to round out their core offerings can look at ways to develop these services so that they provide more value to their clients. Several offerings can be created within the A/P framework (see Figure 2) including:

Figure 2: Accounts Payable Management Framework



Source: Infosys Limited

Better Payment Terms from Vendors

A careful approach to managing payables includes getting better credit limits from vendors by involving the corporate's bank in offering non-borrowing limits such as bank guarantees or letters of credit (LCs).

These can be used to negotiate longer repayment tenors and larger limits with vendors. This focused activity will help to achieve better payment terms between the vender and the corporate during the LC renewal process.

Discounting Limits for Vendors

Banks can consider ways to offer discounting limits for organisations' vendors based on the creditworthiness of the organisation and its track record of prompt payments to vendors. This will encourage vendors to offer better terms to organisations that don't have cash flow problems because vendors can use the discounting facilities of organisations instead of their own banking limits. Banks can choose required corporate attributes to arrive at offer limits to vendors.

Analytical Tools for Organisations

Analytical tools such as financial cost/benefit calculators can be made available, which can calculate the trade-off between paying off payables on time versus prepaying to get discounts for early payments versus delaying payments and incurring penalties against the cost of borrowing funds to pay. These calculators can look at individual payments and take a portfolio view of payments over a specified period, and give a recommendation based on optimisation of an A/P portfolio. An individual view is more appropriate for one-off or infrequent larger payments, whereas the portfolio view would take care of a large number of smaller payments. A dashboard can monitor various payments due, changes in the money market, and alert the organisation to moneymaking opportunities or a reduction in the cost of funds.

Key Considerations

Organisations and banks should consider various inputs while deciding if A/P software packages provided by banks are justified by cost savings. With the changing regulatory environment, it may be worthwhile using these offerings on a trial basis, and revisiting the options based on long-term and short-term goals.

Organisations' Role

Organisations should take a holistic view of cash management and working capital management and consider A/P as an integral component in cost reduction. Additionally, willingness on the corporates' part to share A/P data with banks is required to make this initiative fruitful.

Banks' Role

The ability of banks to offer A/P services using secure channels and to keep customer information confidential are key considerations to selling these offerings. Banks can leverage their own risk management processes – anti-money laundering (AML) programs, for example – to secure client data, and subject them to the same level of scrutiny such as checking with AML blacklists to provide an added level of security.

Banks should consider a pre-packaged set of reports based on their own experiences in managing cash for multiple corporates. A bank can share best practices on A/P management with any organisation by making them available as part of the offerings. Based on data from several organisations, banks can provide useful comparative analyses of how an organisation is managing its A/P versus others in the industry. Banks can bring in their own high standards of security and control for the benefit of the corporate. By introducing such services, banks can increase their basket of offerings and strengthen their roles as a one-stop shop for the financial needs of corporates.

Conclusion

Today, most banks offer A/P solutions to their corporate clients in the form of a one-stop shop for making payments anywhere in the world. While this is a valuable service, it leaves little ground for differentiating a bank's cash management offerings from that of its competitors. A bank can distinguish itself if it increases the efficiency of the A/P process by providing services that enable organisations to better manage their A/P portfolios and maximise a defined value such as cost of borrowing or rate of return on investment.

The bank can co-create such a value-added service with an IT partner and use cloud computing to streamline time to market with minimal upfront investment. Corporates would benefit from more effective payables management and a reduction in overall working capital costs without the overhead of IT infrastructure investment. The IT vendor could leverage the co-created intellectual property (IP) to service other clients and share the IP revenue with the bank. Such a mutually beneficial partnership would create a win-win situation for all concerned.

Payments-On-Behalf and Collections-On-Behalf: A New Trend in Asia Pacific

- Payments-on-behalf and collections-on-behalf are attracting increasing interest from companies operating in Asia Pacific.
- On-behalf arrangements replace the practice of owning accounts for payments and collections; the company designates an agent to execute all associated transaction activities on its behalf.
- Given the regulatory landscape in Asia, the implementation of on-behalf arrangements is still at an exploratory stage.
- Despite the complexities involved, a range of potential opportunities are attracting companies to explore the possibility of moving to on-behalf structures.

Arthur Michael Tanseco, Vice President, Regional Product Management, Global Payments and Cash Management, Asia Pacific, HSBC, Hong Kong

The basic principles of payments-on-behalf and collections-on-behalf are fairly straightforward, but the challenges in implementing these structures can be significantly complex, as these touch on a number of critical areas such as the general payments and collections landscape, foreign exchange, banking guidelines, inter-company borrowing, and even tax. In both cases, a company designates an agent to execute specific activities on its behalf, usually documented through a formal agreement defining the nature of the relationship, and more importantly, outlining the underlying terms and conditions. It is also imperative to ensure that the relationship is demonstrably at arm's length to avoid any potential issues on transfer pricing.

On-behalf arrangements replace the conventional practice of owning accounts for payments and collections, and then participating in a central cash pool, usually managed by a central treasury unit. Instead, every transaction activity associated with either payments or collections, including the corresponding bank accounts, is assumed by the agent. In the process, the agent also gains direct and immediate control of any surplus liquidity across the organisation and is also able to impose a service fee, commensurate with the service it provides. The participating business units are paid credit interest on any surplus funds or charged debit interest on any deficit.

Given the regulatory landscape in Asia and the pace at which it changes, the possible implementation of on-behalf arrangements is still very much at an exploratory stage. While potentially extremely beneficial, these techniques might not be feasible for all markets in the region.

Where's the Interest?

While on-behalf arrangements seem to be potentially possible for any type or size of business, the underlying business drivers are more relevant to larger organisations that may already have achieved a certain degree of scale and sophistication in their treasury management infrastructure. Often, these are companies that are already running shared service centres, in-house banks and payment factories, and are looking to push their process efficiencies to the next level. In adopting on-behalf arrangements to complement their existing structures, they are able to further enhance the visibility and control of their cash.

There are a number of ways (depending on the underlying drivers) in which on-behalf arrangements can be implemented. However, what seems to be of particular interest today is the possibility of designating an overseas entity or a non-resident – usually the central treasury unit or payments factory acting via an in-house bank – to perform financial transactions on behalf of local business units.

What are the Drivers?

Despite all of the complexities involved, a range of potential opportunities are attracting companies to explore the possibility of moving to on-behalf structures. At the top of the list is the promise of improved cash visibility and control, although other benefits such as streamlining processes, reducing foreign exchange risk and managing financial costs are also important, and can further reinforce the supporting business case.

Even with the centralised payments and collections processing structures that companies have put in place today, many of these are still executed from bank accounts that are maintained and controlled by the local business units. Under this model, the central treasury unit may exercise a certain degree of visibility and control over the cash through the effective implementation of specific policies that are cascaded across the business organisation – usually policies on cash consolidation and centralised liquidity management, wherever possible.

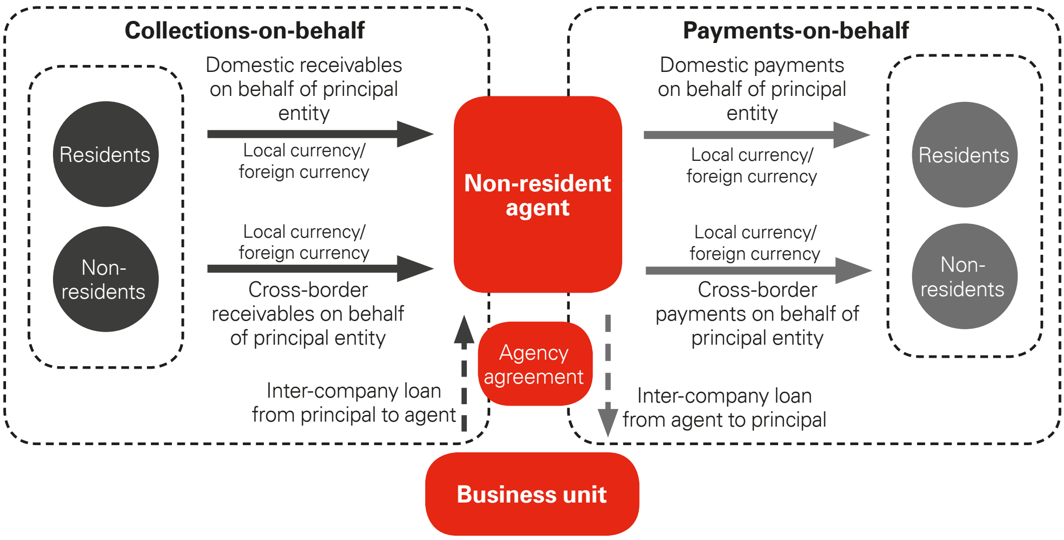
Although this approach may already be delivering substantial benefits to the company, additional synergies can be achieved by extending this to structures that involve payments-on-behalf and collections-on-behalf. Since such structures bring the cash closer to central treasury, there is a significant opportunity to enhance liquidity management, as well as drive further efficiencies in payments and collections management, thereby allowing the company's treasury unit to become more adaptive and agile.

Practicalities

While it is most efficient to implement payments-on-behalf and collections-on-behalf at the same time, it is currently more commonplace to see the former being adopted by companies, as the latter may pose a different and more demanding set of challenges.

The process flow for payments-on-behalf is straightforward (see Figure 1). As the business unit conducts its day-to-day business that triggers certain financial obligations, it sends a request to its designated agent, which executes the necessary payments to settle these obligations. The agent will then record this as a receivable from the requesting business unit, and depending on the situation, may book this as an inter-company loan. Once this process is established, the business unit no longer needs to have any dealings with a payment bank or to have a bank account for payments. Structures supporting payments-on-behalf present a unique opportunity to further streamline the payables process and achieve an optimum cash management structure, as they naturally force the business unit to sweep all of its cash to the designated agent's account.

Figure 1: Payments-on-Behalf/Collections-on-Behalf Mechanism



Source: HSBC

A similar process applies to collections-on-behalf, where the business unit instructs its customers (debtors) to remit their payments to a designated account owned and operated by the agent (see Figure 1). In this scenario, the resulting inter-company exposure may be considered as an investment by the business unit, on which interest will be earned on an arm's length basis. In a situation where both payments-on-behalf and collections-on-behalf are in place, further efficiencies can be achieved through a netting mechanism, whereby only the net position is squared off on a pre-agreed settlement date.

It is important to note that all the functional aspects of payments and collections will still remain intact despite the implementation of on-behalf structures, that is, the primary responsibility to meet the company's financial obligations will still rest with local treasury, or in some cases, the accounts payable team. Likewise, the sales team (in most cases) will continue to be responsible for the business unit's collections and will have to ensure that debtors adhere to the agreed payment terms.

Where is it Possible?

From the perspective of banking capabilities, supporting on-behalf arrangements is relatively straightforward. Global banks, such as HSBC, have the requisite infrastructure to make the implementation and execution similarly painless. However, the situation from a regulatory perspective is less straightforward and requires an understanding of where these structures are both legally and practically feasible. It is therefore essential, if considering payments-on-behalf and collections-on-behalf, to conduct thorough due diligence on the various critical considerations that arise, ideally in conjunction with a suitably qualified professional adviser that has a strong insight into the local regulatory and business landscape.

Based on a preliminary study conducted by HSBC of non-resident, on-behalf structures, countries in Asia Pacific can be broadly classified into the following categories:

- Open markets – where the local regulatory landscape is generally open and hence conducive to non-resident, on-behalf structures. These include Hong Kong, Singapore, Australia and New Zealand.

- Closed markets – where the local regulatory landscape is restricted from supporting non-resident, on-behalf structures. Although at present this definitively includes China and India, further analysis may expand this list of countries.

- Conditional markets – where the local market is highly regulated, but non-resident, on-behalf structures are still possible, although they will need to comply with various conditions that may include any or all of the following:
  — opening and operation of domestic non-resident bank accounts;
  — restricted domestic currencies;
  — restrictions on paying or receiving in local currency;
  — restrictions on borrowing or lending in local currency;
  — central bank reporting requirements;
  — documentation requirements, which may be one-time and/or on a per transaction basis;
  — transaction limits and caps on bank balances and borrowings; and
  — high transaction costs for non-residents, such as lifting fees.

In implementing on-behalf structures in these markets, companies will have to weigh the underlying costs of complying with such conditions against the expected benefits. For example, although countries like Indonesia and Korea appear to be able to support on-behalf structures, the reporting requirements may result in significant costs and challenges.

On the other hand, on-behalf arrangements operated using a resident agent appear more feasible, although they are still subject to the same considerations. Under this scenario, the company can explore appointing, or even registering, a local entity to perform on-behalf transactions.

What is Needed?

Apart from dealing with the questions of local regulation and reporting requirements, any company exploring a move to on-behalf structures will need to have already achieved a considerable degree of scale and sophistication in their treasury management infrastructure. From what we have seen so far, companies that have already achieved this will regard the move to on-behalf arrangements as a natural progression from an existing shared service centre, payments factory or in-house bank.

Sophisticated processes and technology are also required because on-behalf arrangements will typically generate a substantial number of inter-company exposures. Therefore, some form of netting system that is capable of handling any cross-currency implications will also be required.

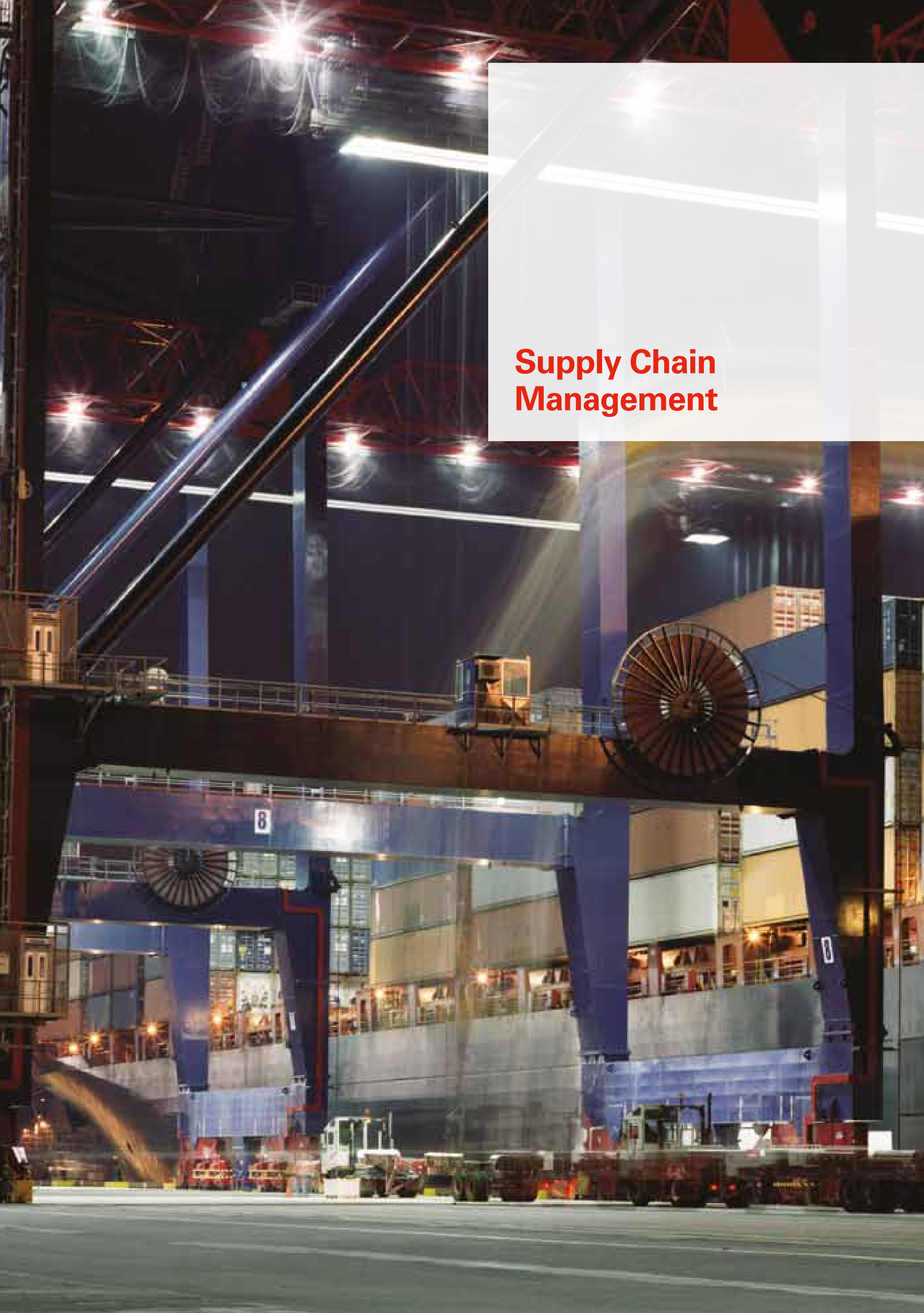
Payments-on-behalf and collections-on-behalf represent a significant milestone in terms of corporate psychology in that the treasury unit is effectively telling business units not to maintain their own bank accounts any more. Treasury will therefore need to have a strong presence and proven track record within the organisation to ensure that this can be achieved. If it already has a strong pedigree of adding value for local business units, then on-behalf arrangements will be considerably easier to implement from a cultural perspective.

As a result, HSBC is currently seeing initiatives for on-behalf arrangements primarily from large, sophisticated companies. These organisations are already operating centralised treasury units out of specialised tax locations, such as the Netherlands, and are able to implement on-behalf arrangements in "open" markets, such as Hong Kong and Singapore. Others have examined the possibility of doing the same in locations such as Thailand, but for the time being have concluded that the various reporting requirements and non-resident restrictions make this largely impractical. Other companies have opted for resident on-behalf structures instead, although the drivers and benefits are very different.

Conclusion

HSBC has conducted preliminary research and continues to enrich its knowledge and experience in this area by working with selected companies examining these opportunities. At this stage, it is apparent that subject to local conditions, these structures can potentially deliver significant benefits.
As Asia is in a constant state of evolution, it is difficult to say whether things will remain the same in the next few years. The question of whether the regulatory landscape will change for better or worse is something that cannot be answered at the present time. As with everything else in the region, it is a case of "wait and see".

Lastly, it is important to emphasise that the implementation of payments-on-behalf/collections-on-behalf in Asia Pacific is neither trivial nor straightforward. In addition to the necessity of working with specialists and professionals in banking, foreign exchange and, most especially, tax (e.g. leading accounting practices), to determine suitable structures and where these are feasible, it is also necessary to be clear about how such initiatives align with the company's overall treasury management approach.



Supply Chain Management

Guarantees in the 21st Century: Selective Evolution

- Guarantees are still a valuable tool in today's global marketplace, with their ability to be issued and be payable in a specific country, anywhere in the world.
- Guarantees can provide a vital sense of security in new commercial relationships between counterparties with limited or no prior dealings with each other.
- As new and more complex global transactions arise, guarantees continue to evolve and adapt to meet these challenges.
- Businesses seeking global guarantee solutions need to ensure that banking partners have the global network and the balance sheet capacity to meet their needs.

Raza Mahmood, Senior Product Manager, Global Trade and Supply Chain, HSBC

Guarantees are one of the oldest trade products but their traditionally paper-based nature can at times make them seem anachronistic. However, there are plenty of commercial situations where no other financial instrument is able to deliver the necessary flexibility and reassurance to support such transactions. While historically seen as a reactive and commoditised product, guarantees deliver a powerful business solution with intelligent structuring. They play a critical role in facilitating the smooth operations of even the most complex commercial transactions, particularly in areas such as large-scale infrastructure projects where numerous counterparties from around the globe may be involved. The financial standing of the issuing bank is an important factor to consider when selecting a banking partner.

Opportunities

As globalisation continues to gather momentum, guarantees are finding an increasingly vital role as the initial catalyst for complex cross-border deals. In many cases, they are the means by which domestic or regional corporations can globalise their businesses by bidding for previously inaccessible contracts in remote locations. The ability of guarantees to be issued and be payable in a specific country, anywhere in the world, provides a vital sense of security that underpins a new commercial relationship between counterparties with limited or no prior dealings with each other. One of the most important elements in such transactions is the customisable nature of a guarantee where it can be issued in a local language by a locally domiciled bank and under local regulations.

The nature of large development projects is changing around the world as multinational companies pitch for projects on foreign shores either independently or in cooperation with local firms. Such opportunities have given further relevance to guarantees as it is not uncommon in today's business world for an American company to build a resort in the Middle East, a Chinese company to pitch for the construction of an Olympic stadium in the UK or an Australian healthcare provider to establish a state-of-the-art facility in Brazil.

These projects are significantly more complex than the traditional bilateral use of guarantees as they will typically involve multiple commercial participants, several syndicate banks, foreign legal jurisdictions and various timelines. Given the unique nature of each deal, bespoke guarantee solutions can be structured to meet the specific requirements of the client. The common theme underlying any successful structured solution will be the bank's ability to leverage its knowledge of international guarantee practices, reputational strength to connect with top tier banks and the ability to access its balance sheet when required.

Standardisation

Guarantees are mainly issued subject to the law of the guarantor's jurisdiction or the jurisdiction of the beneficiary but an international code of practice also exists in the form of ICC Uniform Rules for Demand Guarantees (URDG) 758. The URDG is not a law but a set of guidelines established for the purpose of standardising global practices.

In 2010, the International Chamber of Commerce (ICC) revised its original URDG 458 for the first time since it was issued in 1991, to the current version URDG 758. This revision was executed over a period of two and a half years through collective work by a number of ICC constituent groups, managed as a joint project by ICC's Banking Commission and the Commission on Commercial Law and Practice. Contributions from over 50 national committees were submitted, which were then reviewed by the ICC Task Force on Guarantees consisting of 40 members from 26 countries.

Given the broad spectrum of parties involved across multiple countries in the revision of the original rules, the resulting URDG 758 is a more comprehensive version that reflects the inputs of a wider guarantee community. However, the application of local laws in cases of commercial disputes makes beneficiaries seek guarantees that are subject to those local laws and can be claimed in the beneficiary's country. So, while some international companies engaging with each other in cross-border guarantees may opt for those guarantees to be subject to URDG 758, the majority of domestic guarantees or instances where government departments are guarantee beneficiaries continue to be subject to local law, as it gives beneficiaries a tangible document as security governed by their local laws, possibly in their local language and claimable at a local location.

Despite their contemporary relevance in bringing the commercial world closer, there remain some peculiarities that define how guarantees are used in different parts of the world. The lack of governing law standardisation is the most obvious but another aspect that sets guarantees apart in today's world of e-documentation is the mode of guarantee issuance. While both applicants and beneficiaries have a common requirement in seeking a high degree of issuer credibility, there is a significant divergence when it comes to the medium used for requesting the issuance of a guarantee by the applicant and the receipt of the same guarantee by the beneficiary.

Applicants typically favour the convenience and lower costs of electronic issuance, particularly when multiple beneficiaries are involved. However, they are often impeded in this path to electronic issuance by the countervailing needs of beneficiaries, who typically prefer paper guarantees that can be seen, read and held as security. The underlying factor driving the beneficiary is the traditional association of guarantees as instruments issued by creditable institutions on their letterhead or legal stamp paper with relevant seals, stamps and signatures that provide a sense of protection to the bearer of that paper. Hence the beneficiaries, especially in emerging markets, prefer a tangible guarantee that can be seen and held as security while the applicant prefers an automated channel to issue guarantees, seek amendments and to generate reports on guarantee balances and upcoming expiry dates.

So while standardisation may have certain efficiencies, it is not something that can be applied across the board to guarantees. The needs and preferences of applicants and beneficiaries are different when it comes to the final delivery of the guarantee in terms of wording, governing law and mode of issuance. These differences need to be accepted and appreciated as they provide guarantees their unique place in the today's world of commercial contracts – as a product uniquely capable of facilitating global business, in part due to its non-standardisation.

Regulatory Requirements

Over the years, the evolving global regulatory environment has influenced guarantees, just like any other financial product, from a capital adequacy perspective. Under Basel guidelines, Capital Adequacy Ratio (CAR) requires banks to maintain levels of capital in relation to their risk weighted assets as a cushion for potential losses, thereby providing protection to depositors and other lenders.

Calculation of risk weighting may vary from country to country but general approaches are similar for countries that apply Basel guidelines. For guarantees, since the credit risk factor of non-financial guarantees is lower than that of financial guarantees, the balance sheet usage of capital is lower for non-financial guarantees.

Given the regulatory environment today and with the upcoming Basel III regulations, some banks have become selective about offering guarantee facilities, while others have ceased offering financial guarantees beyond a one-year tenor in order to conserve capital. Another driver in the regulatory space is the tenor of guarantees. Global economic uncertainty and market practice in some regions have given rise to an increasing requirement from beneficiaries for open-ended guarantees. Since open-ended guarantees require higher capital usage, they are not offered by all banks.

With today's tight market conditions and strict regulatory environment, businesses seeking global guarantee solutions need to ensure that their banking partners not only have the global network to support them but also the balance sheet capacity to meet their needs.

Conclusion

With the ongoing changes to the economic environment and increasing need for global connectivity by corporates, guarantees have become an even more relevant instrument for risk management and business facilitation. As new and more complex global transactions arise, guarantees continue to evolve and adapt to meet these challenges but only a select group of issuing banks, with resilient balance sheets, global networks, expertise and strong market reputation, are willing and able to deliver this capability.

Alternative Financial Supply Chain Solutions: Transfer Pricing Risks and Opportunities

John Kondos, Asia Pacific Leader, Financial Services Transfer Pricing, and **Kari Pahlman**, Principal, Asia Pacific Leader, Global Transfer Pricing Services, KPMG

- Whenever transactions cross borders – whether as an intra-group loan, purchase of a receivable, guarantee, cash sweep or service – transfer pricing issues arise.
- Understanding the transfer pricing consequences arising from financial supply chain models is critical for ensuring that desired bottom line benefits are achieved and maintained.
- Transfer pricing presents multinationals with both challenges and opportunities while they are implementing solutions to enhance their financial supply chains.
- While some considerations may seem complex, they are rarely roadblocks if considered well in advance, but not accounting for potential risks may lead to a wide range of transfer pricing issues.

Introduction

When multinationals look to optimise their working capital and streamline their business processes, ambitions and opportunities can be limitless. Changes usually start with integration of treasury and procurement organisations, reverse factoring, cash management and other such areas. These are often accompanied by establishment of shared service centres and strategic investments in technology.

If the process is managed masterfully, what emerges may not only help unlock trapped liquidity but also reward the multinational with an optimised tax profile. Conversely, not accounting for potential risks and challenges may lead to a wide range of transfer pricing issues and controversies.

There is an inadvertent propensity to underestimate the effects that global or regional initiatives and solutions may have on the overall corporate tax liabilities of the multinational group and to what extent these initiatives are under the transfer pricing lens of the tax authorities. In practice, whenever transactions cross borders – whether as an intra-group loan, purchase of a receivable, guarantee, cash sweep or service – transfer pricing issues arise.

A number of cases have demonstrated that understanding the transfer pricing consequences that can arise from the transition to and ongoing operation of financial supply chain models is critical for ensuring that the desired bottom line benefits are achieved and maintained, instead of remaining unmet or being reached then lost.

Changing Role of Treasury and Procurement

Historically, the management of cash has often been considered separate from purchasing and supply chain management. In practice, however, aligning the treasury and procurement functions has become a prerequisite for realising financial supply chain efficiencies. Not surprisingly, the transfer pricing considerations and opportunities associated with the transformation of treasury functions very closely resemble those in procurement.

For example, treasury and procurement functions may be organised in a decentralised manner, acting as local functions for business operations in a particular country. Alternatively, they may be structured in a more centralised manner as regional or global centres or hubs. Stand-alone treasury and procurement companies are also becoming increasingly popular.

Choosing the right approach based on the specific business circumstances drives efficiency in the supply chain and often gives opportunities to prevent unwanted tax leakage. Depending on the treasury and procurement model chosen, transfer pricing policies can range from cost plus service fees to the attribution of a margin or a portion of profits. From a transfer pricing perspective, closely aligning policies with the substance of business operations is a necessity. As such, it is crucial to evaluate the level of responsibility delegated to treasury and procurement functions as well as the risks that are effectively managed and assumed by these functions.

> **"From a transfer pricing perspective, closely aligning policies with the substance of business operations is a necessity."**

For instance, treasury may act as a pure head-office service provider, predominantly involved in providing routine assistance with arranging financial transactions on behalf of the affiliates belonging to the multinational group. Therefore, the treasury function may only be able to bear very limited risks. Similarly, a procurement unit may act as a "transaction hub" whose responsibilities only extend to executing contracts established by other affiliates. Given the limited functional and risk profile, the performance of such functions would likely result in lower but stable compensation; they could, for example, relate to a margin on the internal costs.

Conversely, treasury as well as procurement units may act as in-house intermediaries, doing business with affiliates on the same basis as third parties. This usually involves specific expertise as well as granting the units the ability to bear and mitigate related risks. As a result, activities may represent a strategic component of the supply chain, thus implying a more significant level of compensation that may depend on the value of the transactions or procured goods.

The emergence of wholly or partly centralised treasury functions also raises some conventional transfer pricing concerns such as arm's length intra-group financing rates and creditworthiness of the borrower. Additional care should also be taken in relation to the levels of debt and thin capitalisation regulations. In cases where the group treasury unit is seen as a funding source of last resort for the group, the question arises whether additional commitment fees should be factored in.

Where the benefits associated with centralised functions are to a large extent concentrated in the specialised treasury or procurement entity, the location of the entity becomes critical in realising an optimal tax position. This largely explains the preference of Hong Kong and Singapore for regional treasury and procurement centres within the Asia-Pacific region. In addition to their well developed infrastructure and attractive respective proximity to mainland China and South East Asia, they also offer relatively low tax rates together with other tax benefits.

For example, it may be beneficial to further explore Hong Kong's corporate income rules related to foreign sourced interest income tax in light of Hong Kong's expanding tax treaty network. When requirements are met, corporate treasury operations may benefit from a non-taxable spread between the borrowing and lending positions. The regulations may be even more attractive if treasury has its borrowings with the financial institution as this may result in deductible expenses and non-taxable interest income arising from subsequent lending of funds to overseas affiliates.

While supply chain structures can provide opportunities to improve a multinational's effective tax rate, challenges from tax authorities cannot be ruled out, in particular where the benefits are concentrated due to centralisation of key functions and risks. Centralised procurement and treasury entities are well advised to anticipate challenges from counterparty tax authorities and ensure that their transfer pricing policies and documentation provide clear and robust defence against such challenges.

Optimising Liquidity Management

Alignment of treasury and procurement functions not only contributes to integrated liquidity management and improved understanding of where cash is located but also provides a foundation to implement alternative supply chain finance solutions. Such solutions often raise transfer pricing considerations that require timely consideration.

Reverse Factoring and Other Supply Chain Finance Solutions

Emerging supply finance solutions may often help to extract additional liquidity from the operating cycle and there are a number of potential options available.

“Emerging supply finance solutions may often help to extract additional liquidity from the operating cycle and there are a number of potential options available.”

In the case of reverse factoring or supplier financing, the buyer works with suppliers to help them improve their efficiencies and reduce their financing costs by allowing them to leverage the lower financing rate of the buyer. In exchange, the buyer expects additional early payment discounts. Alternatively, other trade finance solutions are designed to help buyers with agreeing to extended payment terms with their suppliers.

At first glance, this seems to be a straightforward arrangement between third parties deploying a finance solution offered by the bank; therefore, it initially appears that such an arrangement should raise few transfer pricing concerns. However, in practice, in order to achieve the desired scale of supply chain finance solutions, regional or global treasury and procurement organisations have to take a lead role. As a result, the decisions of one affiliate affect the benefits and cost for all the other affiliates in the group and need to be taken into account in the transfer pricing policies.

Moreover, a large part of the trade finance solutions employ some sort of parental guarantee to the bank, which raises another question – how do affiliates benefit from such guarantees and what, if anything, should be paid to the parent acting as a guarantor?

Cash Management

While cash concentration structures and self-funding can have a positive effect by providing cheaper liquidity, there are a large number of issues that need to be considered by treasurers when looking at inter-company borrowing.

> **"While cash concentration structures and self-funding can have a positive effect by providing cheaper liquidity, there are a large number of issues that need to be considered by treasurers when looking at inter-company borrowing."**

Essentially, when the cash and liabilities of the affiliates are pooled and netted together, either by physical transfer of funds or by notionally converting cash available to the US dollar (or other functional currency) to calculate the balance of interest payable or receivable, the primary consideration is whether participants in the cash pool should exchange any form of payment with each other. Eventually, some of the affiliates in the structure will have accumulated surplus cash for which they could have received interest income had they not covered an overdraft in the accounts of other affiliates.

From a transfer pricing perspective it is important to restore the status quo that should exist in third-party arrangements, and set an appropriate deposit rate for the affiliates that effectively lend money in the group as well as an appropriate borrowing rate for the affiliates that utilise the overdraft facilities. Additional challenges in identifying an arm's length price may arise due to the large volume of transactions when deposit and lending rates with the bank vary depending on the size of surplus or deficit.

Further, the compensation of the treasury function operating the pool must be based on a detailed analysis of its risks and functions. The level of compensation appropriate for the central treasury unit depends on the pool's substance, the functions performed and the risks assumed. Depending on the circumstances, a central treasury unit could be regarded as a cost centre whereby the entire benefit of pooling is allocated to the participants. The central treasury unit could also be deemed a profit centre whereby a major portion of the benefit of pooling will be for the central treasury unit's account.

An additional complication is the aspect of credit rating differentials, a predominant driver of borrowing costs, together with the involvement of cross-guarantees inherent in the notional cash pools. From this arises the question of whether the affiliates with lower credit ratings should compensate the stronger members for the provision of the cross guarantee.

It is worth noting that cash pooling structures are rarely identical and usually represent a complex mixture of zero-balancing and notional pooling. Therefore, it is important to ensure that transfer pricing issues receive proper attention when solutions are implemented in order to address potential challenges and seize opportunities.

Looking One Step Ahead – Implementation

Transformation of treasury and procurement functions as well as successful implementation of supply chain finance and liquidity management solutions go hand in hand with integrated service centres and technology advancements. Multinationals are looking at automating their processes whenever possible, installing financial supply chains and working capital technologies and undergoing major enterprise resource planning projects. In practice, this usually means significant strategic investments in IT development, which is expected to deliver cost savings and efficient processes for all the members of the multinational group.

Given the scale of such investments as well as their strategic importance, decisions on such projects are often taken centrally while the results impact on the entire group. Such development projects may create intangible property that needs to be made available to the other group members at an arm's length price. There are wide opportunities to derive tax benefits from such developments if the structure is well considered in advance and tax is also factored into the location analysis. There is generally less room to manoeuvre and be flexible when developments are finalised.

Conclusion

Transfer pricing clearly presents multinationals with both challenges and opportunities while they are implementing solutions to enhance their financial supply chains. Though some considerations may seem rather complex, they are rarely actual roadblocks if considered well in advance.

Transformation of treasury and procurement functions usually involves very similar transfer pricing issues, putting strong emphasis on the value added by those functions in the supply chain as well as the correlation between value and remuneration. The choice of location for global and regional treasury and procurement centres usually is critical in terms of achieving an optimised effective corporate tax rate for the group. Subsequently implemented supply chain finance solutions usually imply more conventional transfer pricing issues such as setting arm's length interest rates, allocating of benefits or savings derived and pricing of guarantees.

Business changes and transformation of internal functions present an opportunity to integrate transfer pricing and business solutions and act proactively to secure optimal outcomes. A sound analysis together with robust documentation has immense value in defending such positions.

Supply Chain Finance: A Value Proposition Evolves

- The realities of the global economy, including trade and investment, are focusing attention on the small business sector and on higher-growth developing and emerging markets.
- For large corporates, there are a growing number of reasons to advocate the small and medium enterprise (SME) sector.
- Political and commercial support are improving SME access to trade finance; the sector also benefits from a renewed interest in emerging markets and commodity trade.
- Banks and trade financiers are assisting corporate clients by devising solutions aimed at providing liquidity to "strategic-supplier" SMEs and to the wider supply chain.

Alexander R Malaket, President, OPUS Advisory Services International Inc, Canada

"Cash is king" – a familiar expression that has been a part of business and finance in any part of the world where commercial ventures are driven by free market or quasi-free market dynamics, across segments from small and medium enterprises (SMEs) to large corporates.

The global financial crisis, and the related constriction of credit facilities and liquidity across the globe, brought certain fundamentals back into sharp focus, such as the importance of cash flow and working capital management. This renewed attention has been particularly timely, given the increasingly strategic role evolving for finance and treasury executives under current conditions.

Whether in the context of small businesses, or larger corporate enterprises, the role of the finance and treasury function has necessarily become more central to the effective management of an enterprise, given the relative scarcity of financial resources, and the additional disciplines of regulation and reporting imposed on finance executives – either directly, or indirectly as business executives work with their bankers and financiers to respond to increasingly stringent demands for transparency, to which banks and other financial institutions have been, quite rightly, required to respond.

Reasons to Advocate Small Business

The textbook concern about crises, and the adverse impact upon small businesses and developing/ emerging economies, appears to have played out exactly as most commentators had predicted: constricted credit and crisis-driven selectiveness related to client relationships and core markets, resulting in a magnified crisis among SMEs, and even more among SMEs based in developing or higher-risk markets. There is, however, room for optimism for advocates of small business, and for those who support the notion that trade is important to international development and the evolution of developing/ emerging economies.

We perceive several reasons for optimism, which, taken together, suggest that the crisis may generate long-term and sustainable benefits for SMEs and developing economies, despite the short-term pain. The following observations support this sentiment:

- The crisis has facilitated a change in market dynamics, likely to endure for some time, where public sector intervention is not only welcomed, but recognised as invaluable.
- The political rhetoric about the importance of small business to economic growth has intensified, both among national leaders and among heads of international organisations.
- Commodity trade and global sourcing patterns are evolving, involving a complex network of small suppliers across the world, including in isolated corners of the planet.
- International institutions such as the International Finance Corporation (IFC), the International Trade Centre and others have devised a rich set of programmes aimed at supporting small and micro-enterprises in developing economies.
- Banks, having reverted to fundamentals in lending, credit adjudication and risk analysis, have also shown greater interest in the SME segment as a client base.
- Trade finance has evolved into the open account and supply chain finance space.

What does this all mean for an entrepreneur, or a manager or finance executive in an SME, including such enterprises located in developing or emerging markets?

SME Access to Trade Finance

The political and commercial dynamics are aligning to offer some new opportunities for small businesses to access business and trade finance, in a variety of markets including developing and emerging economies.

The cost of trade finance for smaller businesses, in higher-risk economies especially, continues to be higher than for mid-market or corporate customers, yet the combination of factors at play, together with banks' decided desire to regain favour and the now more attractive margins to be earned from SME business, combine to create a set of conditions where business and trade finance ought to be more readily available. Trade finance, in particular, continues to reinforce its position as an asset class with very low loan-loss history, and therefore, one can expect the "bankability" of trade finance to be viewed positively among providers of trade finance – particularly those that know the SME segment, and that are active in developing and emerging economies.

In addition to the contextual factors, the development of integrated programmes around supply chain finance is a critical element that contributes further to the expansion of trade financing options for SMEs and for developing and emerging market based businesses.

As banks have sought to remain engaged in trade finance beyond traditional product offerings and in the context of supply chain activity, solutions have evolved from standalone products – even some long-existing mechanisms simply repackaged as supply chain finance – to sophisticated and comprehensive programmes aimed at supporting complex, geographically disparate global supply chains.

As with traditional trade finance, certain financial institutions have been quicker and more innovative in embracing and devising value-added solutions in global supply chain finance, and those leading institutions have devised programmes of various flavours – some of which look at the supply chain ecosystem on an end-to-end basis, and explicitly seek to devise solutions for smaller suppliers in the supply chain, even as these banks service the large corporate buyer/importer, for example, around which the supplier ecosystem revolves.

Support for Strategic Suppliers

Several events and tragedies over the course of the past year or more, have illustrated the adverse commercial consequences related to the disruption of global supply chains through the inability of suppliers to deliver even minor-seeming components, without which, it turns out, entire product lines cannot be delivered to end-consumers. This notion of a "strategic supplier" is an emerging element of focus on the context of global supply chain finance, and is one concrete illustration of the way in which a small business can better access financing and trade financing, under global supply chain finance programmes.

To be specific, banks and trade financiers have identified an opportunity to assist large corporate clients by devising trade and supply chain finance solutions aimed at providing liquidity to strategic suppliers, and to the extent viable, to the wider supply chain. Accordingly, it may be feasible, and attractive from a financing cost point of view, for small businesses to secure financing on the "strength" of a large buyer: whether that be in terms of financial strength and ability to borrow, or whether that be on the basis of the strength of a banking relationship, which then provides the source of funding.

Other programmes also exist, where large suppliers serve to "anchor" a supply chain finance solution, through which smaller buyers can access funding, including relatively cost-effective trade and supply chain finance.

In addition to the commercial initiatives launched by banks and other financial sector trade finance providers, SMEs have been targeted specifically as a client segment, by boutique firms whose services include significant amounts of advisory and transaction-level support – an area where larger institutions have also decided to better engage as a result of current market dynamics.

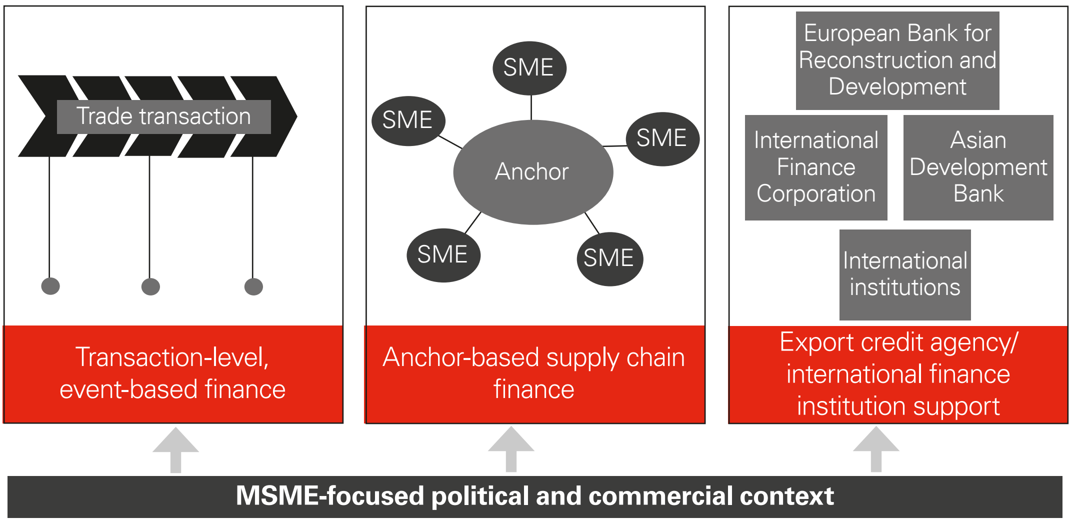
Arguments once used to justify under-serving the SME sector are less and less valid today, and while a single small business still rarely exercises meaningful leverage on a financial institution, the segment overall is deemed more attractive – to the point that even global financial institutions profess an interest in devising interesting product and solution offerings for small business clients. This reality can suggest that sector-level championing of SME interests and needs, both with financial sector providers and with public sector authorities, has the potential to be particularly effective.

Spotlight on SME Sector, Emerging Markets

Those financial institutions still sufficiently robust to pursue a meaningful international strategy are taking note of the realities of the post-crisis world, with near-default in the US and sovereign risk issues in Europe, contrasting attractive growth rates in China, India, Brazil, coupled with interesting opportunities in Vietnam, Indonesia, parts of Africa and Latin America.

The realities of the global economy and the context of international trade and investment are focusing attention on the small business sector, and on higher-growth developing and emerging markets. At the same time, public policy and the mandates of public sector and international institutions are focusing significantly on the SME sector, and on developing economies.

Figure 1: Focus on Micro, Small and Medium Enterprises (MSMEs)



Source: OPUS Advisory Services International

The IFC, a member of the World Bank Group, as well as the International Trade Centre in Geneva, the Asian Development Bank and others, have either developed or are beginning to devise solutions aimed at enabling micro, small and medium enterprises (MSMEs) in developing economies to access trade and supply chain finance at various stages in a trade transaction.

Despite long-standing empirical and largely industry-driven arguments to the contrary, it is clear (certainly in the crisis and post-crisis reality) that there is in fact a market gap in trade finance: a shortage of timely and fairly priced financing, especially relative to the needs of small businesses and emerging economies. By extension, it has become clear that public sector export credit agencies and international institutions have an important role to play in filling that gap, either providing financing directly, or working in partnership with local and international banks, to facilitate the provision of financing options through various guarantee schemes.

Opportunities Outscore Challenges

Entrepreneurs and financial managers in small businesses will be well served to take a fresh approach to identifying and engaging with potential providers of financing and trade finance. The universe of potential suppliers of trade and supply chain finance to SMEs is now significantly broader than perhaps was the case in a pre-crisis, cash-rich business environment.

Small businesses can quite credibly and legitimately approach large, even global financial institutions, either on a standalone basis (particularly those institutions positioning to serve the SME segment), or in the context of an existing supply chain relationship hinged on a large trading partner, which may be a value bank client. Smaller financial institutions, such as second-tier banks or credit unions may be quite receptive to facilitating dialogue for their SME clients seeking access to the expertise and resources of a regional or global institution.

Concurrently, SMEs ought to take the initiative to become intimately acquainted with the various programmes available through export credit agencies and international agencies such as IFC and others. To the extent that certain banks or other trade finance providers may not be fully versed in the options available through international institutions, a small business manager or entrepreneur seeking opportunities in international markets can usefully take a proactive role in informing their house banks about potentially valuable trade financing options.

Small businesses in developing and emerging markets will continue to face challenges related to the risk profiles (perceived and actual) of the markets in which they are based. They will also, however, benefit from renewed interest in emerging markets trade, commodity trade, and the SME sector as a driver of growth in developing economies, and as enablers of poverty reduction efforts.

Traditional trade finance products and solutions, offered over the lifecycle of a trade transaction such as pre-shipment finance to post-settlement funding, supply chain, anchor-client based financing solutions, export credit agency (ECA)/international finance institution (IFI) provided solutions driven by public policy and development imperatives (as opposed to purely commercial considerations) are all options potentially helpful to, and now available to, SMEs and micro enterprises in the current global business environment.

An educated choice related to effective trade finance solutions, and the selection of a well-matched partner, will be invaluable to the international success of a small business. Trade finance is, once again, a competitive advantage in the business of international trade, and it appears that SMEs – including those based in developing economies – may benefit from a confluence of positive circumstances, particularly if the leaders of these enterprises engage actively in shaping their circumstances in the trade and supply chain finance space.

Tax-effective Supply Chain Management: Evolving Landscape in China

- Reforms during 2008-2009 have changed the tax landscape for multinational companies (MNCs) operating in China.
- As the Chinese economy expands, there is pressure on MNCs to improve the efficiency of their supply chain structures in order to stay competitive and gain market share.
- Pilot schemes announced by the Chinese authorities in 2011 offer opportunities to MNCs looking to redesign their tax-effective supply chain management models.
- These schemes take advantage of RMB internationalisation and value-added tax reform, while managing the overall tax costs of doing business in China.

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The unification of corporate income tax laws in 2008 and reforms to value-added tax (VAT) and business tax (BT) in 2009 have changed the tax landscape for multinational companies (MNCs) operating in China. At the same time, the rapid expansion of the Chinese economy and the evolution of the global economic environment, including the global financial crisis, have pressured MNCs to improve the efficiency of their supply chain structures to stay competitive and gain market share.

More recently, starting from 1 January 2012, Shanghai has replaced BT with VAT in a wide range of services on a trial basis, as a step forward to the convergence between the BT and VAT regimes while the People's Bank of China (PBOC) provided additional guidance on a pilot scheme aimed at the internationalisation of the renminbi (RMB). The administrative guidance provided by the Chinese authorities brings new perspectives to MNCs looking at redesigning their tax-effective supply chain management (TESCM) model to take advantage of the opportunities resulting from the internationalisation of the RMB and the VAT tax reform while managing the overall tax costs of doing business in China. This article provides an overview of the potential TESCM planning opportunities arising from these pilot schemes.

Pilot Scheme on Convergence of VAT/BT Systems

In 2008, the Chinese National People's Congress (NPC) approved a five-year plan for the VAT Law legislative process and since then the Chinese authorities have been making efforts to research and formulate an approach to materialise the VAT Law legislative process. In March 2011, the Chinese Ministry of Finance (MOF) expressed in a press conference that pilot schemes would be set up in 2011 to enable certain supplies subject to BT to be included in the scope of VAT. On 16 November 2011, the MOF and the State Administration of Taxation jointly issued Caishui [2011] 110 (Circular 110) and Caishui [2011] 111 (Circular 111) setting out the details of the VAT pilot arrangements (VAT Pilot rules).

Shanghai was selected as the VAT pilot location and the VAT Pilot rules took effect on 1 January 2012. Transportation and certain "modern services" rendered in Shanghai or received in Shanghai from overseas are subject to VAT instead of BT. A new 6% VAT rate applies to certain "modern services", which cover six major categories: research and development, technological services, cultural, logistics and consultation services. Transportation services are subject to 11% VAT and leasing of movable goods is subject to 17% VAT, while a rate of 3% applies to small-scale VAT taxpayers. In addition, certain services "exported" out of China that were subject to a BT cost are now zero-rated or VAT-exempt. In the near future, it is possible that other cities (e.g. Beijing) could roll into the expanding VAT Pilot scheme.

General Implications of VAT Reform

Under the general Chinese indirect tax regime (excluding the VAT Pilot applicable to Shanghai), VAT applies to the supply of goods (including importation of goods) and the supply of services that are closely related to the supply of goods (i.e. repair and processing services) while BT is levied on services that are not subject to VAT, the transfer of real estate and intangible assets. The coexistence of these two indirect taxes has led to cascading effects that translated into significant costs of doing business in and with China. The convergence of BT and VAT is a step forward in introducing structural changes to the Chinese indirect tax system and in helping it to be more closely aligned with other global systems. BT is generally a non-deductible turnover tax, while VAT is generally creditable. The changes should eliminate certain tax costs caused by the BT's cascading effects. The changes are also consistent with the Chinese government's Five Year Plan, which strongly promotes the development of the services sector.

Figure 1: Comparison of VAT and BT Application Under General System (Excluding Shanghai) and Pilot Scheme (Shanghai)

Application Base	General System[1]	Shanghai VAT Pilot Scheme
Supply of goods	VAT	VAT
Supply of services	BT	VAT[2]

1. Under the current system, VAT is also applicable to the supply of services that are closely related to the supply of goods (i.e. repair and processing services).
2. For transportation and selected "modern services"; other services are still subject to BT.

Reactions to Consider for the VAT Changes

Companies doing business in/with China are advised to assess potential cost-saving opportunities, additional tax burdens, as well as new administrative, invoicing and accounting requirements in response to the introduction of the VAT Pilot. We expect rapid changes in the future, and suggest that companies stay abreast of the changes that are going to occur throughout 2012 and beyond.

Possible Planning Opportunity

Following the corporate income tax (CIT) reform in 2008, which significantly increased the tax burden for foreign investment enterprises (FIEs) operating in China by gradually phasing out the preferential tax policies applicable to FIEs in the production and export-oriented sectors, many MNCs have redesigned their TESCM structures to manage their overall tax costs while optimising their business models. To realise this objective, many MNCs have implemented or are currently considering a conversion of their manufacturing activities to toll/contract manufacturing activities in China.

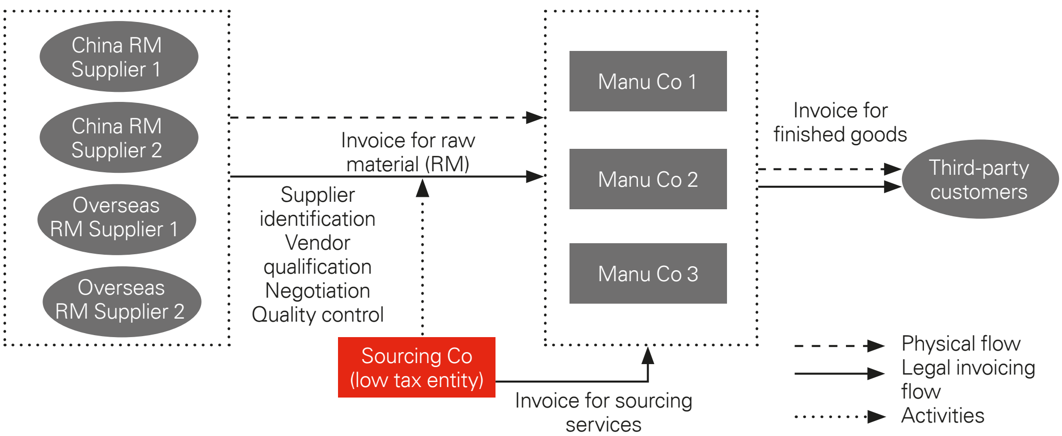
Under such structures, Chinese manufacturing subsidiaries of MNCs, which are now subject to high tax in China, have limited functions and risks and the key value-added functions and the corresponding risks and intangible assets are migrated to a principal company located in a low-tax jurisdiction. When designed properly, it is possible for MNCs under such structures to achieve significant tax savings by having the principal company earn the residual profits and limiting the profit of the contract or toll manufacturing subsidiaries in China to routine profit.

To ensure the sustainability of such structures, it is critical that the principal company has enough business substance and ultimate control over the value-added activities in the supply chain. Pressed for time, many MNCs are implementing such structures in quick succession and may be exposed to certain tax risks if the respective functions and risks of their manufacturing and principal entities do not support the characterisation of their related party transactions. Typical value-added activities that are good candidates to be transferred to principal companies to reduce the tax risk behind such tax planning structures include supply chain management (SCM) and procurement services.

Procurement

There is a clear trend in recent years of MNCs centralising their procurement functions and building up sourcing hubs to deal with the increased emphasis on cost reduction and the evolving complexity of manufacturing input qualifications. Such a movement could yield more synergy when it is integrated with other value-added activities such as design or quality control. Strategic cost savings could be achieved as a result of information advantage, the ability to leverage global logistics opportunities, risk management effectiveness, vendor rationalisation and other key contributing factors that could generate non-routine economic benefits. Depending on the functions undertaken, risks assumed and assets deployed by the procurement company, it could be compensated under a cost-plus method or a commission method (see Figure 2).

Figure 2: Transactional Model Under a Typical Procurement Company Structure



Source: Ernst & Young

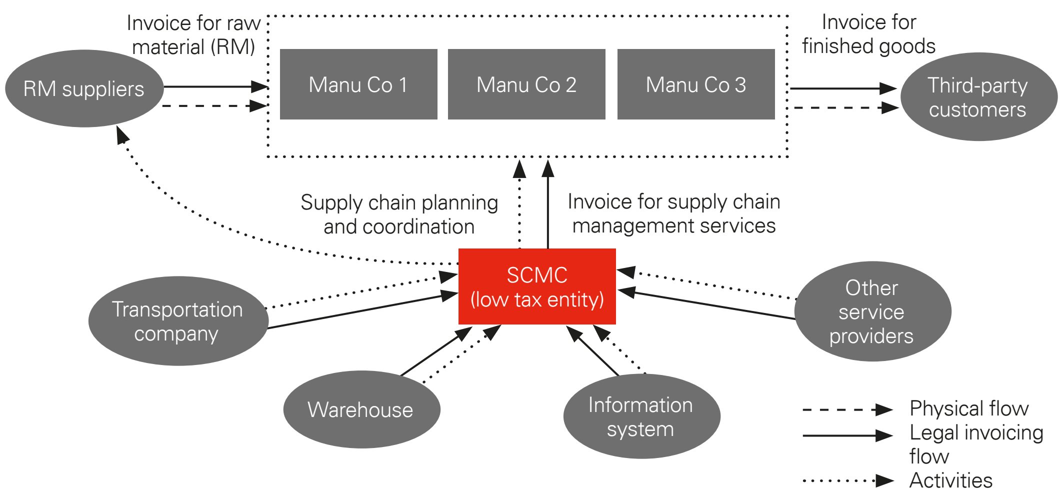
Supply Chain Management

Many MNCs have recognised the need for an effective supply chain to stay competitive in the global market. SCM typically involves the planning and management of business processes such as procurement, conversion and logistics management, covering activities ranging from the managing of raw materials and the processing of materials into finished goods, to the movement of finished goods to the end-consumer. The key supply chain processes include but are not limited to:

- product development and commercialisation;
- demand planning;
- procurement;
- order fulfilment;
- manufacturing;
- supplier relationship;
- customer relationship; and
- after-sales services.

Depending on the functions undertaken, risks assumed and assets deployed by the supply chain management service company (SCMC), the SCMC is compensated under a cost-plus method or a share of residual profits (see Figure 3).

Figure 3: A Possible Tax-effective Supply Chain Management (TESCM) Structure Using a Supply Chain Management Service Company (SCMC)



Source: Ernst & Young

Impact of BT and VAT Convergence

Under the general BT regime, these services would be subject to a non-recoverable BT (roughly 5.6% if it includes surcharges) if provided by the procurement company or SCMC. If there is no effective way to mitigate such BT costs, the potential income tax savings may be significantly reduced. Under the

Shanghai VAT Pilot scheme, transportation and certain modern services are no longer subject to BT leakage; instead, such services are subject to creditable VAT. Therefore, the new convergence between the VAT and BT system is likely to bring additional tax benefits to the TESCM structure for MNCs having operations in China and looking to centralise or transfer functions to a principal company located in a low tax jurisdiction.

Pilot Scheme of RMB Cross-border Trade Settlement

As integration of China's economy with the world economy increases, it is a natural trend for the RMB to become more widely used in trade and investment transactions. The Chinese government has promulgated a series of regulations over the past two years to promote RMB internationalisation.

On 1 July 2009, the PBOC, together with five other administrative departments, jointly issued a milestone circular "Administrative Rules on Pilot Scheme of Renminbi Settlement of Cross-border Trade Transactions" (China Banking Regulatory Commission (CBRC) Joint Announcement [2009] No. 10),[1] which is considered a significant step towards internationalisation of the RMB.

Under the pilot scheme, eligible enterprises in selected mainland cities (i.e. Shanghai, Shenzhen, Guangzhou, Zhuhai and Dongguan) will be allowed to settle in RMB for import/export of goods with their corresponding enterprises in Hong Kong, Macau and the Association of Southeast Asian Nations (ASEAN) countries.

This pilot scheme was further expanded on 17 June 2010 by the "Notice of Expansion on the Pilot Scheme of Renminbi Settlement of Cross-border Trade Transactions" (Yinfa [2010] No. 186), to enterprises in 20 provinces and cities[2] settling trade in RMB with any part of the world.[3] In addition, the scope of trade is expanded to cover service trade and other current account transactions.

The detailed implementation rules of the pilot scheme, which provide guidelines for eligible enterprises and banks, were also issued by the PBOC in July 2009.

The RMB cross-border trade settlement scheme allows the following settlement:

- eligible Chinese enterprises (including both domestic and foreign investment enterprises) can pay RMB to overseas trading partners;
- eligible Chinese enterprises can receive RMB from overseas trading partners;
- overseas parties can buy and sell RMB with the clearing bank (e.g. Bank of China Hong Kong); and
- banks outside China can buy and sell RMB with clearing banks, corresponding banks in China or other banks in the offshore markets.

Enterprises that undertake import/export businesses and are located in the selected cities, can apply to the local government (e.g. local ministry of commerce bureaus, depending on the local administrative measures on application) for the pilot status as eligible enterprises for RMB cross-border settlement. Tax bureaus are responsible for the review of the applicant enterprises against certain criteria stipulated in the State Administration for Taxation Circular Guoshuihan [2010] No. 303.[4] At the end of 2010, there were 67,359 companies approved as eligible enterprises in China.[5]

RMB Business in Hong Kong

China's 12th Five Year Plan designates Hong Kong as an offshore RMB financial centre for China. The pilot scheme is a step towards achieving that goal. Under the pilot scheme, a comprehensive range of offshore RMB products and services can be provided by overseas financial institutions participating in cross-border trade settlement, including deposit-taking, currency exchange, remittance, trade financing, cheque and credit card services and issuance and trading of RMB bonds.[6]

As regards Hong Kong, participating banks can provide, among others, a wider range of RMB services.[7]

Deposit-taking

Hong Kong residents, "designated merchants" (those belonging to the seven categories of retail sales, catering, accommodation, transportation, communications, medical and educational services), as well as trade enterprises (from July 2009), can open RMB deposit accounts with Hong Kong participating banks. As of July 2011, RMB deposits in Hong Kong stood at RMB572bn.[8]

Currency Exchange

Designated merchants can exchange RMB cash obtained from their normal course of business for Hong Kong dollars (HKD) (one-way) without limit. RMB bond issuers in mainland China (the Mainland) can convert RMB to HKD for the settlement of expenses incurred in bond issuance. Since July 2009, trade enterprises have been able to exchange HKD for RMB or vice versa, based on actual trade transactions.

Remittance

Issuers of RMB bonds in Hong Kong can remit proceeds from bond issuances to the Mainland. Starting from July 2009, two-way remittances can be conducted between enterprises on the Mainland and those outside the Mainland, based on actual trade transactions. Fund transfer services within Hong Kong are also available, but such transfers are confined to those between "same-name" accounts of the same enterprise held at different banks for pooling RMB funds to make payments in relation to trade settlement.

Trade Finance

With the launch of the RMB trade settlement pilot scheme in July 2009, Hong Kong participating banks can provide trade finance to enterprises outside the Mainland that choose to settle their trade with Mainland enterprises in RMB. Such trade finance should be limited to the amount of a corresponding trade transaction, and be paid directly to the Mainland enterprises.

Cheques

RMB cheques drawn on current accounts held with Hong Kong participating banks can be used both in Hong Kong and on the Mainland. Within Hong Kong, customers can make payments and fund transfers in relation to subscription and acquisition of RMB bonds. On the Mainland, RMB cheques can be used for consumer spending in Guangdong province, subject to a daily limit of RMB80,000 per account.

Starting from July 2009, RMB cheques can be used for transferring funds between "same-name" accounts held by the same enterprise at different banks for pooling RMB funds for trade settlement.

RMB Bonds

Since 2007, Mainland financial institutions, after obtaining relevant approvals, can issue RMB bonds in Hong Kong. In 2009, the range of issuers was extended to Mainland subsidiaries of Hong Kong banks. The amount of bond issuance has increased over the years, from RMB10bn in 2007, to RMB12bn in 2008, and to RMB16bn in 2009. The range of issuers has also expanded over time. To date, apart from the MOF, the issuers that have issued or launched RMB bonds in Hong Kong include: China Development Bank, China Export and Import Bank, Bank of China, Bank of Communications, China Construction Bank, HSBC (China), Bank of East Asia (China), Hopewell Highway Infrastructure Limited, McDonald's, the Asian Development Bank and the International Finance Corporation.[9]

Cross-border Trade Settlement

The launch of the pilot scheme for cross-border trade settlement in RMB on 1 July 2009 was a significant milestone in the continuing development of RMB business in Hong Kong. The scope of RMB banking has been expanded with authorised institutions now offering a range of services for trade enterprises using RMB as the settlement currency for their trades with the Mainland. For the first half of 2011, the RMB cross-border settlement in Hong Kong amounted to RMB804bn, a significant increase from the 2009 annual figure of RMB369bn.[10]

It has been emphasised in the speech made by Vice Premier Li Keqiang during his visit to Hong Kong on 17 August 2011[11] that China's central government is supportive of the development of an offshore RMB business centre in Hong Kong. One of the new policy measures to improve cross-border settlement for Hong Kong is the expansion of the scheme to make it nationwide. Soon after the vice premier's speech, a new circular was released on 23 August 2011 stipulating that RMB cross-border settlement is expanded to the whole country with immediate effect.[12]

Cross-border RMB Direct Investment and the Channel of RMB Flow to China

On 6 January 2011, the PBOC issued another landmark circular, "Administrative Rules on Pilot Scheme of Renminbi Settlement of Overseas Direct Investment". Under the scheme, non-financial enterprises in the selected cities are allowed to conduct and settle overseas direct investment in RMB, and the profits derived from the overseas direct investment can be repatriated back to the Mainland in RMB.[13] This scheme is important to allow the circulation of RMB funds to China.

Also mentioned in the speech made by Vice Premier Li Keqiang are new measures in the offing for the introduction of an RMB Qualified Foreign Institutional Investors (RQFII) scheme for investing in the Mainland's securities markets (with an initial quota of RMB20bn) and a pilot arrangement for foreign banks to increase the capital of their Mainland subsidiaries using RMB. These are considered as a further expansion of the channels for the flow and circulation of RMB funds from Hong Kong to mainland China.

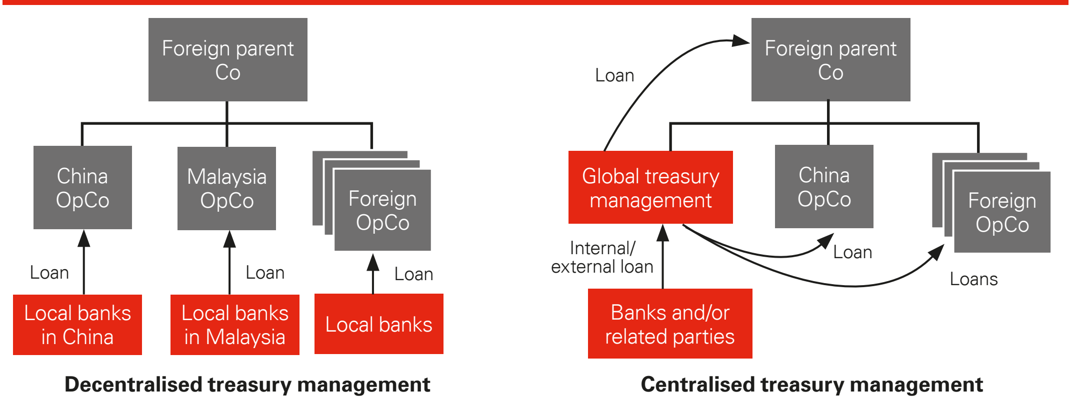
Challenges and Opportunities for Global Treasury Management

MNCs nowadays are facing several issues in global treasury management: managing foreign currency risks, consolidating cash pools and controlling costs of finance, to name a few. In order to keep up with the constantly changing economic and regulatory environment, MNCs search for better global treasury management solutions, which could bring about more efficient use of cash and better liquidity management, minimise external borrowings at non-competitive rates, consolidate management of foreign exchange (FX) risk to minimise exposure and reduce transaction and administrative costs.

Figure 4: Challenges/Benefits of a Decentralised/Centralised Treasury Management Function

Challenges of decentralised management	Opportunities of centralised management
• Inability to forecast cash needs at the group level and pool cash reserves • Debt managed at an individual local country level, leaving possible gaps in risk management • Relatively high funding costs (bank charges on international payments, administrative fees from numerous bank accounts, etc.) • Size of group and synergies need to be leveraged better (duplication of duties in various operating subsidiaries) • Use of debt not optimised within the corporate group	• More efficient use of cash and better liquidity management • Minimisation of external borrowings at non-competitive rates • Cost reduction by reducing number of banks used (consolidated management of FX risk to minimise exposure and reduce transaction and administrative costs) • More competitive borrowing rates • Tax efficiency • Improved risk management and liquidity management (greater transparency, access and control over cash, collections and payments in various currencies) • Elimination of duplication of duties by centralising payment processing

Figure 5: Decentralised vs Centralised Treasury Management Structures



Source: Ernst & Young

When implementing a global treasury management function or centralising the local treasury management function of a subsidiary, numerous operational and tax considerations should be analysed to assess the feasibility of such conversion, including the total cost savings potential, the impact on the overall SCM and the flow of physical goods and invoices.

Figure 6: Issues and Considerations in Setting up a Global Treasury Management Function

Issues	Considerations
Group treasury management	• Recommend ways to capture cost reduction potential and improve transparency on current and future cash flows • Recommend improvements to cost structure • Share best-in-class experience on transparency of current cash reserves and standardised cash flow forecasting tools
Group financial strategy	• Explore the feasibility of an in-house bank by refinancing its operating company's (OpCo) foreign debt with debt to take advantage of cheaper funding cost at the foreign financing affiliate (FinCo) and consolidate currency exposure at FinCo • Explore the structure and practicality of inter-group financing
Corporate governance	• Review policies for cash, borrowings, derivatives and FX transactions at FinCo and OpCo levels • Identify gaps and recommend areas for improvement
Taxation and regulatory implication	• Tax considerations at FinCo and OpCo levels: — Direct and indirect tax review and opportunities for tax planning — Withholding tax on interest payment for refinancing — Implication of direct and indirect tax on gain or loss arising from (early) retirement of debt — Potential permanent establishment risk to FinCo in its capacity as lender — Availability of supporting documentation and filing requirements — Applicability of thin capitalisation and interest restriction rules — Transfer pricing considerations (e.g. complying with thin-capitalisation provisions, determining arm's length interest rate on related party financing and appropriate allocation of cost savings resulting from participation in global treasury pool) • Respective FinCo and OpCos exchange control requirements
Implementation and roadmap action required	• Create framework and timetable with consideration to: — New mission statement and objectives — Possible organisation restructure demarcating responsibilities between companies in group — Tools to increase transparency and ensure efficient allocation of capital

Finally, the internationalisation of RMB provides an opportunity for MNCs to restructure their global treasury management and, especially for those companies that have strong trade ties with China, to leverage the new measures for offshore RMB settlement. Furthermore, while companies are integrating their movement of goods, functions and roles from different geographic locations, it is also important to redesign cash movement and integrate global treasury management for the overall efficiency of SCM and the flow of physical goods and invoices.

Conclusion

Benefits resulting from changes in supply chain can be increased if tax and other regulatory considerations are taken into account. Tax planning incorporated into the company's business model and regulatory changes are allowing MNCs greater flexibility to optimise tax savings. With a thorough consideration of the particularities of the Chinese tax system and regulatory and business trends, an effective TESCM structure can mitigate the tax costs arising from China's CIT and VAT/BT reforms while optimising tax saving opportunities.

Endnotes

1 *CBRC Joint Announcement [2009] No. 10 "Administrative Rules on Pilot Scheme of Renminbi Settlement of Cross-border Trade Transactions" and Yinfa [2009] No. 212 "Detailed Implementation Rules on Pilot Scheme of Renminbi Settlement of Cross-border Trade Transactions".*

2 *18 provinces are added to the list: Beijing, Tianjin, Inner Mongolia, Liaoning, Jilin, Heilongjiang, Jiangsu, Zhejiang, Fujian, Shandong, Hubei, Guangxi, Hainan, Chongqing, Sichuan, Yunnan, Xizang and Xinjiang. The entire Guangdong province is covered instead of only four cities.*

3 *The overseas areas are expanded to include all countries and regions.*

4 *Guoshuihan [2010] No. 303 "Notice of Evaluation on the Pilot Enterprises under Renminbi Cross-border Settlement Scheme and Tax Refund on Exports of Goods".*

5 *PBOC news release dated 6 December 2010. (www.pbc.gov.cn/publish/goutongjiaoliu/524/2010/20101206184442957396214/20101206184442957396214_.html).*

6 *Hong Kong Monetary Authority (HKMA) circulars dated 6 July 2009 and 11 February 2010.*

7 *HKMA news release "Renminbi Business in Hong Kong" dated 11 June 2011.*

8 *HKMA statistics, July 2011. (www.info.gov.hk/hkma/eng/statistics/msb/new_msb_tables_b.htm).*

9 *HKMA booklet "Hong Kong: The Premier Offshore Renminbi Business Centre" (29 June 2011).*

10 *HKMA statistics (www.info.gov.hk/hkma/eng/press/2011/attach/20110831e5a1.pdf).*

11 *Speech of Vice Premier Li Keqiang on 17 August 2011.*

12 *"Notice of Expansion of Selected Areas on the Pilot Scheme of Renminbi Cross-border Settlement of Trade Transactions".*

13 *PBOC Announcement [2011] No. 1 "Administrative Rules on Pilot Scheme of Renminbi Settlement of Cross-border Foreign Direct Investment".*

BPO: An Instrument for the Next Generation of Trade and Finance

- For mitigating trade risk, market focus is shifting to sophisticated solutions that rely on an understanding of end-to-end supply chain processes and workflow.
- SWIFT is collaborating with other industry bodies to advance the adoption of new products/services, and a common set of definitions, suitable for open account trade.
- One such instrument is the Bank Payment Obligation (BPO), an irrevocable obligation of an obligor bank to pay a specified amount to a recipient bank.
- The BPO provides an assurance of payment, mitigates risk and has the potential to be used as collateral in working capital financing.

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Despite the challenges raised by the recent financial crisis, the value of international trade has continued to grow, fuelled by ongoing globalisation and harmonisation. Developing countries adopting trade liberalisation policies have experienced favourable effects on both international trade and economic growth. Of course, the global markets remain dominated by three major economies, the US, China and Germany, both on the import side and the export side. Together with France, Japan and the UK, these six countries account for 40% of world trade. Having said that, trade touches every nation in the world, from Aruba to Zimbabwe. In ever changing market conditions, there are many economic indicators that increasingly will influence the future direction of trade growth, including debt service ratios, carbon dioxide emissions, industrial outputs, inflation indices and a host of other natural facts related to individual economies.

Goldman Sachs has predicted that China and India, respectively, will become the dominant global suppliers of manufactured goods and services whilst Brazil and Russia will become the dominant forces as world suppliers of raw materials. China today has a current account surplus of almost USD400bn while the United States has a current account deficit well in excess of USD700bn. According to HSBC, more than half of China's total trade flows – primarily bilateral trade with emerging markets – will be settled in renminbi by 2015. This will further strengthen China's influence in geopolitical and economic affairs. At the same time, India's population is set to grow by almost 30% by 2025 while, for example, 30% of Japan's population is aged 60 or over, according to *The Economist*. In addition, the evolution of modern transportation systems has significantly increased availability and accessibility to international trade, all the way from the Silk Road to Silicon Valley.

While much has been written and spoken about the emergence of the so-called BRIC economies (Brazil, Russia, India, China), a significant amount of growth is accounted for by distinct regional trading blocs, including MERCOSUR (Mercado Comun del Sur in South America), the GCC (Gulf Cooperation Council) and APEC (Asia Pacific Economic Council). More recently, we have also witnessed the growing influence of the SEMNS bloc (South Africa, Egypt, Morocco, Nigeria and Sudan).

International transactions can of course be simple; or they can be complex. What is certain, however, is that in all cases the transaction is not complete until the goods or services have been delivered, payment has been made and all related obligations have been fulfilled. Ensuring that these three basic criteria are met is all about the management of risk. There will always be concerns regarding fulfilment of a contract and finality of payment. More often than not there will also be interim concerns related to the availability of working capital finance. Expanding into new markets can be profitable but only if the risks are adequately controlled.

Looking Beyond Traditional Methods

Traditionally, risks related to non-delivery and/or non-payment have been mitigated by the use of financial instruments, most commonly the documentary letter of credit (LC). Some believe that the history of the LC can be traced back originally to ancient Egypt and Babylon, dating from 3000 BC. There are scholars who also believe that the development of LCs in Europe was largely inspired by the discoveries of Marco Polo in China in the 13th century. One thing is certain; the LC has been around for a very long time.

Yet it has been true for some time now that the adoption rate for documentary credits as a means of mitigating trade risk has been in steady decline. Conventional wisdom suggests that somewhere between 80% and 90% of international trade today is conducted on open account. While the elimination of cumbersome document checking has reduced an element of cost, the removal of the underlying security has significantly altered the risk dynamics in buyer-seller relationships. Increasingly empowered by the Internet, large importers have positioned themselves more and more to dictate the terms of trade, favouring the freedom of open account over the impediments of documentary trade. Rapid advances in automation have greatly expanded the scope for streamlining financial processes, giving birth to collaborative platforms in support of new ways of doing business, for example through document dematerialisation, automated data matching and workflow management and electronic invoicing.

At the same time, an equally important development in recent years has been the increased demand for capital rationalisation, or cash management. Decisions relating to payment terms, the choice of settlement currency and financing options have a direct impact on the underlying capital requirements. Market focus has shifted away from the management of transaction risk to more sophisticated working capital management solutions, which rely on an understanding of end-to-end supply chain processes and workflow. Though the old view of the supply chain was about warehouses, distribution centres, trucks and planes, now it's about people, processes, products and information. There is a demand for new products and services to address the changing needs of the market and a demand for new rules and tools for the next generation of trade and finance.

New Tools for Supply Chain Finance

Supply chain finance relates to the use of any financial instruments that optimise the working capital of supply chain processes, while enabling the reduction of operational risk and cost. This definition extends itself beyond so-called reverse factoring, approved payables finance and purchase order commitment to pay to include the full range of traditional products, including LCs, collections and standbys.

In essence, we are looking at events that happen in the physical supply chain, relating to the physical movement of goods, as evidenced by the underlying documentation, acting as trigger points for the delivery of financial supply chain services. The documents in question can be anything from a purchase order to a commercial invoice, a bill of lading, an inspection certificate, an insurance policy and so on. Whereas in the past banks have found it necessary to examine and "match" every word on every line of every document, today it is possible through the deployment of new technology to extract those elements of data that are relevant to the financial decision-making process and perform the matching process electronically.

This not only simplifies the process of determining whether a transaction is compliant or not but it also removes any element of subjectivity regarding the analysis of potential discrepancies. In an automated system, data either matches or it does not and where it does not a participating bank can decide whether to accept a mismatch or reject it. Costly disputes and delays with goods incurring demurrage charges in transit are avoided.

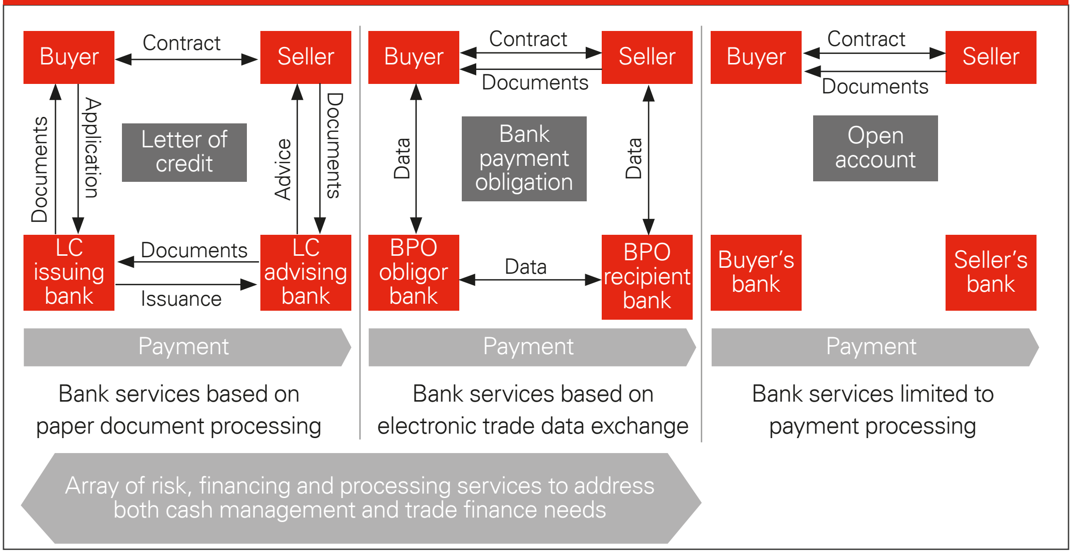
To support the delivery of new products and services through the deployment of new technology, an essential element is that of standardisation. A popular joke used to be that the great thing about standards was that there were so many to choose from. Even today, there are many different messaging standards that exist to cover different geographies and business areas. Many individual institutions use their own proprietary standards internally and externally. The use of different syntaxes and different semantics is a barrier to the end-to-end automation of value chains.

The International Standards Organisation (ISO) is an international standards setting body composed of representatives from 160 national standards organisations. It promulgates worldwide standards in a variety of domains designed to facilitate the cross-border exchange of goods and services. ISO 20022 is an agreed methodology adopted by the financial services industry to create consistent messaging standards across all business processes. The ISO 20022 method is based upon separate layers to support business processes and concepts, logical message models and syntax.

In the world of supply chain, ISO has approved for adoption a range of 50 standardised XML messages that have been developed by SWIFT to enable the exchange of data extracted from a comprehensive range of trade documents. These messages can be used by financial services providers to exchange information in a standardised way via a third party data matching application so as to establish a common view of an individual transaction against which a variety of financial services can eventually be made available. These messages are currently in use in SWIFT's Trade Services Utility (TSU) but can equally be applied in any alternative technology platform where the matching of data performs an essential part of the required workflow.

One of the optional components in the messaging workflow is a Bank Payment Obligation (BPO). A BPO is an irrevocable obligation of an obligor bank to pay a specified amount to a recipient bank according to the established terms of a single transaction. A BPO will constitute a legally binding, valid and enforceable obligation of the obligor bank to the recipient bank under the appropriate standard of law, enforceable in accordance with its terms. The BPO will not only provide exporters with an assurance of payment; it will mitigate risk for all parties and has the potential to be used as collateral for the provision of working capital finance.

Figure 1: The BPO is a New Payment Risk Mitigation and Financing Instrument



Source: SWIFT

New Rules to Support International Trade

As a member-owned co-operative, SWIFT acts as a catalyst to bring the financial community together to work collaboratively to shape market practice, define standards and consider solutions to issues of mutual interest. In 1919, the International Chamber of Commerce (ICC) was established to facilitate the flow of international trade. The Uniform Customs and Practice (UCP) was later introduced as a means of addressing the inconsistent use of national rules as set by individual countries. The UCP remains the most successful set of private rules for trade ever developed.

SWIFT believes that by working closely with the ICC, the BPO can become established as a new market practice consistent with the changing needs of the market, supported by a standardised legal framework and a standardised set of ISO 20022-accredited financial messages.

This work is further complemented by BAFT-IFSA's 2010 publication of a set of standard product definitions for open account trade processing and open account trade finance to support the need for a common understanding of the terminology used in managing such transactions.

Both the ICC and SWIFT believe that by working together and leveraging their respective positions across the trade finance community, the BPO will have an important role to play in supporting the development of international trade in the 21st century and in addressing cost pressures in the face of increased automation and changes in the regulatory environment.

In its existing form, the commercial availability of a BPO is restricted to a closed user group of financial institutions subscribed to SWIFT's TSU service. The usage and enforceability of the BPO today is governed by SWIFT's contractual documentation (i.e. the TSU Service Description and Rulebook). In order to promote wider adoption of this new financial instrument the ICC will validate the existing set of rules and adapt them as necessary in order that a BPO can technically be delivered through any underlying technology platform that is capable of supporting the defined workflow, making use of the relevant ISO 20022 open messaging standards. It is the intention of the ICC to publish the revised set of rules not later than 2013.

In order to support the ICC in its evaluation of the BPO, SWIFT will continue to work with its existing membership in order to present additional evidence of commercial usage and value. Both the ICC and SWIFT recognise the need for registered financial institutions to make continued use of the BPO in its existing form and supported by the existing legal framework, using the TSU as the delivery channel. This will ensure that the evidence brought before the ICC during the course of its deliberations will demonstrate the relevance of the BPO in supporting the collective needs of importers and exporters as well as meeting the requirements of the financial services industry.

A standing committee, the ICC BPO Working Group, co-chaired by the ICC and SWIFT, has been created to ensure that the joint objectives of the two organisations are fulfilled. This group is responsible for developing the legal framework, promoting market awareness through education initiatives and promoting market adoption through ongoing commercialisation.

Benefits of a BPO to a Seller

- The seller is assured of payment as long as the terms and conditions are complied with.
- The seller can obtain more flexible access to pre-shipment or post-shipment finance.
- The credit risk is transferred from the buyer to the obligor bank.
- The BPO reduces risk for situations in which the buyer may wish to cancel or change the order.
- The buyer cannot refuse to pay due to a complaint about the goods.
- Foreign exchange risk can be eliminated with a BPO issued in the currency of the seller's country.
- The seller can structure the delivery schedule according to the seller's interests, determining when payment will be made and shipping the goods accordingly.
- The bank bears responsibility for any oversights.
- Automated data matching reduces complexity and increases reliability.
- By removing the subjectivity of physical document checking the risk of discrepancy, dispute and delay is reduced.
- A BPO can be introduced at any stage of the transaction and mismatches can be accepted.
- Automated processing accelerates settlement and financing, resulting in enhanced cash flow forecasting.

Benefits of a BPO to a Buyer

- Facilitates financing for the buyer e.g. extended payables.
- The buyer can structure payment according to the buyer's interests.
- The buyer can confirm that the goods are shipped on or before the due date to the required specification.

- Safer than prepayment. The buyer does not have to pay up front before receiving the documents of title to the goods purchased.
- The buyer can negotiate better terms and conditions. By issuing a BPO, the buyer demonstrates the ability to pay and can negotiate improved terms in the future.
- The BPO protects the buyer since the bank only pays when the seller complies with the specific terms and conditions and produces the data required.
- The buyer can build safeguards into the BPO, including inspection of the goods and quality control, and set production and delivery times.
- A BPO helps to expand business opportunities. It may increase competitiveness in foreign markets.
- A BPO strengthens buyer/seller relationships. It secures the supply chain.
- A BPO increases convenience and reduces cost, facilitating enhanced management of cash positions.

Benefits of a BPO to a Bank

- Low risk business and prudent use of capital;
- Steady source of commission and fee income;
- Opens the door to new business opportunities;
- Strengthens core relationships;
- Automated solution leading to lower operating costs; and
- Meets the market requirement for banks to collaborate more on risk and client on-boarding.

Conclusion

Whatever the business context, importers and exporters, large and small, share three common goals: to minimise risk, to minimise the cost of payment and to minimise the cost of finance. For service providers to be able to offer solutions that satisfy these needs they need access to the right information at the right time. Information is the common link that brings together the physical and financial supply chains. Investment in new technology to support the automation of relevant business processes will enhance the quality of service delivery.

There is no denying that the automated matching of data is more efficient than the physical checking of documents. Since the market has for many years placed its unerring trust in an instrument that creates an obligation to pay based upon the physical presentation of compliant documents it surely follows that the time has come to consider the adoption of a new instrument that creates a similar obligation to pay based upon the electronic presentation of compliant data. The BPO is that instrument.

Connectivity

Switching Tracks: Putting Customer Experience to the Test

- Increases in global trade have driven growth and complexity in global payment flows, coupled with the ongoing adoption of automation by corporations and banks.
- These factors have contributed to the continuous evolution of bank/corporate connectivity, which is mutually beneficial.
- However, it is vital to remain mindful of the customer transition experience, which is key for a successful partnership.
- Banks need to adopt a truly consultative approach combining experience and expertise in identifying the latest connectivity solution that fits with clients' current and future business needs.

Guruprasad Gaonkar, Vice President, Regional Product Management (Channels), and **Hong Boon Tew**, Senior Vice President, Regional eDelivery, Global Payments and Cash Management, Asia Pacific, HSBC, Singapore

Evolving needs of various client segments has over the past few years resulted in banks accelerating the pace of development of new corporate connectivity options, while recent developments within the corporate connectivity space – ranging from on-device, on-premises and off-premises technology options, to evolving industry standards – have presented corporates with new choices, with varying degrees of automation leading to higher levels of sophistication.

While banks continue to develop new corporate connectivity options for new bank customers, it is also increasingly important to identify those among existing clients who can benefit from adopting the latest corporate connectivity solutions. In doing so, these clients can enjoy improved productivity, the convenience and efficiency of straight-through processing (STP), and cost efficiencies. However, banks face a variety of challenges if they are to deliver an excellent transition experience for their clients. This applies to both the immediate transition to a new connectivity solution as well as its subsequent use, putting customer experience to the test.

Globalisation, Cross-border Trade and the Financial Crisis

Corporate transaction flows with supply chain participants (customers, suppliers, etc.) have continued to expand. A major factor in changing both that growth and the nature of those flows has been globalisation. While this has been an established trend for some time, the events of 2007-2008 accelerated the process. Companies that outsourced their manufacturing or services to domestic companies as a means of lowering costs started exploring overseas options that might further reduce costs and allow them to benefit from industry best practice and to reach out to wider markets.

The overall effect has been a major expansion in both the size and geographical scope of supply chains. As a result, on the purchase side, corporates that once dealt with just a handful of domestic suppliers have had to radically revise their supplier management and purchase-to-pay models. Their manufacturing processes are now broken into more discrete components, with each component outsourced to a different supplier, many of which are on the other side of the globe. For more complex manufacturing processes, this supply chain fragmentation has occurred on an even greater scale. End customers purchase products from manufacturers that outsource each sub-assembly to other manufacturers, which in turn outsource sub-sub-assemblies to other manufacturers, and so on.

The net result of these changes is that physical supply chains have become far more integral, however complex and diverse over the past few years. This has obvious implications for the associated financial supply chains; for each physical transaction there is an associated financial transaction – i.e. the seller delivers the goods/service and the buyer sends a payment in return. Therefore, as the number of counterparties in the supply chain increases, so does the payment volume. A further consideration is that where a physical supply chain spans multiple countries the payment traffic also becomes more complex. A buyer purchasing from one domestic supplier makes one payment in the local currency. If the buyer then opts to use multiple manufacturers in different countries, the payment count increases, but issues such as foreign currency translation/hedging, local regulations and different clearing systems also arise.

The Corporate/Bank Relationship

The financial supply chain is obviously where banks are involved as the backbone for the physical supply chain, by providing transaction banking and other services, such as trade services. Therefore, as a corporation's supply chain extends and becomes more complex, banks need to be able to predict the implications and respond to these within the associated financial supply chain.

Bank-to-corporate relationships have also been altered by globalisation, such as in the growing need to support global trade regardless of the size of the business. A key factor here is the need for both corporations and banks to have modern technology that enables them to interact efficiently. One example of this has been the evolution of multi-bank platforms for the financial supply chain and trade services. This is helping deliver an architecture that customers can use to access multiple banks across their financial supply chain transactions via a single interface.

Another example is the evolution of standards such as ISO 20022 that facilitate information exchange between banks and corporates. These standards enable customers to use individual bank-specific connectivity channels while still being able to benefit from the standardised information exchange across multiple banks.

The traditional corporate/bank relationship is evolving into a virtual ecosystem with collaboration among banks, corporates, standardisation bodies, enterprise resource planning (ERP) and treasury solution vendors, and other third-party vendors. Banks play a pivotal role in this virtual ecosystem by incorporating common standards into the connectivity solutions that they provide. In addition, through their collaboration with vendors/service providers, banks are able to develop a better understanding of how corporates use ERP and treasury technology. This combined role as service provider and consultant for the financial supply chain is a win-win situation; corporates gain end-to-end value, while banks benefit in return from enhanced client relationships.

Technology, Standardisation and the Internet

In order to make the physical supply chain more efficient, corporations typically use ERP systems that incorporate highly sophisticated sourcing, production and distribution functionality. While ERP systems have historically been the preserve of large multinationals, in recent years ERP vendors have started to provide ERP technology suitable for even small and medium enterprises (SMEs).

Historically, bank proprietary standards and messaging have meant banks have been able to lock in clients. Standardisation and the Internet have led the need for banks to move beyond offering just transactional banking services to providing a more consultative relationship. The role of organisations such as SWIFT in supporting standards such as ISO 20022 has facilitated the standardised exchange of information between corporates and banks.

Internet technology has hugely facilitated the distribution of banking services and reduced costs. By removing the need for dedicated workstations loaded with proprietary banking software, clients can interact with their banking partners globally from any location with Internet connectivity. Furthermore, the low cost of such connectivity and the use of web technology means that it has become cost-effective for banks to interface in this manner with even their smallest SME clients.

The Right Mix of Bank Connectivity Solutions

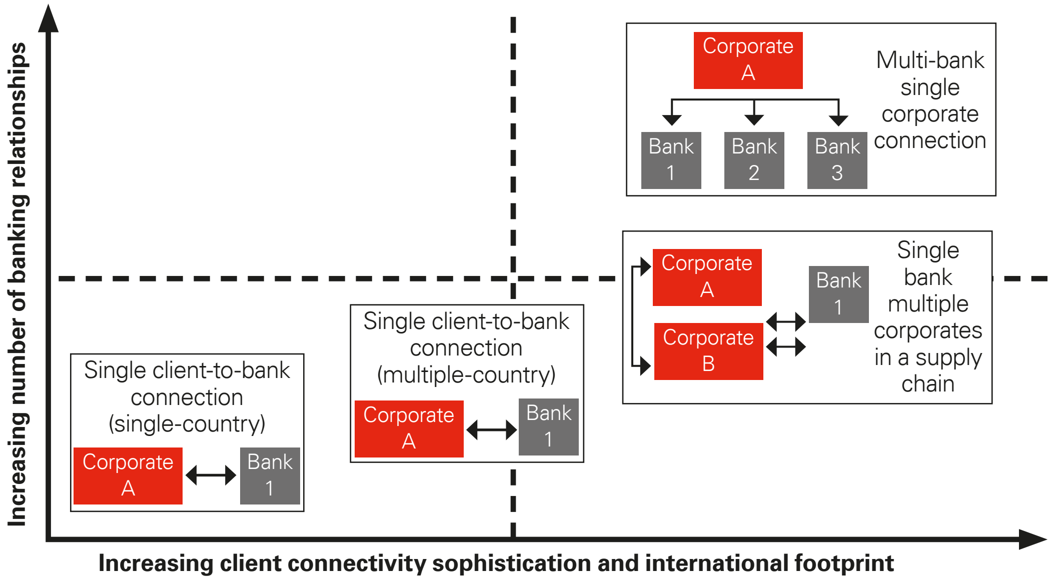
Changing business needs and technological advancements have led to various forms of bank connectivity solutions. Today's bank connectivity solutions can be broadly categorised as:

- on-device – Internet banking, mobile banking, etc.;
- on-premises – direct connectivity with the individual banks via point-to-point or host-to-host connection; and
- off-premises – indirect connectivity with single or multiple banks via organisations such as SWIFT, SWIFT Service Bureau or third-party service providers.

The choice of bank connectivity for corporates has been driven by business needs and growth. These primarily involve factors such as the number of banking relationships, banking services needs, connectivity sophistication and international footprint (see Figure 1).

In a new-to-bank scenario, the corporate client typically evaluates the various available bank connectivity solutions. By contrast, in the case of an existing corporate-bank relationship, the corporate tends to continue with the connectivity solution originally provided by the bank or one the bank may have subsequently provided as a reactive response to a client request.

Figure 1: Corporate/Bank Connectivity Options



Banks are uniquely positioned to adopt a proactive stance and use their client knowledge and experience of typical growth in client transaction volumes and geography to suggest the most appropriate solutions to clients in advance of actual need. A simple example of this would be noting rising client transaction volumes and suggesting that the client migrates from Internet banking manual file upload to fully automated host-to-host connectivity.

A consultative approach from the bank in giving existing clients timely advice on the most appropriate connectivity solutions will help these clients to improve productivity, by enhancing efficiency and cost effectiveness through achieving maximum STP levels. This approach will also allow the bank to position itself as a trusted adviser and partner, thereby adding value to the relationship.

Transition Management

Historically, the change implicit in a connectivity migration would be something that the corporate would just have to handle on its own. However, some banks realise that this is no longer acceptable; if they are a truly engaged banking partner, they will see it as part of their role that any necessary changes are made as straightforward as possible for the client. Simply suggesting a better solution is one thing; offering practical support and assistance in implementing it is quite another.

Based on its extensive experience in assisting other clients, a bank that is truly committed to this approach will be able to offer specific guidance and best practice around transition management in areas such as staff training and the least disruptive ways of implementing process changes. In addition, it will also be able to offer tools for facilitating specific technology tasks, such as converting paper instructions to an electronic format or pre-built bank/ERP interfaces.

A bank capable of delivering this creates a win-win situation for both the client and itself. The client benefits from a smooth and less costly transition to a better solution, while the bank benefits from a deeper customer relationship.

Client Knowledge

Where a bank and client have an established relationship, the bank has a unique opportunity to leverage this to provide the best possible consultancy regarding changes. This opportunity is based upon two facets of the relationship: analysis of the client's day-to-day transaction data, scope of banking services, geographical expansion/shift and regular client dialogue, particularly regarding any future plans.

Transaction traffic analysis can obviously identify situations where volumes are approaching the limits of the current client process. Traffic analysis can also reveal bottlenecks in existing processes, such as where existing payment authorisation limits are set too low so that numerous individual manual approvals are required.

Regular client dialogue that covers future corporate plans can have a major influence on the quality of the bank's recommendations because it allows for more effective roadmap planning. The bank trying to anticipate a client's solution needs two or five years hence, and co-ordinating that with the bank's own development pipeline, can do so far more effectively if it has insight into the client's future business plans. The crucial point is that the bank is able to recommend and deliver extensible solutions that can grow with the client for the long term, so that at no point is the client's business model constrained by its banking model and at all times internal change/disruption on the client side is kept to the irreducible minimum.

Conclusion

Banks will continue to develop impressive new products and solutions, but in isolation these have minimal value to clients if their adoption necessitates major disruption. Existing customers will benefit immensely from their bank positioning itself as an adviser and partner by identifying the latest connectivity solution that fits with the clients' current and future business needs. At a time when product differentiation among banks has narrowed, those that adopt a consultative approach combined with experience and expertise will stand out from their peers.

Connectivity in Asia: Easier Than You Think

Based on information obtained during HSBC's 2011 Asia Corporate Forum US road show, including inputs from **John K Dieker**, Vice President and Treasurer, Greif, Inc, **Michael King**, Global Client Director for HSBC, SWIFT, **Laurence Leyden**, Director, Transaction Banking, SAP EMEA, **Jack Spitzer**, Assistant Treasurer, Starwood Hotels & Resorts Worldwide, Inc, and **Marcus Treacher**, Global Head of Client Experience, Global Payments and Cash Management, HSBC

- The regulatory challenges for liquidity management in Asia have led corporations to assume that connectivity in Asia is similarly demanding.
- However, collaboration among standards bodies, technology vendors – especially enterprise resource planning vendors – and banks is enhancing corporate connectivity in the region.
- The benefits of consolidating bank connectivity are attractive, opening the door to better visibility, efficiency and strategy.
- There are certain pre-requisites to ensuring the success of such a project, including support from senior management and capabilities of banking partners.

Asia's multiple currencies, clearing systems, regulatory regimes and business practices mean that it is usually the last region that non-Asian corporations focus upon in their bank connectivity master plan. Yet recent collaboration among standards bodies, technology vendors – especially enterprise resource planning (ERP) vendors – and banks means that many of the local nuances in Asia are no longer obstacles to enhancing corporate connectivity in the region.

The importance of that enhanced connectivity cannot be overstated, as it can ultimately deliver a wide range of benefits including reduced costs and risk, plus enhanced liquidity utilisation and efficiency. This is particularly important at the corporate to bank interface level, where the quality of connectivity effectively determines the quality of service that the bank can provide.

Without top class connectivity much of the value the bank can add remains undelivered. This is particularly true of Asia, where high quality corporate-to-bank connectivity makes it far simpler to obtain real control of corporate finances across the region from any location, such as a regional or global treasury.

Recent Innovation

So what has changed that now makes improved connectivity possible? One important factor has been the high level of collaboration recently between technology vendors and banks. In the past, corporations were largely left to figure out the connection between their ERP systems and banks themselves. This was costly and also had to be redone whenever there was a change in banking relationships.

This situation has improved as ERP vendors such as SAP are now working closely with banks such as HSBC to construct plug-and-play connections between their technologies. As a result, corporations are now increasingly finding that pre-built interfaces are already available between major ERP vendors and banks, thus saving them considerable time and cost. ERP vendors have also been active in creating standard interfaces from their technology into SWIFT, which allows corporations a single point of access to multiple banks via the SWIFT network.

This change has not gone unnoticed in corporate treasuries. "When we started working on improving connectivity about five years ago, the connections were being made just through banks," says Jack Spitzer, Assistant Treasurer, Global Treasury Operations at Starwood Hotels. "The work being done together by entities such as SAP, SWIFT and HSBC means that things are now far more collaborative than they were in 2006, which makes the use of SWIFT as a connectivity mechanism a much better way to go."

> **One of the most interesting fruits of this collaboration has been the emergence of embedded SAP components that provide connectivity both to a bank's technology as well as SWIFT.**
> **Laurence Leyden, SAP**

"One of the most interesting fruits of this collaboration has been the emergence of embedded SAP components that provide connectivity both to a bank's technology as well as SWIFT," says Laurence Leyden, Director Core Banking, EMEA, SAP. "This gives an optimal mix of data transparency and STP [straight-through processing], but also potentially extends the capability of the infrastructure beyond payments to areas such as trade finance, liquidity management and hedging."

A ubiquitous and standardised infrastructure is obviously valuable, but to achieve the greatest benefits the traffic that runs across that infrastructure also needs to be in a standardised format. The growing acceptance of the ISO 20022 XML standard looks likely to tick this box. To date, it also appears to be avoiding the trap of custom implementations of a standard into which EDIFACT fell.

Opportunity

A primary reason that connectivity has become a popular discussion topic among treasurers and CFOs is that good connectivity unlocks value within the organisation. "The Internet provides a convenient analogy here," says Marcus Treacher, Global Head of Client Experience, Global Payments and Cash Management, HSBC. "Early electronic communication often consisted of independent islands with internal email systems, but with no interaction between islands. Then TCP/IP and the browser arrived –

and everything changed. In the financial space, the combination of ISO 20022 and SWIFT, together with the right mix of ERP and bank technology, offers a similar promise."

This is because it allows transparent access to all the data relating to corporates' financial activities that otherwise remains locked within their banks. Armed with this, the corporation can control its financial positions globally, in a standardised and efficient manner. A single pipe (SWIFT) dispenses with the need to communicate with each island (bank) in its own proprietary manner. It also has the merit of compelling banks to differentiate themselves by the service quality they can deliver – not by the technology into which they lock the client.

From an information perspective, this consolidated yet highly connected approach delivers value on both inbound and outbound transactions. Automated reconciliation of all receivables globally becomes a practical reality, while all payments become STP and have a complete audit trail from the point of confirmation backwards. That not only delivers efficiency, but provides an invaluable basis for more accurate cash flow forecasting. "Over time, the quality of data allows this forecasting to become more accurate even down to an individual customer level, as by using clean historical data it becomes relatively easy to predict when a specific customer is likely to pay," says Jack Spitzer. "The end result is that short-term cash flow needs can be forecast with confidence and the liquidity management process can be radically enhanced."

> **"... with its launch of 3SKey, SWIFT now also has a solution for the inconvenience of maintaining multiple security credentials.**
>
> **Michael King, SWIFT"**

On the technological side, streamlining connectivity in this manner substantially reduces costs. For a variety of reasons, corporations tend to find themselves dealing with a larger number of banks in Asia than in regions such as Europe and the US. If a corporation is, for example, connecting separately to five banks in Asia, then that requires five proprietary technologies that must be installed and maintained. Contrast this with the more homogeneous approach of using SWIFT where the implementations and maintenance are reduced to just one interface. For an organisation such as treasury, which often struggles to obtain IT resources, this is an important consideration.

"There is also the consideration that where multiple individual bank interfaces are used, the value chain of information flow is also effectively severed by each individual proprietary connection," says Michael King, Global Client Director, SWIFT. "Operational risks are also introduced because of the need to stop data, collect it, batch it and retransmit. Use of a common standard avoids these issues and with its launch of 3SKey, SWIFT now also has a solution for the inconvenience of maintaining multiple security credentials. 3SKey provides a method of digitally identifying an individual within a corporation to multiple banks, allowing the corporation to send sensitive banking information securely without having to maintain different tokens and encryption devices for different banks."

The potential value of this is clearly understood by some corporates and is motivating them to adopt SWIFT for this purpose. "We already have excellent visibility in terms of the core banks we are working with, such as HSBC," says John Dieker, VP and treasurer at Greif. "However, we don't have this visibility from our non-core banks and our objective is to use SWIFT to achieve this and bring in these other balances from around the world to obtain the global view we want."

Success Factors

While the benefits of consolidating bank connectivity may be attractive, there are one or two pre-requisites to ensuring success with such a project. One of the most obvious (and one that applies to every treasury technology project) is having resources and support from senior management. Fortunately, the business case for this sort of connectivity project is typically compelling. Nevertheless, those resources and support need to be consistent. "Maintaining focus is essential here," says John Dieker. "For example, if your CFO changes, then so might your corporation's priorities and focus."

> **Maintaining focus is essential here. For example, if your CFO changes, then so might your corporation's priorities and focus.**
>
> **John Dieker, Greif**

Another vital point is that companies need to deal with banks that have the right mindset and will therefore be able to maximise the flow and transparency of corporate transaction data. Unfortunately, there are still many banks that think purely in terms of lowest cost per payment and cannot grasp the wider corporate viewpoint that holistic information flow can be far more valuable. (This point was amply illustrated by a US treasurer attending one of the HSBC Asia Corporate Forums who remarked that having access to data that could reduce their receivables by two days would improve cash flow by USD25m per day.)

The obvious caveat here is that a corporation might invest in multibank SWIFT connectivity to its banks, only to find that some or all of those banks could not provide all the desired data for other reasons. Therefore there is a need to conduct due diligence on exactly what data each bank will be able to provide – in terms of both granularity and timeliness.

Another area where due diligence is required is the precise bank implementation of standards. "While at this stage, ISO 20022 appears unlikely to fragment in the same way as EDIFACT, there is still a need to be alert for any nuances in dialect," says Marcus Treacher. "Nevertheless the groundwork of agreeing with banks (and commercial counterparties) on the same terminology will definitely be repaid. Apart from anything else, it will ensure that matters are arranged to the corporation's convenience, not the bank's."

> **Nevertheless the groundwork of agreeing with banks (and commercial counterparties) on the same terminology will definitely be repaid ... it will ensure that matters are arranged to the corporation's convenience, not the bank's.**
>
> **Marcus Treacher, HSBC**

A convenience here is that because ISO 20022 uses XML, messages are intelligible to non-specialists. Due to the tags used, data elements are self descriptive and expressed in plain text. Therefore, unlike EDIFACT (which is, by contrast, cryptic), much of the discussion of dialect can be conducted at a business level, without requiring major IT or other specialist input.

Future Trends

Looking ahead, it seems apparent that the opportunity for corporates to obtain more information from their banking network will continue to expand, as will the ability to control individual payable/receivable functions far more thoroughly.

The channels by which that data is accessed and control is exerted are also likely to expand. Although also relevant globally, the use of mobile technology is particularly pertinent to Asia in view of the huge wireless infrastructure investment made across the region in recent years. As treasurers spend more time travelling in order to engage directly with business units, the ability to execute tasks that were historically tied to a physical workstation in the office increases in value. If a liquidity management decision can be securely taken and implemented in an airport lounge rather than being delayed until a return to the office, why not?

As high quality transaction data becomes more readily available, the possibilities expand. However, banks looking to develop products that can add value to this data need guidance – and that requires dialogue. Therefore, the trend of strategy sharing that is already present today among leading treasuries is likely to accelerate. If the treasury can give its banking partners a clear insight into its intended medium- and long-term strategy, then the banking tools and solutions they develop will be more relevant. As a result, the value derived from enhanced connectivity can be substantially increased.

Corporate Perspective on Asia Connectivity

Jack Spitzer, Assistant Treasurer, Global Treasury Operations at Starwood Hotels

We started our global bank connectivity initiative some five years ago and one striking change over the intervening years has been the increase in collaboration among banks, vendors and SWIFT – which is definitely simplifying matters from a corporate perspective.

Our connectivity experience in Asia Pacific was very similar to our experience in our domestic market in the US – there were certainly more similarities than differences. Having said that, for US corporations there is a need to be aware of the differences in file formats. Because the domestic US market doesn't typically use SWIFT, extending connectivity into Asia Pacific will necessitate becoming familiar with SWIFT MT file formats.

Another point to be aware of if you are a US corporation running a connectivity project in Asia Pacific is the impact of time differences. In our case, we were rolling out SAP globally and connecting each implementation to our primary international bank, HSBC, at the same time. One of the challenges we've noticed is that testing across time zones slows things up. Conducting and responding on local tests to a head office team on the other side of the world inevitably introduces lag, so it is advisable to factor this into project timelines.

Conclusion

Particularly for multi-banked corporations, the business case for bank connectivity via SWIFT looks increasingly compelling. The cost of SWIFT corporate connectivity compares favourably with the costs of maintaining multiple proprietary bank interfaces. But this is only a small part of a much larger picture; the benefits of bilateral single interface connectivity go far beyond this. The ease of assimilating data from multiple sources in a single format opens the door to far more accurate and timely forecasting and, by implication, enhanced liquidity management. Other areas also benefit; foreign exchange (FX) hedging becomes far more efficient as natural hedges become immediately – and reliably – apparent. Furthermore, SWIFT provides a channel for initiating and managing multiple other transaction types, such as trade finance.

Finally, there is the inducement that any treasury embarking on a consolidated connectivity project will be pushing at a door that is already swinging open. ERP vendors, major banks and SWIFT are continuing to collaborate closely on improving the corporate experience. As a result, the hurdles for such a project continue to diminish.

For more information about the Asia Corporate Forum, visit www.asiacorporateforum.com.

An Innovative Payments Approach at Swiss Re

- An increasing emphasis on transparency, efficiency and risk management led Swiss Re to review and revise its bank connectivity.
- The decision was made to replace proprietary technology with a single bank-independent connection utilising SWIFT.
- The new technology and connectivity infrastructure has brought a variety of benefits at a global and regional level.
- In Asia, there were specific challenges to overcome, but the regional bank appointed leverages Swiss Re's technology for internal payment processing and SWIFT connectivity, comprising a fully-fledged payment solution.

Damien Taets van Amerongen, Vice President, Information Technology, Swiss Re

Swiss Re is one of the world's largest re-insurers with over 10,000 employees and operations in 20 countries across over 200 entities. Although the company works with around five key banks, Swiss Re has over 2,000 accounts globally with around 50 banks. As a result of changing market conditions and a greater emphasis on transparency, efficiency and risk management within the business, Swiss Re made the decision to review and revise its bank connectivity.

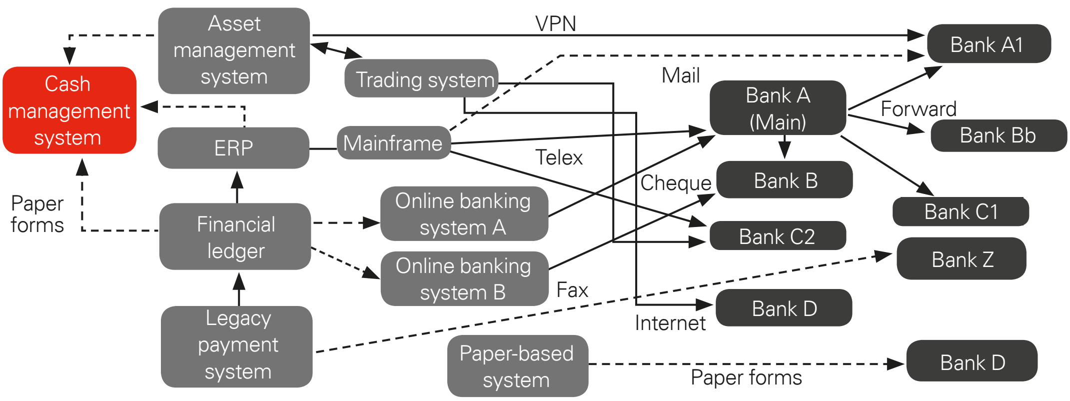
Changing Connectivity Requirements

After the tragedies of 9/11, market conditions changed significantly in the insurance industry, with an increase in trading activity, growing foreign exchange (FX) volatility and difficulties in maintaining return on equity. As well as taking steps to enhance efficiency, controls and risk management, Swiss Re recognised that its existing banking infrastructure had a series of shortcomings (see Figure 1). With a multi-channel infrastructure in place, it was cumbersome and time consuming to set up communications with each bank.

At that time, the company used a core bank proprietary workstation with a variety of other bank links including fax, telex and electronic banking systems. This led to data and process fragmentation with a lack of visibility, restricted information flow and delays in execution due to the variety of manual processes. Furthermore, by relying on a single bank, there were concerns about counterparty risk, which became particularly evident after the events of September 2008. In addition to concerns about bank connectivity, fragmentation of internal systems meant that cash management information was frequently delayed, disjointed and incomplete.

In Asia, there have been some specific challenges to overcome. For example, while it was originally Swiss Re's intention to continue with a multi-bank approach to payments, not all banks in Asia were able to support the company's preferred connectivity mechanism. Furthermore, while payment methods are

Figure 1: Legacy Bank Connectivity (simplified)



Source: Swiss Re

being harmonised in Europe through migration to the Single Euro Payments Area (SEPA) there are far more substantial differences between countries in Asia. As a result, Swiss Re recognised that it needed to partner with a regional core payments bank that supported SWIFT connectivity and supported in-country payment requirements in each country.

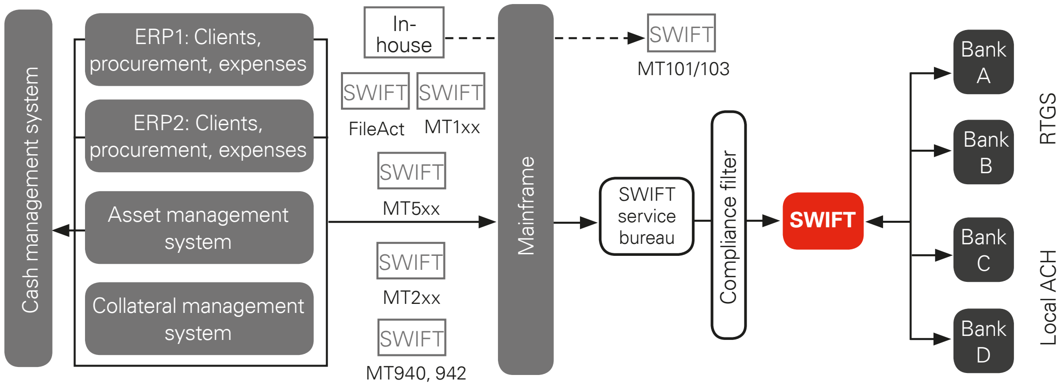
An Innovative Approach

To meet its global connectivity needs, Swiss Re made the decision in 2001 to rationalise its internal technology, concentrate its cash management activity, whilst still managing counterparty risk, and replace proprietary technology with a single bank-independent connection (see Figure 2). SWIFT was identified as the market standard for multi-bank connectivity, which was a pivotal element of the overall infrastructure to standardise and rationalise bank communications. Over the past 10 years, the company consolidated its in-house systems and implemented a treasury management system for treasury and cash management that was integrated with the two enterprise resource planning (ERP) installations, one of which covers Europe and Asia and the other for UK and the Americas.

Addressing Requirements in Asia

In Asia, a regional bank was appointed with which many Swiss Re branches already had a relationship, which helped to avoid internal roadblocks to making the transition. More significantly, the bank was unique in supporting an innovative arrangement that leverages Swiss Re's ERP-based technology both for internal payment processing and SWIFT connectivity, therefore comprising a fully-fledged payment solution. The bank accepts payment messages through SWIFT using FIN and then automatically formats and reroutes them to the relevant local clearing systems as well as to cheque printing facilities, which are still in use in some countries.

Figure 2: Revised Bank Communication



Source: Swiss Re

Despite the effectiveness of this solution, Swiss Re recognised that the company needed to manage its counterparty and concentration risk, so a mirrored arrangement was set up with a second regional bank that could be used if total payment volumes reached a certain limit or in case of the primary bank's inability to perform payment services. While the bank did not fully support the same automatic routing to local clearing systems, it was able to provide competitive pricing for local automated clearing house (ACH) payments. This mirrored approach, together with some remaining local banks, gives Swiss Re the flexibility and efficiency it requires to address both counterparty cash exposure and operational risk.

Operational and Strategic Benefits

The new technology and connectivity infrastructure has brought a variety of benefits to Swiss Re both at a global and regional level in Asia. With harmonised processes across the company, Swiss Re has been able to outsource finance operations to a payments shared service centre (SSC) that acts as a centre of competence. This has been a major advantage as previously, local business units maintained their own local payment systems, which were costly to maintain and compromised control objectives. Treasury was also able to decommission banks' proprietary electronic banking systems, eliminating the security risks associated with having to manage different security devices and user profiles across systems.

Straight-through processing (STP) rates have increased significantly with a scalable solution that can easily be extended to new countries in the future. For example, the infrastructure is currently being extended to India, without the need to set up new systems, and with the same quality of data, process control and visibility that exist in other countries. Use of standardised, well-controlled information and communications infrastructure is also an important factor in complying with Sarbanes-Oxley and other compliance requirements, particularly as all payments are automatically screened against the United States' Office of Foreign Assets Control (OFAC) and other embargo lists, further enhancing security and control. The systems infrastructure is versatile so other systems could be hooked in without the need to establish multiple interfaces or to set up new bank connectivity; this is particularly advantageous during mergers and acquisitions.

Transaction costs have been reduced substantially. Although the transmission cost through SWIFT may appear relatively high compared with using banks' proprietary software, the end-to-end cost is lower with greater control and transparency. Software and hardware costs have declined and resources can be redeployed to more value-added tasks. Swiss Re has achieved greater visibility over its cash on a global basis. Although this is most difficult in Asia, with a more regulated financial environment than in other regions, the company has better control over cash and is able to avoid increasing working capital.

The advantages are not only operational in nature. Risk management is a key priority and the project has contributed substantially to achieving the company's risk management objectives. By following a multi-bank approach counterparty and concentration risk have been successfully mitigated. This structure is also instrumental in managing operational risk as Swiss Re can switch to its back-up bank if its primary bank is unable to process transactions. The company now has greater negotiation capabilities with its banks, particularly to convince some of its local banks to support SWIFT Corporate Access.

Overcoming Challenges

A project of this scale and complexity, particularly in Asia, requires a combination of bottom-up and top-down approaches to implementation. For example, it was vital that senior management at both a group and local level were supportive of the project to help remove roadblocks. A pragmatic attitude has also been crucial. For example, although the chosen payments bank in Asia was not part of the global banking panel, its appointment was approved on the basis that it provided the technology and services that Swiss Re required. Swiss Re has developed significant expertise in SWIFT connectivity both globally and in Asia, which has been valuable in making the most of the opportunities that exist through SWIFT. Even so, when using non-standard FIN messages for local clearing systems, it has been important to leverage partner banks' expertise to ensure the right information and tags are used.

There have inevitably been some challenges to contend with. As an early adopter of SWIFT Corporate Access in Asia, Swiss Re faced issues from local banks, which did not necessarily understand why it was choosing to use FIN to access local clearing systems. In some cases, they expected the company to use FileAct and in others, they were generally unprepared. However, the solution that Swiss Re subsequently put in place has helped to avoid the potential impact of non-readiness for SWIFT amongst its local banks.

Next Steps

Now that payments have been automated and streamlined, the next step is to further consolidate internal reporting platforms and enhance cash forecasting abilities. Although the ideal scenario would be to implement a global ERP, there remain local processes that are required to support local regulatory and technological requirements. However, Swiss Re has implemented a scalable, flexible treasury and cash management infrastructure that is well-positioned to support its requirements as they evolve.

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Small Giants: International e-SMEs

Shayan Hazir, Head of Business Banking, Global Payments and Cash Management, Asia Pacific, HSBC, Hong Kong

- International e-SMEs are a new breed of small and medium enterprises (SMEs) that combine their inherent business agility with a global outlook and a strong grasp of technology.
- The emergence of e-SMEs has important implications for larger corporations, which might choose to view them as a threat or an opportunity, but can no longer afford to ignore them.
- Instead of simply competing with them, larger corporations can consider synergic relationships with international e-SMEs, which would maximise the skill sets of both.
- However, the inherent risks must be successfully managed for such partnerships to have a positive effect on the corporate balance sheet and achieve a competitive edge in the marketplace.

To many larger corporations, small and medium enterprises (SMEs) may not be of particular interest; possibly used as local suppliers, but not typically perceived as potential global business partners or competitors. With regard to a particular new type of SME, this assumption is no longer valid.

Within just the last decade, a new breed of SMEs has emerged. Unlike "traditional" SMEs, which are primarily local in their outlook and customer base, these new SMEs are global operators that make extensive use of e-commerce solutions. Their avid adoption of technology has also allowed them to maximise the business agility inherent in their relatively small size to support their atypical business models. This article examines the important implications this new breed of SME has for larger corporations.

The New International e-SMEs

These new SMEs combine the traditional agility of the SME with a global outlook and then leverage both with a strong grasp of technology. This combination can result in an organisation with phenomenal global growth potential that (depending upon whether they are a partner or competitor) can significantly assist or disrupt the business strategies of corporations many times their size. Their niche expertise is no longer constrained to the clichéd traditional "mom and pop" store, but can be deployed globally via the Internet with the aid of emerging technologies.

Advances in globalisation and technology have now effectively "geared up" the traditional attributes of these SMEs so that they now have the opportunity to punch far above their weight. That many have chosen to do so is evident from the number of household names today – such as PayPal, Skype and eBay – that have emerged within the past two decades. The end result is an organisation that is effectively an "international e-SME".

Technology ...

The evolution of the Internet over the past few years has given SMEs a degree of technological agility[1] that fits exceptionally well with their existing business/strategic agility. Business processes and infrastructure that were formerly a significant time and resource burden for SMEs are now both far more accessible and affordable; in effect, the frictional costs of doing business for SMEs have declined, while the scale of their potential markets and customers have increased.

When it comes to dealing with customers, suppliers and distribution, international e-SMEs now have access to services such as Ariba, Amazon, eBay and Alibaba.com, which can all deliver global reach at minimal cost. For payments, they can use services such as PayPal, Square and various escrow services, while for accounting and ancillary services there are Xero, Yodlee and assorted API tools. When it comes to communication they are positively spoilt for low-cost choice, with assorted IP-based forms of telephony and and short messaging service (SMS). Finally, they now even have access to enterprise resource planning (ERP) technology that was formerly the preserve of far larger organisations, in the form of products such as SAP Business One and Business ByDesign.

> **"... the frictional costs of doing business for SMEs have declined, while the scale of their potential markets and customers have increased."**

On the financial side, as banks become aware of the potential of international e-SMEs, some of them have responded with products that go well beyond their traditional quasi-retail domestic SME offerings. Banking platforms that deliver multicurrency accounts and transfers, together with hedging and trade applications are now becoming available. Banks have also started to release a series of more agile mobile products that are particularly well suited to international e-SMEs and their customers. Android banking applications, banking platforms tailored for mobile use and mobile expense tracking tools for the SME credit card market have all emerged in recent months.

... and How to Use It

A further consideration is that all these areas of technology and technology-based service are evolving rapidly. Again, this is a natural fit with the way that the new international e-SMEs do business; if a technology looks relevant and promising to the business, they can implement it within days. By contrast, at a large multinational it might take months for it to be ratified by the board and for trials and user acceptance testing to be completed.

1 *"The New Small" by Phil Simon, see www.thenewsmall.com.*

As a result, international e-SMEs can now offer products and services in areas that directly compete with the largest multinationals and where they were previously excluded because of the capital investment in technology required. At the same time, SMEs in general are increasingly eager to take advantage of this opportunity on an international basis; a past HSBC survey of small business confidence[2] revealed that 29% of SMEs already operated internationally and that 40% were planning to so within the next two years.

The Opportunity – or is it a Threat?

Considering the various attributes of the new wave of international e-SMEs, it is inadvisable for larger corporations to ignore them. Their impact both on established markets and in creating new markets is self evident. Lastminute.com went from SME to global brand phenomenally quickly and in doing so fundamentally changed the nature of the travel business. While it created a new market (online, last minute, "on a whim" travel purchases) it also took significant volume away from traditional "bricks and mortar" travel agencies and holiday companies. Therefore, the entrepreneurial talent and exponential growth possibilities of the international e-SME can make it either an opportunity – or a threat.

Compete?

The way in which larger corporations respond to this sort of disruptive newcomer varies considerably. Some will attempt to play catch up with a "me too" offering that attempts to replicate the SME's. While this may have some success, there are several obstacles. Apart from first mover advantage, international e-SMEs' facility with technology and their business agility gives them an evolutionary edge. By the time the corporation has rolled out its competing offering, the SME will almost certainly have redeveloped or refined its original offering multiple times, leaving the larger competitor continually attempting to reach a rapidly moving target.

> **"Apart from first mover advantage, international e-SMEs' facility with technology and their business agility gives them an evolutionary edge."**

Another obstacle is brand; in an e-commerce world, the domain name is the brand. The SME that sets the ball rolling and benefits through the viral marketing that comes from being a successful first mover in a new niche establishes the definitive brand for that niche. For a larger corporation to establish an e-brand of similar value may cost millions in conventional and online marketing, as well as potentially diminishing their own existing brand equity.

Acquire?

Other corporations will seek to acquire new breed SMEs that have compelling products and services. This can be either a defensive or creative step, or both. The defensive stance is self-explanatory; the corporation perceives the SME as a direct threat in itself or possibly as an even bigger threat if acquired

2 *"HSBC Global Small Business Confidence Monitor", HSBC Commercial Banking, January 2011.*

Connectivity

and successfully managed by a competitor. A few corporations will deliberately try to stifle an acquired SME to ensure that a direct threat has effectively been bought out of the market. The obvious downside to this strategy is that other corporations that acquire competing SMEs and manage them well will be an even bigger threat. There is also the consideration that SMEs are often founded by serial entrepreneurs, so once their non-compete period has expired they may start up another new competitor.
By contrast, those corporations that acquire an international e-SME and manage it creatively as an integral part of their businesses can "scale up" the SME's brand and turnover by providing the right supporting infrastructure. Sabre's acquisition of lastminute.com and AOL's purchase of bebo.com are examples of how this can work in practice.

Partner?

The alternative to competition or acquisition is partnership. This is a strategy that an increasing number of corporations are adopting (sometimes as a prelude to acquisition, sometimes not). Where an international e-SME has a particular and well-defined niche expertise, larger corporations may seek to leverage this rather than attempt to compete.

> **"Where an international e-SME has a particular and well-defined niche expertise, larger corporations may seek to leverage this rather than attempt to compete."**

A good example of this is the voiceover specialist voices.com. Rather than developing their own competing voiceover businesses, multinational advertising agencies around the world opt to use the services of this SME because they appreciate the choice, flexibility and pricing of its service. They can see little point in re-inventing what is already a highly efficient wheel.

While such partnerships between large corporations and international e-SMEs may be at arm's length in terms of ownership, some corporations take the opportunity for closer collaboration. On an informal basis they may provide resources otherwise inaccessible to the SME, such as specialised hardware, or more general business advice and assistance, or even working capital via a supply chain financing scheme. Apart from generally enhancing the supplier relationship, this approach may also facilitate the international e-SME's development of "niche within niche" products or services specifically tailored to the corporation.

The Reality

Relationships between larger corporations and international e-SMEs offer numerous synergic opportunities. The founders of this type of SME typically do so because they have an idea for which they have identified a niche market. Their product or service is their primary focus and also the area in which they can add the most value; more general business processes (such as accounts receivable) are not. In most cases SMEs regard such processes as something they must endure and would gladly be rid of.

Business Infrastructure

This is therefore a potential win-win for the right combination of corporation and international e-SME. The SME can offload the business processes it regards as non-core to the corporation, which has the expertise and economies of scale to manage them more efficiently. This is particularly important in view of the explosive business growth international e-SMEs can experience, which can ironically prove fatal to the business. It is not inconceivable for an international e-SME to go from needing to issue 100 monthly invoices to 5,000 in a matter of a few months. If that process collapses, then it can take the business with it.

In short, the availability of professional management and process frees up the SME's time, allowing it to focus on its core expertise because it no longer has to worry about the business infrastructure required to support future growth. (This need for scalable corporate infrastructure was one of the points raised by PayPal founder Max Levchin in the BBC's *"Start-Up Stories"*, a series of interviews with the founders of international e-SMEs.)[3]

Technology Infrastructure

Despite e-SMEs' reputation for technological prowess, professional technology infrastructure support can be another area where a larger corporation can add value. Many extremely successful entrepreneurs have remarked on how hit-and-miss their early approach to technology was. In a BBC *"Start-Up Stories"* interview, Bebo.com co-founder Xochi Birch remarked that despite her and husband Michael's background in computers and programming they were "complete amateurs" when it came to Internet start-ups. Michael recalls the beginning as "a comedy of errors, just trying things out".

> **"Despite e-SMEs' reputation for technological prowess, professional technology infrastructure support can be another area where a larger corporation can add value."**

Brent Hoberman cited a similar experience for himself and fellow lastminute.com co-founder Martha Lane-Fox. "I understand technology but we weren't technologists … so it cost more than we thought, it took longer than we thought and it didn't work very well," he said. "Basically the site was very buggy. Martha and I would wake up every morning and have to test the site. Was it still up? Was it still working? Could you actually transact?"

Market Knowledge

Alongside process and technology support is knowledge support. One of the biggest obstacles to globalisation for most SMEs is lack of knowledge. Matters such as taxation, regulation, local business practice or even just lack of business contacts can seem insuperable for SMEs looking to expand overseas. The time taken to research these properly will be hard to find alongside day-to-day business operations. Again, this is an area where a larger global corporation can contribute, as it will already have this knowledge. As a result, armed with this support, the SME is in the fortunate position of being able to expand globally far more quickly and with far less risk than if acting on its own.

3 *www.bbc.co.uk/news/business-11629784*

The Risks – and Managing Them

Corporations can benefit from the growth potential and niche expertise of international e-SMEs, while the SMEs can benefit from the professional management and infrastructure support of corporations. However, maximising these benefits to both parties involves dealing with a number of important risks.

From a corporation's perspective, the international e-SME's agility comes at a price – namely its dependence upon a very small number of personnel (perhaps only one). Post-acquisition, if any or all of these key personnel depart, much or, in some cases, all of the value of the acquisition is lost. While key person insurance offers some recourse, a more pro-active and forward looking method is to maximise knowledge transfer to others in the organisation. One method of accomplishing this is to keep acquired SMEs together in "incubator units", which also increases the probability of new creative ideas being generated. When the SME is an independent supplier rather than an acquisition, managing this situation is more difficult. In some cases it may be the catalyst for an acquisition or the direct recruitment of disaffected SME personnel as so-called "intrepreneurs" (individuals with entrepreneurial roles within existing organisations or corporate structures).

> **"One factor that can trigger the premature departure of key personnel from an acquired SME is their unwillingness to give up day-to-day control."**

One factor that can trigger the premature departure of key personnel from an acquired SME is their unwillingness to give up day-to-day control. This is something that needs to be addressed before the acquisition closes; who will be responsible for what post-acquisition and why? The chief executive officer (CEO) of the SME may not actually like conducting many of the business processes he or she is responsible for, but giving them up may still feel like loss of control. The onus is on the corporation to make it clear that it will be responsible for only non-core processes – the key creative processes will remain with the SME's personnel.

For many SMEs, a major concern post-acquisition is that their creative processes will be stifled by the corporate environment. Accustomed to a "just do it" working environment, the concept of obtaining multiple approvals and sign offs does not appeal. The key here is for the corporation to focus on removing all non-core processes from the SME's responsibility, but without substituting others. The innovative skill is the commodity that has been purchased; suffocating it makes little business sense and increases the risk of key personnel departing.

Conclusion

For corporations looking for growth opportunities, the new breed of international e-SME has huge potential. Maximising the synergies between the skill sets of the two types of organisation may not be trivial, but if successfully accomplished, it can have a swift and positive effect on even a large corporate balance sheet.

Fostering the SME's creative processes while taking control of its administrative processes is the key. This may be counter-intuitive to the normal corporate business model, but those corporations that can accomplish this change in mindset will have established a competitive edge over their peers.

Ctrip: Accommodating Growth

Headquartered in Shanghai, online international travel and tour agent Ctrip.com deals with a large number of vendors (hotels and airlines) across Asia. The company is using the Internet as a conduit to expand business internationally both in terms of its customers and suppliers.

In common with many international e-SMEs, the company was experiencing exceptional growth. It was already successfully using HSBC*net* to make supplier payments by online manual input, but its rapidly increasing transaction volumes indicated that automating this process was advisable. Ctrip.com therefore chose to implement an automated host-to-host bank connection in the form of HSBC Connect. As HSBC Connect has the capability to adjust to any ERP solution, implementation was straightforward.

The new solution enables the company to transfer files containing multiple payments in various currencies in standardised ISO 20022 XML format from its ERP system to HSBC automatically. This revised workflow has delivered a number of important benefits for Ctrip.com, including:

- reduced manual operations;
- lower payment costs;
- greater operational efficiency in its Shanghai headquarters; and
- facilitation of centralisation and control at its financial base in Hong Kong.

The company's adoption of HSBC Connect also confers a strong degree of future-proofing, as the connection is extremely scalable up to the volumes usually associated with the largest multinationals, which is valuable for a rapidly growing international e-SME such as Ctrip.com. Finally, it is interesting to observe how Ctrip.com is representative of many international e-SMEs in that it has adopted a solution typically used by much larger corporations – it is in fact the first-ever HSBC SME customer to implement HSBC Connect.

Customer-focused Business Intelligence in Banking

- With customer behaviour becoming more complex, an in-depth understanding of business drivers is critical to formulate sound strategies and enable quick execution.
- Business intelligence (BI) is now a key focus area for corporates; customer-focused BI will be the next competitive differentiator in defining and building corporate relationships.
- Elements of a customer-focused BI model include a suitable BI platform, a delivery channel and a detailed understanding of customers' business processes.
- The rewards can be significant, including enhanced customer relationships, lifecycle engagement and improved revenues.

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As companies expand internationally, having visibility over business activities, vendor and supplier intelligence and real-time market developments becomes increasingly challenging. In the corporate space, much has been written about management information (MI) business impact, best practices, systems and technology along with the shift to analytics and business intelligence (BI) as the next step in MI evolution. Much of the focus, however, has been from an internal perspective, on how corporates can use data to grow their customer base and market share.

There is a clear difference between MI and BI. MI, in the context of this article, refers to a system or database that facilitates easy aggregation of different types of information (i.e. data) across the organisation, which can be used to provide routine reports required at different levels of management, such as sales performance or staffing. BI, on the other hand, is leveraging the information available to improve business performance by obtaining the maximum understanding of the business environment – external and internal – and scenarios that can advance or impact progress towards a strategic goal or objective.

The Need for Customer-focused Business Intelligence

A customer-focused BI platform can deliver greater benefits to corporates, while reducing the time spent on information gathering and integration. The core use of BI is as a strategic decision-making tool linked to likely future scenarios that may play out based on market forces exerted by customers, competitors, vendors and suppliers. MI, however, looks at historical information to provide an "as-is" snapshot and possible historical trends, making it a subset of BI. As the marketplace becomes uncertain, and customer behaviour becomes more complex, an in-depth understanding of the drivers affecting the business is critical to formulate sound strategies and enable quick execution, which is why BI is now the key focus area for corporates.

To achieve and effectively translate information into BI, a critical requirement is ensuring information flows from all the companies doing business with the corporate in the external operating environment. A few examples to illustrate the criticality of this information flow from the external operating environment are:

- optimisation of inventory costs and just-in-time production being directly impacted by knowledge of daily production levels achieved by major suppliers of the corporate;
- impact on time to market and pricing on account of the average time taken by the corporate's distributors to ship products to different locations; and
- production scheduling optimisation linked to the number of orders being booked by sales channel partners of the corporate.

What clearly stands out across these few examples is that any BI needed to assess the impact of business variables will be dependent on data flowing in from all the other companies doing business with the corporate.

By developing more customer-focused BI, corporates will enable their customers to more effectively weigh information about the external operating environment and integrate that information with the internal knowledge of the organisation. This will facilitate the identification of dynamically changing market variables to help formulate a range of scenarios predicting probable future outcomes to be able to discern potential opportunities, and barriers against achieving them.

Developing a Customer-focused BI Platform

To develop a customer-focused BI platform successfully, the main considerations are:

- Commitment: Appreciation by the senior management of the competitive differentiation opportunity and willingness to invest in building such a platform – this will require a directional change towards leveraging BI as part of the on-going customer engagement proposition; historically, investment in BI has been made from a customer relationship management (CRM) perspective or through focus on automation and cost reduction.

- Understanding: A sound understanding of the customer lifecycle and needs, since customer-focused BI will translate into different requirements based on the lifecycle of a company's customers. Specific propositions around leveraging customer-focused BI for new customer acquisition, retention, growth and service of existing customers will need to be considered, and customer advisory boards and pilots are useful tools in this context.

- Engagement: Engagement with stakeholders, both internal and external, will need to be outlined to ensure a clear long-term roadmap with defined principles around governance, technology, minimisation of information duplication, revenue return measurement guidelines, deployment plans etc., similar to any regular product development lifecycle.

- Resources: Appropriate time and resources should be made available for gathering and scoping customer requirements in order to deliver a tool that has the right amount of data required by the customer, yet maintains information confidentiality and is intuitive enough to make it self-service capable for customers in the longer term. The data available must be structured around a suitable framework easily understood by customers and be easily deliverable.

Figure 1: Customer-focused Business Intelligence (BI) Model

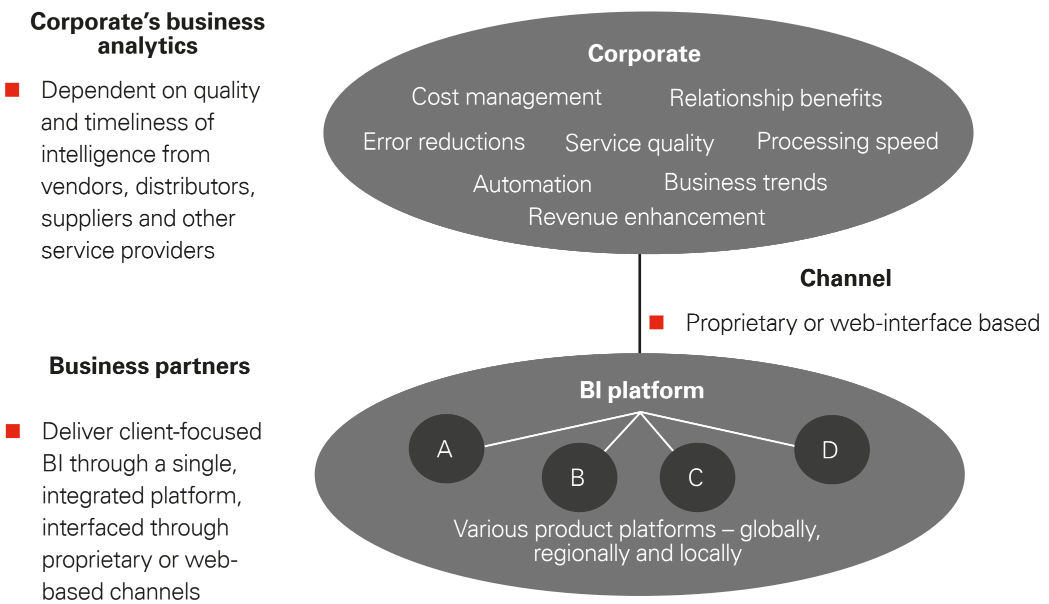


Figure 1 illustrates the overall customer-focused BI model, whose key elements are:

- the development of a suitable BI platform that effectively draws information from a range of diverse (and typically independent) product platforms globally, regionally and locally to provide a single integrated view – suitable technology exists to make this possible, which can be sourced from a range of vendors in engagement with internal technology teams;
- the enablement of a proprietary electronic channel or an appropriate web-based interface to deliver this information to the corporate's MI platform or, alternatively, providing the appropriate online tools to facilitate the corporate in building analytics to meet its own BI requirements; and
- a detailed understanding of customers' business processes – it is critical that the company engage its customers to obtain an in-depth understanding of the customers' key strategic drivers and business processes impacting them, to ensure that an appropriate BI framework can be delivered that has been customised for the customers.

BI in Action

The examples below demonstrate the effectiveness of customer-focused BI in actual business situations, using a platform developed by the corporate's banking partner.

Improved Information Flow and Visibility

A large multinational corporation (MNC) with more than 200 accounts across 19 countries in Asia needed to review its account management structure and to identify opportunities for greater investment returns and lower borrowing costs. The MNC requested a customised report that would allow it to see the fund movements in its accounts for the past 90 days on a daily basis. Previously, this ad hoc task would have been daunting, as it would require participation from various countries, with timing and quality of the output depending on resource availability. However, the pilot regional BI platform enabled the generation of a report through a front-end tool at the click of a button. This allowed both the MNC and bank to discuss opportunities for enhancement further and translated into financial benefits for both parties.

Enhanced Service Response

A consistent customer experience is one of the top priorities for MNCs, as this leads to customer loyalty and enhanced wallet share, but it is difficult to achieve if service managers use different reports and manual methods to monitor customer activity and reactively engage customers on service issues. A robust alert mechanism made possible with the BI platform would allow service teams of the MNC and its customers to simultaneously identify and enable opportunities for improvement. Such a proactive approach would translate into cost savings for customers and improve their relationships with the MNC.

Handling the shared service centre (SSC) payment processing of an MNC is challenging as it involves voluminous transactions and different payment methods across different countries. The creation of a customised BI service report established a single point of contact with the MNC's SSCs, measuring performance on a regular basis against service level agreements (SLAs), query response times, error types and reasons, along with facilitating a discussion on internal or external causes of the errors and how this could be addressed. Trends over a few months demonstrated significant error reductions and enabled the MNC to engage effectively with its vendors and suppliers to enhance process efficiency.

Customised Solutions

In the current competitive environment, customers' demands for customised solutions – especially in the case of information – are increasing, and service providers are expected to address these requirements. The trending and data modelling capabilities of a BI platform support effective structuring of solutions for a set of customers with common behaviour and transaction patterns, providing both packaged solutions and industry-specific offerings.

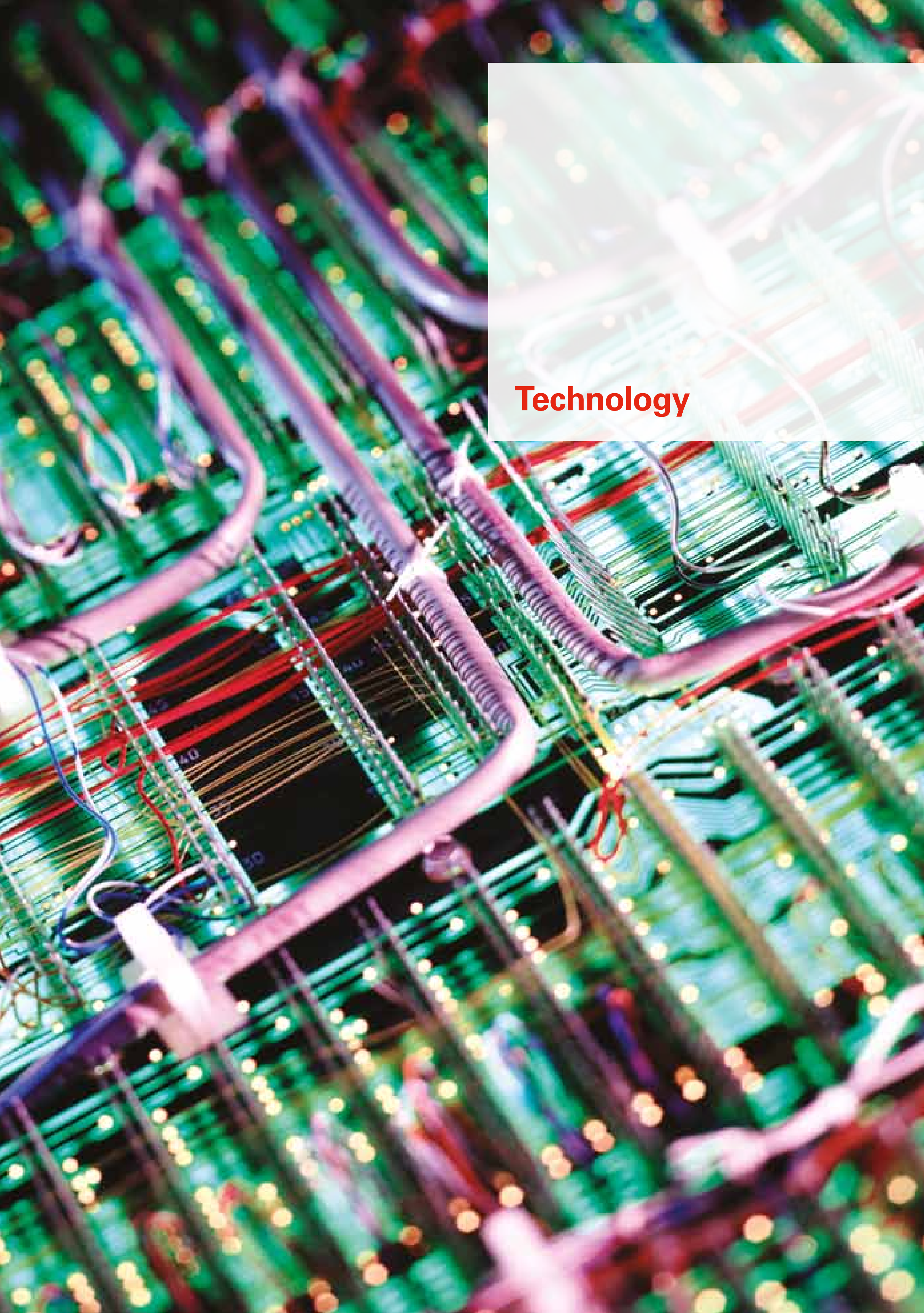
A major pharmaceutical company was undergoing a review of its accounts receivable (A/R) processes across different countries in order to reduce its day sales outstanding (DSO). The company's sales manager was able to develop a solution in engagement with customers that provided the customers with customised BI on collection services, covering both in-country practices and an integrated regional view. Critical to delivering this was the ability of the bank's BI platform to pull together these information tables across multiple internal systems.

These are but a few examples of the significant impact of customer-focused BI. Incremental improvements of 5% or more in existing revenue are a definite possibility as a base case through successful deployment and commercialisation of customer-focused BI.

Conclusion

Customer-focused BI will be the next competitive differentiator in defining and building corporate relationships in the business ecosystem. Enabling this will require a strategic view as well as investment by corporates over the longer term. The rewards will be significant in terms of enhancing customer relationships through a stronger value proposition, improved lifecycle engagement, and financially, through improved revenues for both companies and their customers.

Technology



Treasury Management Systems Transition to the Cloud

- Using spreadsheets is cost effective, but at the expense of efficiency, prompting treasurers to transition to customised treasury management systems (TMSs).
- For companies that want a TMS without a significant impact on IT expenditure, moving to the cloud is an optimal option.
- There are several business drivers behind moving to cloud including cost advantages, flexibility and the ability to continue using legacy applications.
- As with any migration, the associated risks need to be assessed, such as security, reputational, continuity, interoperability and portability risks.

Sam Felix Pradeep Kumar, Senior Consultant, Financial Services and Insurance Practice, and **Nripen Aniyan Mathew,** Senior Associate Consultant, Financial Services and Insurance Practice, Infosys Limited

Companies spend up to 75% of their IT budgets just on maintaining and running existing systems and infrastructure, according to a survey conducted by Infosys. In addition, experts estimate the annual cost of owning/managing software applications can be as much as four times the cost of initial purchase. Using spreadsheets has been cost effective but at the expense of efficiency, prompting treasurers to look for customised treasury management systems (TMSs). But corporates have had to stretch their IT budgets to bring those solutions onboard. For companies that want TMSs in place without a significant impact on IT expenditure, moving to the cloud would be an optimal option. This article explores the business drivers behind moving to the cloud, and details the risks and ways of mitigating them.

Keeping Pace With Technology

Technological advances have transformed the way corporate treasurers operate. Treasury management has seen a multitude of changes in the recent past, including a quiet move towards automated TMSs from human-driven Excel spreadsheets or generic enterprise resource planning (ERP) systems. Spreadsheets often lead to inaccurate cash forecasting due to the risk of data entry errors, since the process is manual. Still, spreadsheets continue to be a competitor to automated TMSs, since moving away from Excel worksheets often involves costs and can seem intimidating. ERP systems for treasury services are yet another option, but the associated cost is high and also they struggle in dealing with complex treasury functions.

Reeling from the recent global financial crisis, corporates have felt the need for automated systems that would help them improve operational efficiency, and they understand that the cost of manual errors on a spreadsheet-based system outweighs the cost of implementing an automated system. There is an increased affinity towards automated TMSs, but the cost of implementing such a system cannot be ignored. From setting up the infrastructure to selecting a vendor for implementation, it is an arduous task. One alternative for corporates is to look for TMSs available on a subscription basis via the cloud.

The US government's National Institute of Standards and Technology (NIST) defines cloud computing as "a model for enabling ubiquitous, convenient, on-demand network access to a shared pool of configurable computing resources (e.g. networks, servers, storage, applications, and services) that can be rapidly provisioned and released with minimal management effort or service provider interaction".[1]

Cloud computing is currently the "magic phrase" among IT decision-makers in all areas, and TMS implementation is no exception. The cloud computing model provides access to scalable and elastic IT-enabled capabilities that can be released on demand, giving rise to a new breed of cloud-based TMSs. Moving to the cloud would provide treasurers with access to such systems on a pay-per-use basis, thereby providing significant cost advantages. While cloud-based treasury services are relatively new and often limited to allowing users to see reports and analyse data, they are expected to become more sophisticated as the market develops.

Business Drivers for Cloud

Legacy Applications

Corporates currently use in-house applications, including automated TMSs, to manage their treasury operations. These include heterogeneous applications to manage cash positions, foreign exchange (FX), deal initialisation and finalisation, which are built on various technologies and platforms. Revamping the system and building from scratch would not be feasible for corporates already working towards cost optimisation. Moving to the cloud would help these corporates better manage their treasury operations, as they would seldom need to think about application upgrades and would be able to put the latest technology to use.

Cost Reduction

Setting up a treasury management system could take anywhere between six and 18 months[2] and the need to spend continuous effort on maintenance should not be ignored. Additionally, corporates might need to pay large upfront licensing costs and annual support costs. The cloud helps corporates gain the same functionalities at a fraction of the cost. Cost reduction was quoted as the top reason that drives cloud computing, according to research conducted by the 1105 Government Information Group (see Figure 1).

Flexibility

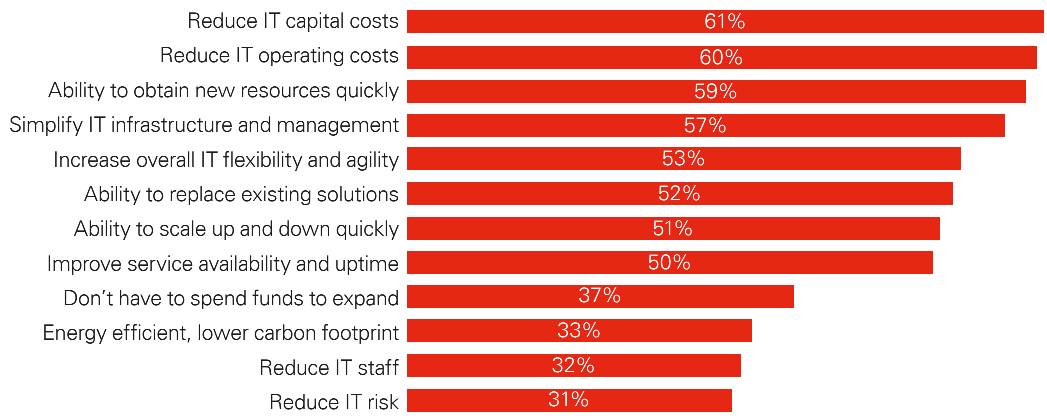
One of the defining attributes of the cloud is its flexibility. The scope of treasury management is vast and it continues to grow, no longer being limited to cash management and forecasting. A licensed application with certain features to cater to the needs of a corporate today might not be good enough to cater to its needs tomorrow. Upgrading the application or adding features progressively might create compatibility issues. With the cloud, corporates would be able to access necessary modules on a subscription basis, as and when needed. The system would also be scalable to support the growth of the company, since

1 *Mell, Peter and Grance, Timothy. "Draft: A NIST Definition of Cloud Computing" Special Publication, National Institute of Standards and Technology. http://csrc.nist.gov/publications/drafts/800-145/Draft-SP-800-145_cloud-definition.pdf.*

2 *www.treasuryworkstationreview.com/2010/03/selecting-treasury-workstation.html.*

with a cloud-based TMS, capabilities can be rapidly and elastically provisioned for, allowing the company to scale up or scale down quickly.

Figure 1: What Drives Cloud Computing



Source: 1105 Government Information Group

Transition Challenges and Risks

Moving to the cloud does not bring in new risk elements, but it is associated with a change in the nature of existing risk elements. Transitioning to the cloud involves a lack of control over where internal data and applications reside. It also brings in the risk of system failure and risks associated with unauthorised access to data and lack of control over privacy (see Figure 2).

Reputational Risk

Reputational risk, often called the "risk of risks", remains significant considering the fact that any harm to client or proprietary data could negatively impact the reputation of the corporate. Corporate treasury often manages the organisation-wide liquidity position and it relies on offshore units for a regular and reliable forecasting of the cash positions. It is also responsible for managing cross-border payment flows and multi-currency inter-company payments. Moreover, any data or information that flows in or out of the treasury system is sensitive, as it discloses where the company stands with respect to its cash/liquidity/FX position.

Security Risk

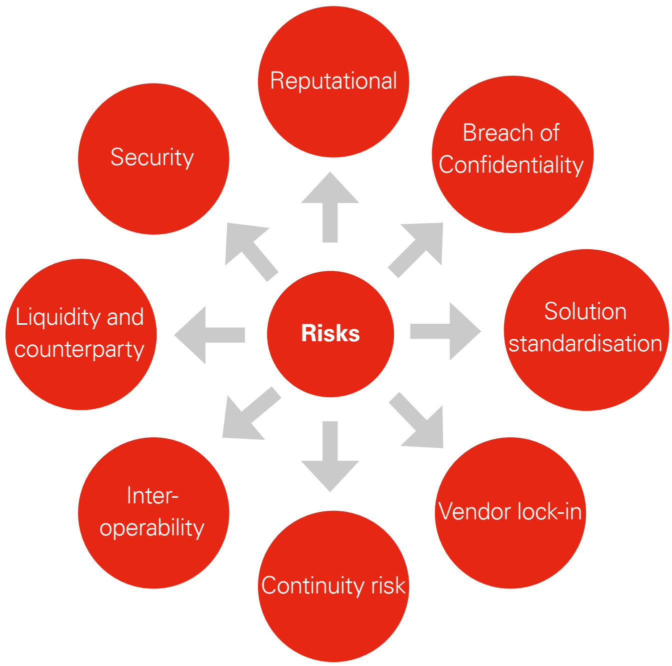
Security is the most important concern for organisations moving to the cloud. Security risks are more pronounced if treasury services are moved to a public cloud, which increases the number of people with access to the organisation's resources, including the various Excel-based models used for analytics, pricing of products and risk management tools that are proprietary assets. Other challenges include assessing the security aspects of the cloud provider and that of the software/systems.

The major source of security risk comes from the defining characteristics of the cloud, namely multi-tenancy and resource sharing. Multi-tenancy implies that users will be accessing a single instance of the hosted application. A malicious "tenant" of that cloud provider could access and attack the information of other firms hosted on the same cloud. Exposure of client information to third-party vendors poses significant security risks to the corporate. Any application hosted in the cloud requires data and information transmission between the systems to traverse the Internet, thereby making the systems susceptible to security risks inherent to the Internet.

Breach of Confidentiality

Treasury systems are built with the capability of aggregating data from various sources and presenting it in usable data formats. A breach of confidentiality involving data in the cloud could compromise sensitive and confidential information. Data that has been tampered with can present a false picture of the cash or liquidity position at any point in time. Minor glitches or errors in treasury could have a massive impact on the financial well-being of the corporate as a whole.

Figure 2: Risks Associated With Transitioning to Cloud



Source: Infosys Limited

Solution Standardisation

Treasury operations have historically been crucial for corporates. Hosting of treasury operations on the cloud adds another dimension to the risk already present in the system. The risks and challenges vary from one function to another, depending on whether it is a front office operation or a back-end regulatory function. Risk also varies based on the criticality of the data handled by the functions. While functions like accounting, settlement and real-time position tracking are common across the board, functions like

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risk management, simulations, value at risk (VaR) calculations or analytics can be specific to each firm's position. Hence, as far as such operations are concerned, standardisation of solutions will be a challenge.

Vendor Lock-in

The risk of locking in to a specific vendor for treasury solutions applies to cloud services as well. Vendor lock-in would result in the firm being tied to one particular vendor, which might prove detrimental if the services of the vendor are not satisfactory, or if the vendor is not meeting the desired performance that was guaranteed.

Continuity Risk

Another major risk in hosting IT platforms outside a firm is the risk of power outages. Though not very common, the impact that this could have on treasury operations is threatening –especially for functions like accounting, real-time position tracking and trading modules – power outages even for a few minutes could affect the financial health of the firm. This is even more critical for front-end operations involving trading of highly volatile instruments like equity options, exchange rate based instruments or futures.

Liquidity and Counterparty Risk

Corporates are increasingly reliant on TMSs to help them improve FX management. Using a TMS's ability to access accurate data, quantify currency exposures and provide accurate risk analysis, a corporate can effectively hedge its cash positions. In order to accomplish this, there needs to be a continuous monitoring of market movements, identification of FX cash flow/exposures and identification of best available price in the market. This information needs to be available in real time – any delay would put the corporate under severe liquidity and counterparty risk.

Interoperability

A typical treasury solution will have linkages with external systems for getting feeds from the equity, derivative and FX markets. Thus in order to host the front office part of the operations on the cloud, the feasibility of integrating the applications hosted on the cloud with other cloud operators/servers and applications has to be looked into.

Mitigating the Risks

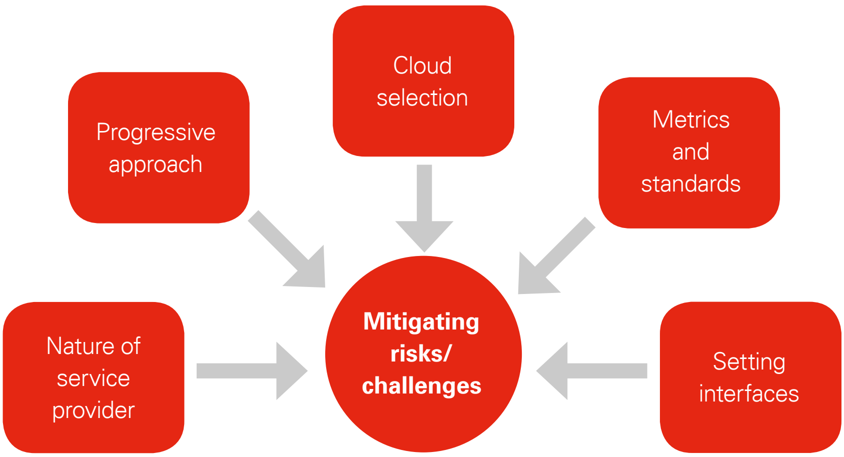
Progressive Approach

Corporates could adopt a "progressive" approach, rather than making a complete transition to the cloud all at once. They should look for cloud providers that provide individual modules/functions on a subscription basis and start with areas that are less risky before progressively expanding to other sensitive modules. This would include basic email and reporting capabilities and basic treasury functions such as cash management/forecasting, treasury transaction management, and account consolidation from multiple accounts/services. Such a scaled approach would help the firm assess the suitability of the cloud and its own readiness. Another approach would be to select the core modules to meet basic requirements and then get add-ons as required.

Cloud Selection

Owing to the critical nature of the data and operations, hosting treasury services on a public cloud is not a suitable option. By opting for either private or hybrid cloud services, firms can retain the critical operations and data within their control and need risk only general, less critical ones on a public cloud, if opting for a hybrid cloud. A hybrid cloud helps organisations to quickly deploy a treasury management solution and companies can benefit from upfront cost reduction, ease in implementing these services, reduced IT resource requirements and automatic service upgrades. Private hosting, which offers organisations a cost-effective IT solution that is agile, scalable and, to a greater extent, secure, is

Figure 3: Mitigating the Risks and Challenges of Transitioning to the Cloud



Source: Infosys Limited

required for some of the vital treasury management functions. Though this is more expensive than the community cloud option, organisations can benefit from higher levels of availability, resiliency and scalability, along with added security, control and auditing abilities.

Service Level Agreements

To ensure quality of the cloud service, firms should have service level agreements (SLAs) with their service providers to protect themselves against outages or substandard performance. It is also desirable to have an exit strategy in order to ensure a smooth transition from one vendor to another. The contract should contain the necessary clauses to ensure that the firm knows or has the ability to find out the geographical location of storage. Any controls with respect to country location restrictions should be defined and enforced. Also, the storage retirement process of the provider should be understood, since data resides in a multi-tenant environment and any data destruction process can be extremely difficult. It is advisable to get the SLA assessed by a neutral third party.

Nature of Service Provider

When selecting a cloud service provider, due consideration needs to be given to factors such as system features offered, number of years in service, number of clients, necessary certifications/audit compliance and SLAs that would help the corporate to mitigate most of the risks. Corporates should aim to work with SAS-70 compliant providers, as this will provide a point of reference for auditors. It is also important to understand the scope of SAS-70 audits and verify if all requirements can be met.

Metrics and Standards

A set of well-defined metrics and standards for measuring performance and effectiveness of moving into the cloud-based treasury should be in place prior to the move. Corporates should understand and document their current metrics and visualise how they will change – such a planned exercise would help to validate the decision of moving into the cloud and allow the corporate to work on improvement areas, if any.

Setting Interfaces

Corporates should evaluate the ease of setting up interfaces with other systems when looking for cloud-based treasury services. Treasury functions involve interfacing with bank systems, trading portals and FX portals, and the need increases with the passage of time. If the interface set-up is complex or if the system does not support external interfaces, due consideration should be given.

Conclusion

Transitioning to the cloud does not eliminate risks or collapses; however, it provides the inherent advantage of a TMS in helping treasurers to navigate uncertainty or risks with increased confidence and effectiveness. It provides a way for corporates to realise significant cost savings when proper study and planning precedes implementation. Despite the buzz, the cloud is not a suitable solution for everyone or for all scenarios. Individual organisations should study the environment and risks before they make the decision to transition to the cloud.

Flexible and Future-proof: A Modular Approach to ERP/Bank Integration

- Interfacing an enterprise resource planning (ERP) system to a bank is a significant task, with a focus on risk mitigation, security and contingency measures, while minimising systems infrastructure changes.
- Anything that future-proofs such an implementation by providing flexibility adds value.
- As a corporation grows or changes, ERP system changes can be accommodated by contained adjustment to individual implementation components.
- With a modular approach, flexibility can be attained without requiring wholesale change and disruption.

Vengadasalam Venkatachalam, Regional Head of Client Integration and eDelivery, Asia Pacific, Global Payments and Cash Management, HSBC

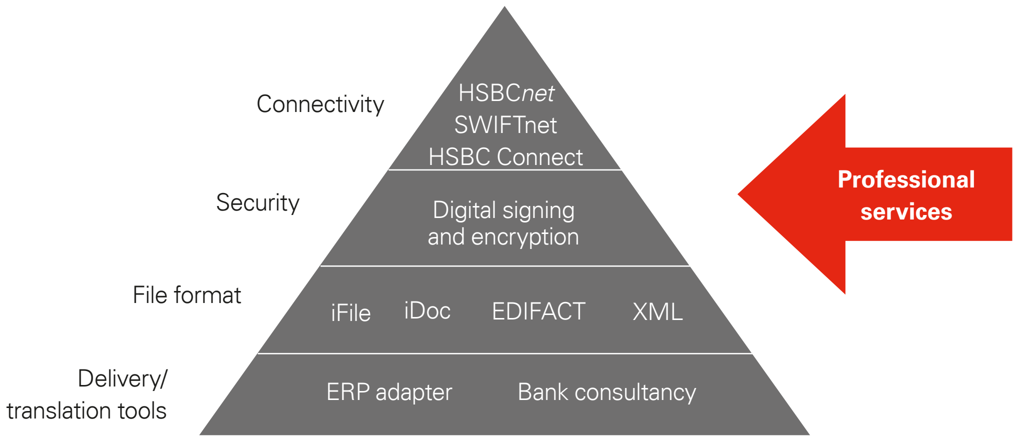
Corporations are dynamic organisations that change over time; sales and transaction volumes fluctuate, new business units are started or acquired, and new markets are entered. All these changes have implications not only for internal financial processes, but also for the interface between a corporation's enterprise resource planning (ERP) system and its banking partners. This bank interface has the potential to be an obstacle to corporate development; if the interface has to be substantially reengineered every time the corporation changes in any way, then the disruption and costs inherent in that become a growth barrier. Therefore, the ERP/bank interface ideally needs to be engineered so that individual elements of the interface (see Figure 1) are independent of each other; changes can be made within one element without affecting any of the others.

Key Objectives

Any ERP-to-bank implementation will have a number of primary objectives. While the relative importance of these objectives will vary from corporate to corporate, the overall list will probably be very similar and the chances of fulfilling it will depend heavily upon the need for modular flexibility. Minimising operational and technical risks is obviously essential on a day-to-day basis to prevent issues such as failed payments arising and the corollary to this is that the bank/corporate interface should guarantee secure automated end-to-end file transfer. However, despite any risk mitigation and security measures, it is also desirable for contingency measures to be an integral part of the design. For example, if there is a corporate-to-bank network failure, then contingency components such as SWIFTNet or browser-based secured file upload should be available and tested to ensure business continuity.

The need to minimise systems infrastructure changes is self evident in that it will also facilitate the scaling of the solution to accommodate not only increased volume but also a broader range of instruments and a near real-time view of such instruments, ranging from cash to trade, foreign exchange (FX) or derivatives positions.

Figure 1: Layers of a Modular ERP/Bank Integration Architecture



Source: HSBC

Integration Considerations

As seen in Figure 1, these objectives translate into a need for modular components in four key areas:

- Delivery/translation tools: At the base of the pyramid (at the start of the corporate-to-bank transaction flow) are the delivery and translation tools. These will vary according to circumstances, but could include tools to generate (and, if necessary, also translate any internal/proprietary formats into) the standardised file formats in the next pyramid tier. Or they may alternatively consist of bank professional services consultancy.
- File format: The delivery/translation tools may output files in industry standard formats such as XML/EDIFACT, or possibly a popular ERP format such as SAP iDoc, or even a bank-specific format such as HSBC iFile.
- Security: The next tier in the pyramid is security, which will probably include a variety of measures. These can range across communication layer security, application/data level security (including digital signatures and encryption) and user authentication.
- Connectivity: At the tip of the pyramid is the mechanism used to transmit the data, which might be an Internet-based thin client platform, host-to-host solution or SWIFTNet.

Possible Combinations

One of the principal benefits of separating the integration elements into the four layers outlined in the previous section is the degree of flexibility that it makes possible. For example, consider a corporation that currently only transmits vendor payments from its ERP system directly to a bank. A typical combination of components for such an organisation might appear as in Figure 2.

Figure 2: Vendor ERP to Bank Transmission Components

	Vendor payments
Connectivity	Host-to-host (SFTP/FTPS)
Security	PGP
File format	XML
Delivery tools	ERP adapter

If the corporation subsequently decided that it wanted to perform end-of-day automated reconciliation of its bank statements, this would require transmission of bank account statements by the bank for capture by the corporate ERP system. However, as can be seen in Figure 3, the actual changes required can be kept to a minimum and only apply to the file format element (where the Camt.053 end-of-day account statement reporting message format is added to the existing XML format used for payments) and the delivery tools. The connectivity and security elements are completely unaffected, so the cost and disruption caused by the change are minimised. Corporate IT input would be confined to reviewing the ERP configuration and making any necessary changes.

This compartmentalisation also responds well to unplanned changes caused by external factors. For example, there are many business rules within an XML payment file, but if the file is configured in a standard manner it is reasonably straightforward to respond appropriately. If, for instance, a regulator introduces a rule that payments above a certain value must be sent as high-value payments, then only one field in the XML file will need changing – everything else remains the same.

Figure 3: Changes Required for End-of-Day Automated Reconciliation

	Vendor payments	Bank statement auto reconciliation
Connectivity	Host-to-host (SFTP/FTPS)	Host-to-host (SFTP/FTPS)
Security	PGP	PGP
File format	XML	Camt.053
Delivery tools	ERP adapter	Reconciliation consultancy by bank

Experience and Expertise

This modular approach can clearly deliver a range of benefits, such as cost reduction, efficiency and strategic flexibility. However, the level of benefit achieved depends heavily upon two critical factors – experience and expertise. A banking partner that can deliver both will be able to assist in producing the cleanest possible structure that is also accurately aligned with a business and its financial processes. (Figure 1 illustrates how professional services bear upon all layers of a modular integration architecture; experience and expertise will deliver various structural benefits – such as the clearest possible delineation between module layers.)

Consultancy Checklist

In order to ensure a productive and painless implementation, corporates need to probe potential partner banks' capabilities in the following areas:

- Process consulting: To review the current process and propose enhancements.
- Technology consulting: To assist in selecting the most appropriate technology both for the immediate need, but also in the context of possible future requirements for bank interface needs.
- Solution consulting: To ensure that the proposed solution is aligned with the corporation's key objectives and will also be able to grow with the company. This is particularly critical, as corporate growth and technology trends cannot be predicted with ease, so the proposed solution should be able to accommodate a wide range of possible future development paths.
- Payable, receivable and reconciliation consulting: To ensure the highest level of STP and process efficiency.
- Qualifications: Can the bank provide certified consultants in SWIFT, SAP, Oracle, project management and process specialisation as part of the interface project team? (This is essential for ensuring a future-proof solution.)
- Tools: What dedicated implementation tools can the bank provide? Will they facilitate more effective collaboration between bank and corporate implementation teams? How?

A bank that has done occasional implementations of this nature is insufficient; one that is accustomed to handling them on an everyday basis is essential. Furthermore, single country implementation experience is irrelevant to a multinational corporation; the bank must be able to prove that it has conducted multiple multi-country implementations successfully. A bank with this breadth and longevity of experience will also be more likely to have previously conducted implementations in a particular industry and will therefore be able to make the most relevant and valuable recommendations regarding process improvements.

When it comes to expertise, the bank should, of course, be able to offer a team of consultants suitably certified in key technologies and processes, such as SAP, Oracle Financials, SWIFT and Six Sigma. However, that alone is of little use if these consultants are only concentrated in one or two major locations. In order to deliver tangible results, they need to be on the ground and available in the locations where implementations are actually taking place, so timelines can be minimised and value maximised.

Conclusion

A modular approach to ERP/bank integration can deliver multiple benefits. Apart from reducing costs and disruption, it also gives the corporation greater strategic and tactical flexibility. Adjustments can be made quickly to allow for major and minor changes to the corporate business model or financial processes. Business acquisitions, expansion into new markets, a new supply chain financing scheme, a new bank or even a complete change of corporate ERP system can all be more conveniently accommodated. Nevertheless, while the four layer modular architecture may be ubiquitous in the general sense, the exact implementation will vary from corporation to corporation. How effective that implementation is in practice – both in terms of immediate benefits and future flexibility – is heavily dependent upon the quality of the professional services used. An organisation that can point to a long and proven track record in this space is critical to achieving success.

Solution Checklist

While the precise nature of any ERP/bank implementation will depend upon individual circumstances, some general principles apply. In order to achieve best practice, here is a list of questions that need to be considered regarding possible provider solutions.

Prior to implementation:

- Is the systems architecture composed of plug and play components?
- Is it sufficiently flexible to accommodate changes to business and technical developments?
- Is it a standard solution or heavily customised? (Heavily customised solutions will impede flexibility.)
- Is it a workflow-based business rules configurable solution? Can the systems team quickly explain the steps required to make a change? (Ask them to show the changes required to accommodate a change request.)
- How robust are the contingency measures for each implementation layer? How quickly can they be brought online? What measures are in place for informing third parties (e.g. partner banks) of a switch to contingency operation?
- Are any proprietary file formats, security or connectivity tools used? (Wherever possible, avoid them, as they will reduce flexibility and extend timelines.)
- Are core business rules and country-specific rules completely discrete? (Any intermixing of the two will significantly reduce flexibility and inflate the cost of any changes that have to be made later.)
- Does the implementation present opportunities to enhance or streamline existing processes?
- Does the proposed solution work for both centralised and decentralised processing?

Once the implementation is underway:

- Does the implementation team include sufficient experts and experienced personnel? Do these include specifically certified consultants for speciality tasks such as SAP, Oracle, SWIFT and integration? Are they focused on the implementation? (i.e. they are not running implementations for multiple clients simultaneously.)
- Are the project management tools of sufficient quality to manage the implementation efficiently and ensure that any changes made are not disruptive?
- Is the project progress status visible to all stakeholders spread across multiple time zones and geographies online and can they interact to obtain real-time updates?
- What impact does putting through a change have? How easily is it implemented?
- Are the contingency measures adequate? Review test cases and test plans to ensure they really do accommodate all possible scenarios.

Scenarios

The following items are examples of the sort of changes that corporations commonly experience that will affect ERP/bank integration. The use of a flexible and modular architecture will mean that these can be efficiently accommodated.

Business or exogenous changes

- Mergers and acquisitions, resulting in an heterogeneous infrastructure
- Multiple ERP systems or different versions of the same ERP system
- Addition of payroll or treasury systems to the bank interface
- Statutory or regulatory changes

Business rule changes

- Change of payment method from high to low value (or vice versa)
- Approval mechanism changed from within ERP system to within the banking environment
- Reconciliation process changed from manual to automatic
- Reconciliation rules or posting logic changed in ERP
- Volume increase or instrument change due to centralisation or organic growth

Technological changes

- Changes within the ERP system
- File format change, for example from EDIFACT PAYMUL to XML
- Change in security methods, such as the introduction of digital signatures
- Change in communication mechanism, such as from web-based banking file upload to host-to-host or SWIFTNet FileAct
- Systems hardware change
- Systems software change, such as new operating system or database

SWIFT for Corporates: Beyond Treasury and Cash Management

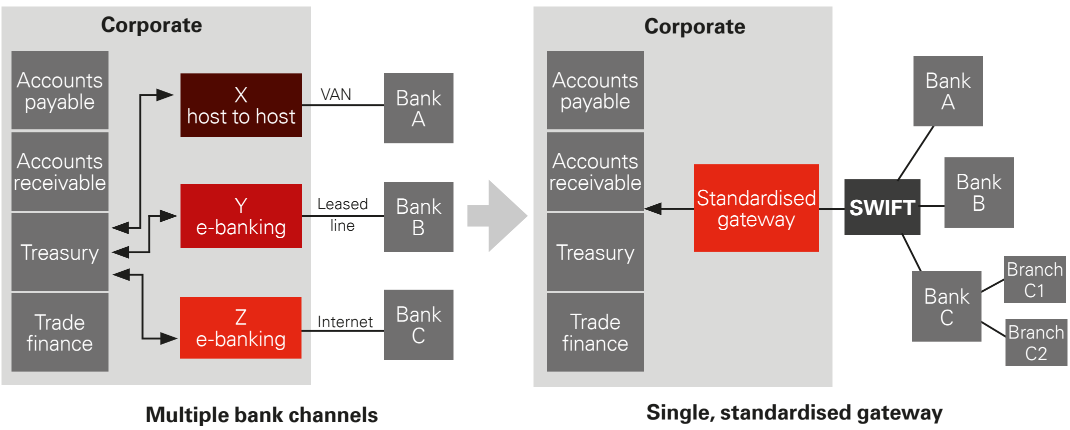
- The case for corporate treasurers to move to a SWIFT-based open architecture model is becoming more compelling as new services become available on the platform.
- Corporate treasurers are now extending their use of their SWIFT platform capabilities into the trade and supply chain space and into electronic bank account management.
- Letters of credit based business can now be automated using SWIFT MT798 standardised flows and FileAct capabilities.
- SWIFT's 3SKey provides corporate treasurers with a single digital identity in a multi-banking, multichannel world.

Daniel De Weyer, Client Director for HSBC Asia Pacific, SWIFT, Hong Kong

More than 900 corporates – 11% of them in Asia – are taking advantage of SWIFT to provide them with greater visibility across their banking relationships. They range from large multinational companies to local, small and medium-sized enterprises. They are using SWIFT primarily for cash management, sending – treasury and/or commercial – payments to their banks, and in return, they receive statements electronically, which provides them with global visibility on their cash balances.

SWIFT reduces cost and risk and improves auditing processes, ensuring easier compliance and increased straight-through processing (STP). SWIFT also enables corporate treasurers to better optimise cash and liquidity management and streamline their operations. Integration with back office applications is easier and cheaper. Many enterprise resource planning (ERP) solutions and treasury management systems (TMS) providers have embedded SWIFT capabilities into their applications, so that integration is delivered virtually "out of the box".

Figure 1: From Multiple Channels and Formats to a Single, Secure, Standardised Gateway



Source: SWIFT

Efficiency in International Trade

Increasingly, corporates are using SWIFT for more than cash and treasury management. Efficient management of international trade often requires corporates to operate in both open account and documentary environments. The choice of instruments is influenced by different factors: by counterparty and (perceived) counterparty risk, by type of business, by value of the transaction, by geographical location and/or by the legal framework within which the company needs to operate.

Letters of credit (LCs) and demand guarantees/standbys have been around for a long time. Evidence suggests that trading on open account terms is increasing, but documentary trade finance instruments still have a crucial role to play. In addition, the credit crunch and financial crisis have re-enforced the need for corporations to work with a growing number of banking partners.

In order to support necessary business processes and to ensure thorough visibility on trade transactions across diverse banking relationships, corporate treasurers are increasingly adopting multi-banking trade finance solutions.

Gerard Heubeck, Head of Trade Finance Advisory & Transaction Services at Siemens Financial Services GmbH, confirms, "When we embarked on our trade re-engineering project, it became evident that the only viable option for us is multi-banking. We deal with letters of credit and demand guarantees across the globe with more than 50 banking partners and they need to be aligned in order to fulfil our working capital management requirements."

Promoting Industry Standards

The International Chamber of Commerce (ICC) has for many years provided rules to support the legal framework for international trade, for example the UCP 600 (Uniform Customs and Practice for Documentary Credits), the URDG 758 (Uniform Rules for Demand Guarantees) and ISP 98 (International Standby Practices). SWIFT offers the inter-bank MT (Category 7) messaging standards and technologies. In order to meet pressing market requirements, SWIFT has extended those standards to the corporate market.

Such industry standards underpin solid, reliable multi-banking trade finance solutions for banks and corporates alike. The MT798 message covers 43 flows for corporates looking to automate LC and guarantee/standby flows in a multi-bank environment.

Rapid, Easy Access to Information

The way a corporate chooses to implement its trade operations will have a direct influence on business processes. If the exchange of information relies on paper-based instruments, there can be significant delays in accessing the required data – and if the data is delivered through a multitude of interfaces, it becomes harder to get a simple, centralised view of transactions and to discern the complete picture. Different technologies and multiple connections create operational complexity – which is a drain on resources and which may also result in complicated reconciliation processes prone to manual errors.

Re-engineering trade transaction flows promises clear benefits and efficiency gains. The effective electronic distribution of data is a business enabler. SWIFT's Trade for Corporates standards enable the use of multi-banking trade finance solutions independent of any one technology or service provider.

Corporates are benefiting from SWIFT in both the cash and trade areas of their businesses. Accounts payable and accounts receivable, treasury and trade departments can all take advantage of multi-bank connectivity. Better visibility on cash positions, more automation, easier auditing and improved security all increase productivity. SWIFT sees a growing number of corporates moving in that direction – including Alcatel-Lucent, Arcelor-Mittal International, Metsä Finance, Saudi Aramco, Schneider Electric, Siemens Financial Services and Voith.

A Single Digital Identity

Corporations still face challenges in implementing standardised solutions across the multiple banks with which they do business. Addressing one of those challenges is SWIFT Secure Signature Key or 3SKey, which simplifies the authentication process for corporates linking to multiple bank treasury systems.

3SKey is a digital identity solution to enable banks and corporates to exchange information in a secure way. Using 3SKey, corporate treasurers can manage their various banking relationships using a single, multi-network personal signature device. This reduces the complexity of managing the ever-increasing number of tokens and passwords typically needed to administer multiple accounts with multiple financial institutions. 3SKey is a single token with one password that replaces the many different devices such as secure IDs, digipasses and other tokens corporate treasurers need to access numerous different websites and bank applications.

3SKey was launched at Sibos in Amsterdam in October 2010, and has since been adopted by major banks in Europe and more recently in the Americas. Banks are now starting to offer 3SKey as the most appropriate solution to meet their corporate customers' authentication needs, regardless of the channel being used. Interest in 3SKey in the Asia-Pacific region is growing, as corporate treasurers look for ways to more easily manage their multiple accounts – with solutions that can also be rolled out to their subsidiaries.

The Value Proposition of 3SKey

SWIFT's digital identity solution provides a range of key benefits to corporates and banks:

- Simplicity: 3SKey simplifies the signing process for corporate treasurers across applications and banks. They no longer need to maintain multiple authentication methods.

- Efficiency: 3SKey allows for the creation of a single credential for personal signature, facilitating seamless transaction processing, increasing efficiency and reducing operational risks and costs for both banks and their clients.
- Cost reduction: 3SKey allows banks and corporates to eliminate the duplicate spend involved in managing multiple devices and processes for secure financial information exchange, replacing them with a single, standardised multi-bank solution for personal identity management.
- Security: 3SKey is a highly secure solution built using the latest cryptographic technology. This minimises the risk associated with personal authentication of corporate representatives. SWIFT will ensure the technology at the heart of 3SKey is updated as cryptographic techniques develop, enabling banks and corporates to benefit from the latest developments in this space.
- Standardisation: 3SKey is built using commonly used industry standards, so it can be easily and rapidly integrated into corporate and bank applications, including online web channels offered by the banks to their corporate clients.
- Multi-network functionality: 3SKey can be used on the SWIFT network, but also on proprietary bank channels (bank web interfaces), domestic networks and other private channels.

For banks, the value proposition of 3SKey is twofold. First, SWIFT handles all the public key infrastructure (PKI) related processes as a trusted party, enabling a bank to outsource these operations. Second, using 3SKey, the banks remain in control of their own registration and know-your-customer processes when enrolling the tokens of their customers.

A Successful Pilot

The launch of 3SKey in October 2010 followed a successful pilot in France, involving major banks including HSBC, Société Générale, BNP Paribas, Crédit Agricole CIB and BPCE, and several large companies including Danone, France Télécom and Airbus.

Pierre Jalade, VP Treasury, Airbus SAS, comments, "The successful 3SKey pilot has been for Airbus a great opportunity to validate the SWIFT certificate solution. I am fully convinced that 3SKey is setting the new industry-wide standard for personal signatures. With 3SKey, SWIFT is certainly providing, to corporate treasurers operating in an international environment, the most appropriate answer to authentication requirements." He adds, "My aim is now to cascade it to all my banks in all the countries where we operate."

SWIFT's electronic bank account management (EBAM) solution to the manual, paper-based process of account opening, closing and maintenance, which has been live since mid-2010, also uses 3SKey to securely identify operators and authenticate information.

Current Approaches in Counterparty Risk Management

- Today's treasury best practice requires that an effective counterparty risk management solution be in place.
- A menu of more market-sensitive indicators such as credit default swap spreads, security prices and indices should supplement solutions based on classical credit ratings.
- Technology plays a central role in the delivery of a solution mechanism that can be highly automated so counterparty exposures are objectively and effectively monitored.
- The evaluation of an optimum counterparty limit management solution depends on several factors, including required response speed, robustness and cost justification.

Pole Yu, Regional General Manager, IT2 Treasury Solutions Ltd

More than three years after the global financial crisis, its effects continue to reverberate around the world's financial markets. The emphasis of concern may have shifted from the banking to the sovereign sector, but the underlying issues for corporate treasuries remain the same: quantifying the real creditworthiness of all counterparties, assigning and managing appropriate counterparty dealing limits, and monitoring changes in creditworthiness with the necessary speed and sensitivity so that effective and timely responses to any sudden deteriorations may be made.

Sovereign debt issues amongst the weaker eurozone countries and the United States' narrow avoidance of a politically-provoked technical default – followed by an unprecedented downgrading by Standard & Poor's – have caused uncertainty in the markets. Today's global economy means that companies operating in financially strong areas and sectors are not immune to the risks of direct or indirect exposure to less creditworthy counterparties, whether they are corporate, banking or sovereign institutions. These risks may be experienced directly, because of the multinational nature of many companies' business operations, or indirectly through the knock-on effects transmitted through the banking sector. Credit risk is encountered in treasury exposures, in investments, and in the commercial receivables book, so the corporate sector should be included in the analysis, in addition to the sovereign and banking sectors.

Accordingly, a key element of prudent corporate treasury management is the evaluation of the approaches to counterparty risk management that are presently attracting interest among the world's corporate treasuries, combined with the modification of treasury policy to implement improvements appropriate to the organisation.

Credit Ratings Are No Longer Enough

More and more treasuries are now supplementing the use of classical credit ratings to evaluate counterparties' creditworthiness with faster-moving and therefore more sensitive indicators – it is salutary to recall that Lehman Brothers carried an investment grade 'A' rating from Standard & Poor's at the time of its collapse in 2008. In the more recent case of credit deterioration of some Eurozone countries, credit ratings were again found lacking as leading indicators of the mounting problems, with several commentators stating that the eventual downgrades came too late to be of real value to the investment community.

The rating agencies seem to have sharpened their response in the unfolding of the sovereign debt issue – but can the use of credit ratings alone now be regarded as best practice for corporate treasuries? Financial institutions have led the way in developing new, more effective approaches to credit evaluation. In the corporate treasury sector, the adoption of a range of market-linked measures has become best practice in the evaluation of counterparties' creditworthiness.

One of the most widely adopted measures is tracking counterparties' credit default swap (CDS) spreads. In fact, the performance of Lehman Brothers' equity price and CDS spread both operated as accurate leading indicators of a rapidly deteriorating credit status in the weeks preceding the actual failure.

CDS spread monitoring is the basis of the recommended methodology of the US Association for Financial Professionals (AFP) for assigning a monetary value to non-performance risk, as required under FAS 157. It is appropriate to note that very few corporate treasuries actually use the CDS as a hedging instrument – the volatility that makes the CDS such a sensitive monitoring measure makes its use unattractive to the majority of corporates. In addition to CDS spread monitoring, there are several other measures for counterparty credit monitoring: these include equity and bond prices and indices, probability of default factors published by expert third parties and working capital ratios. Most now accept that no single indicator on its own can adequately answer the risk management objectives of treasury.

Corporate treasurers now enjoy a wealth of options in terms of tools to evaluate and monitor the performance and creditworthiness of their counterparty universe, so that they can supplement credit ratings with faster-moving indicators, as appropriate for their business-risk profile.

The Role of Technology

Today's credit management requirements are complex and the effectiveness of solutions depends on their integration with existing treasury technology, allowing the entire exposure to be monitored and sudden deteriorations for a given counterparty (or counterparty grouping) to be signalled via alerts and reported in real time, or at least on demand. The risk factors adopted as policy at a given treasury may be built into a number of treasury management system (TMS) functions, including mark-to-market valuations and, for companies with US reporting obligations, for FAS 157 compliance purposes. In terms of counterparty risk management, the chosen risk factors may be applied to the allocation and management of counterparty trading limits, and to the continuous monitoring and analysis of counterparty exposures.

The actual solution mechanism can be highly automated, so that monitoring and the issuing of any necessary alerts can take place without direct human intervention. This provides a strong degree of management assurance that counterparty exposures are being objectively and effectively monitored. The setting up of the automated solution will include a straightforward configuration process that links and integrates the TMS's risk management functionality with a reliable source of the selected risk indicators, such as equity prices and CDS spreads. Once the integration has been set up, the required data may be automatically "pushed" into the TMS whenever changes occur, or automatically "pulled" into the TMS at a pre-defined frequency, or imported on demand. Once the information has been updated, the TMS can automatically apply the changes in all relevant areas, including valuations, limit assignments and counterparty exposure analysis, so that all information reported by the TMS fully and accurately reflects the current situation. The provision of the necessary integration tools and automated functions to provide secure, hands-free counterparty exposure management is a standard feature of today's treasury technology.

This overall process enables the derivation of a synthetic or "shadow" rating and its application within a TMS. With appropriate weighting of each factor, the synthetic rating (or individually weighted risk factors) may be employed by the corporate treasury as a sensitive, customised tool to ensure that counterparty exposures are evaluated and managed with the optimum speed and precision, enabling the organisation to detect sudden deterioration in a counterparty's creditworthiness – and to take the necessary mitigating action, quickly and effectively.

Solution Scope and Performance

When corporate treasuries are determining the details of any upgrade to their counterparty exposure management infrastructure, they will naturally evaluate the required investment against the benefits of operating a best practice solution. One key factor is the objective determination of the level of counterparty risk that they are carrying versus the requirements of treasury policy, and then deciding, for example, whether it is appropriate to implement a hands-free, real-time solution, as opposed to an on-demand arrangement. The detailed cost justification will be specific for each corporate treasury, because of individual differences in policy and business profile, as well as differences in the size, location and quality of counterparty banks and issuing entities. The implemented policy may well be determined for reasons other than pure counterparty creditworthiness, such as the existence of important lending and other commercial relationships. So there may be radical differences in the appropriate level of risk management solution that should be adopted by corporations of similar type and size.

So what is the required response speed of a best practice counterparty limit management solution? A case can certainly be made for the real-time solution, with integrated monitoring of one or more market-sensitive creditworthiness indicators, such as the CDS spread. A fully automated solution that will issue alerts to nominated individuals if there is a sudden deterioration in creditworthiness for a counterparty (or counterparty grouping) provides the most robust and secure result, since, once set up, monitoring and alerting is not reliant on human intervention, and is significantly more dependable. In practice, the response to the automated detection of a pre-defined credit problem condition could be implemented to include the continued issuance of alerts and escalation processes until remedial action is initiated.

The technical elements of implementing an enhanced counterparty risk management solution should include an accommodation to the true scope of the composition of a credit exposure to a given counterparty. In practice, a corporate's exposure to a given bank might include:

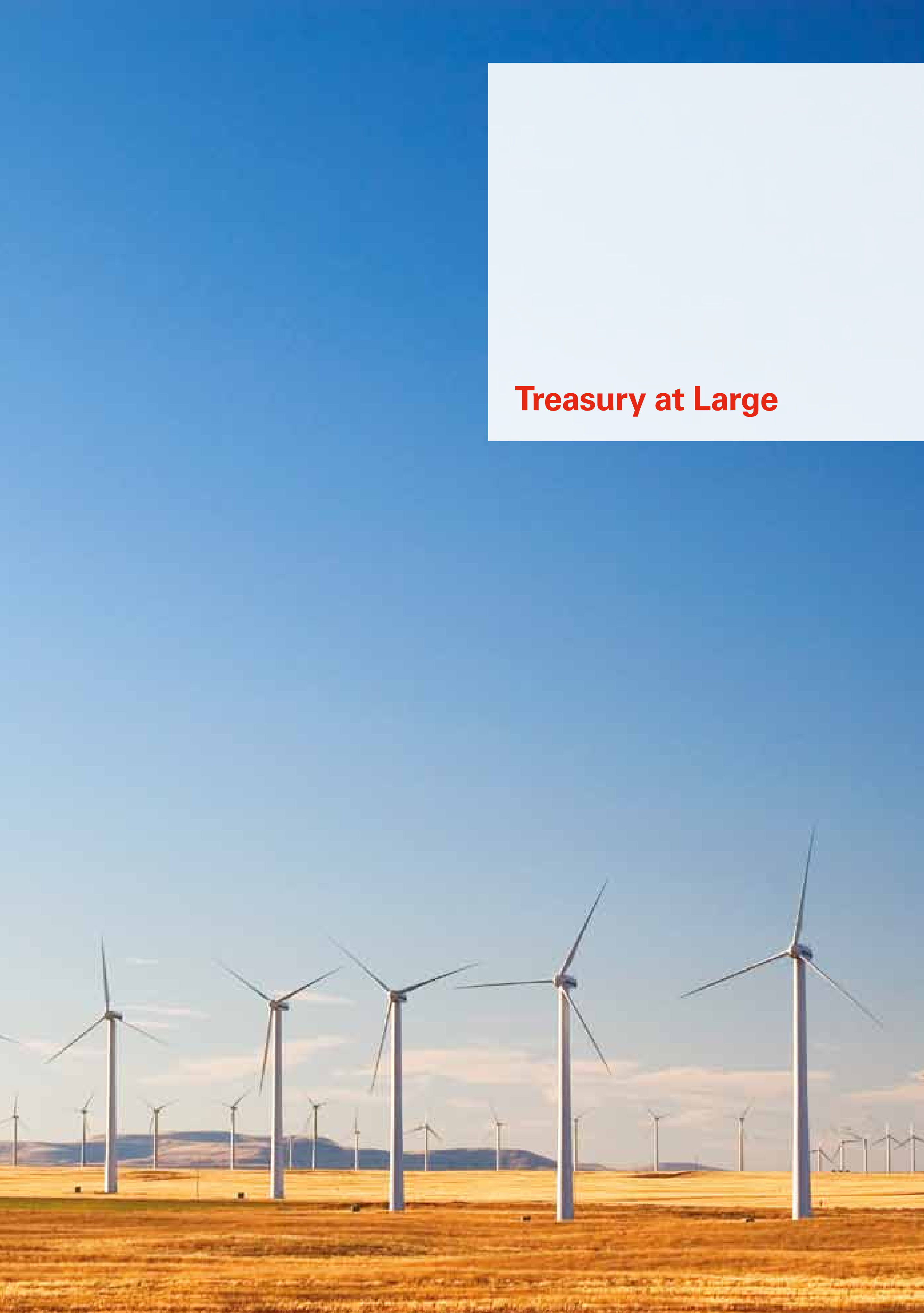
- global bank account balances;
- time deposits placed;

- money market investments held, e.g. certificates of deposit (CDs), acceptances, repos, commercial paper;
- open foreign exchange (FX) deals, e.g. spots, forwards, swaps, futures, options;
- open interest rate derivative deals, e.g. swaps, cross-currency swaps, options, swaptions, forward rate agreements (FRAs), futures;
- bond investments held;
- equity investments held; and
- collateral held against assets.

The diversity of these components – cash, investments, collateral, and instruments with streams of future fixed and variable cash flows – indicates that the implementation of a complete and fully effective solution may in some cases be more complicated than it initially appears. The technical solution is quite demanding; it needs to collect and manage information from multiple sources within and outside the organisation, apply the chosen creditworthiness measures to each counterparty exposure, broadcast the results and manage the response as required. Naturally, many corporations will not carry exposures to all or even many of these asset classes. The important issue is that they should be investigated when a specific company's trust exposure spectrum is analysed, to verify that the analysis is complete and accurate.

Navigating an Uncertain Future

This article has outlined some of the considerations and approaches to counterparty exposure risk management that organisations are taking in today's corporate treasury industry. They will be of interest to corporate treasurers in the Asia-Pacific region and beyond, in their evaluation of routes for achieving best practice operations in this sensitive and important area. A strong solution means that the organisation will be in a position to receive accurate early warning of an emerging creditworthiness issue with a counterparty or group of counterparties, in any sector (sovereign, bank or corporate), ensuring these organisations are competitively positioned to define and execute any necessary remedial action – perhaps in the early stages of a crisis when the speed and precision of the response may well be critical to success, as recent experience shows. Implementing an optimal technology solution for counterparty exposure management cannot of course eliminate the endemic risks and uncertainties of the financial markets – but it can certainly help with more assured navigation into the future.



Treasury at Large

Risk and Volatility: Asian Profitability and a Good Night's Sleep

- While not as standardised as many developed markets, Asian markets still present a wealth of business opportunities.
- A concern for many corporate treasurers is how to manage the foreign exchange and interest rate risks associated with these opportunities.
- A review of four key Asian markets – China, India, South Korea and Vietnam – shows that increasing numbers of instruments are becoming available for efficiently managing these risks.
- However, designing and implementing a hedging strategy is heavily dependent upon having comprehensive local knowledge.

Ivan Wong, Managing Director, Head of Corporate Sales, Greater China, Global Markets, HSBC, Asia Pacific

Historically, hedging currency or interest rate risks in many Asian markets has not been straightforward, due to issues such as currency controls or other diverse local regulations. However, while the situation is still some way from the standardisation and simplicity of many developed markets, there are clear signs that things are definitely improving in certain countries, so with the right local knowledge, a peaceful night's rest for treasury is now a reality, not just a dream.

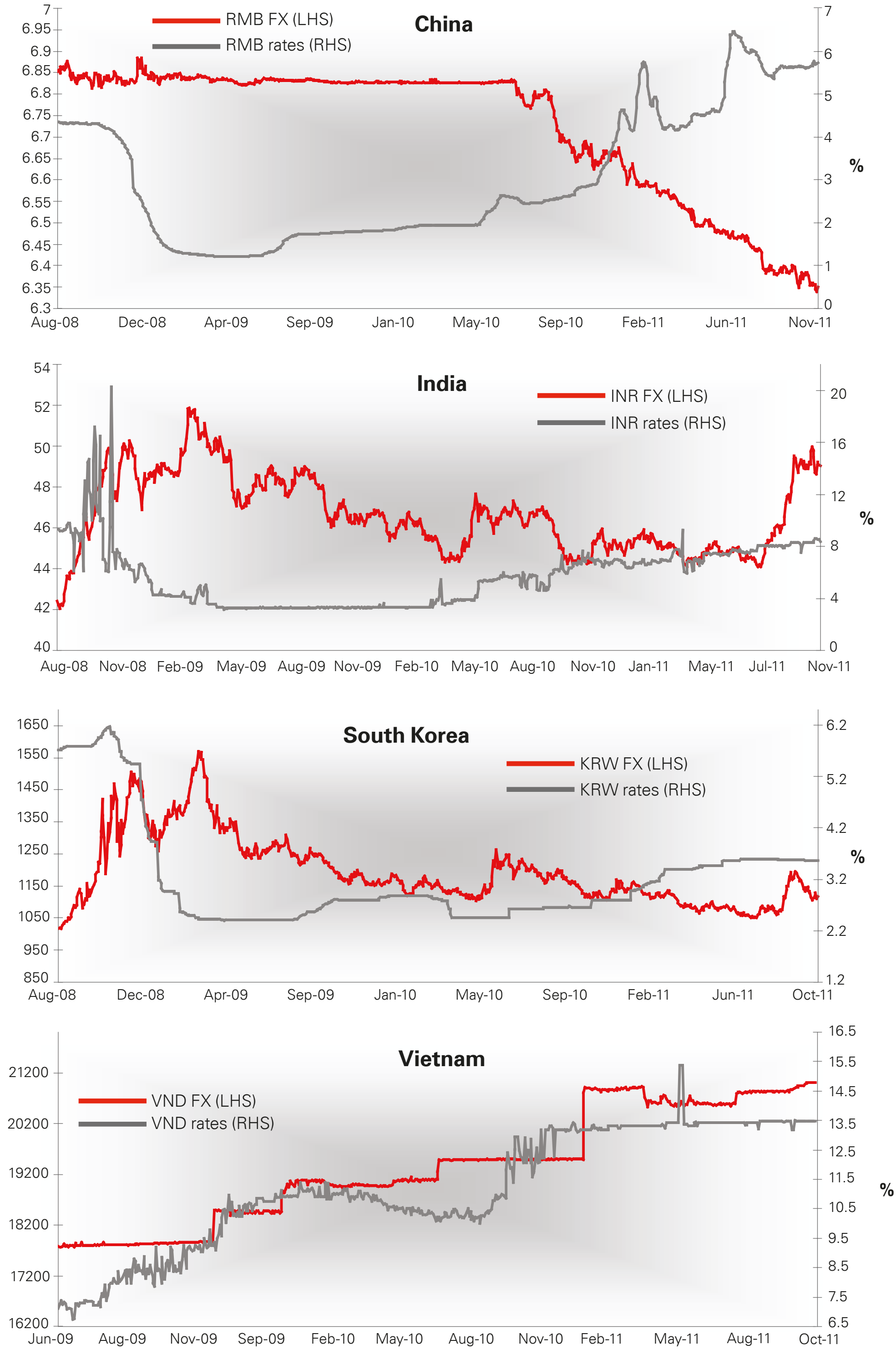
Volatility of a Different Order

While most currency markets have been volatile of late, in Asia volatility is measured on an altogether grander scale. Moves of 20-30% in just a matter of months are not uncommon, but even larger shifts can and do occur. For example, between late 2008 and early 2009, the South Korean won (KRW) moved by more than 60% against the US dollar (USD). While those with longer memories will recall the huge moves seen during the 1997-1998 Asian currency crisis, when the Thai baht (THB) fell from 25 to 56 to the USD and the Indonesian rupiah (IDR) plunged from 2,500 to nearly 20,000.

For those caught on the wrong side of it, foreign exchange (FX) volatility of this magnitude has major negative implications for the bottom line. Furthermore, this volatility is not always unidirectional across the region – as Figure 1 shows, the renminbi (RMB) has been appreciating while the Vietnamese dong (VND) has been depreciating. In addition, rates may start and finish a particular period at a similar level but exhibit wide volatility in between – as shown in Figure 1 for the Indian rupee (INR) and the KRW.

Although the overall trends for interest rates have been more consistent, with most markets' interest rates having already bottomed out and now heading back upwards (typically in response to concerns about inflation), there has still been considerable volatility here as well (see Figure 1).

Figure 1: Volatility in Four Key Asian Currency Markets



Source: HSBC, Bloomberg

Convertibility

A lot of currencies in Asia are still not entirely convertible, which obviously complicates the hedging process. Another important consideration is liquidity, which varies considerably across markets in the region – as well as between onshore and offshore markets for the same country.

Nevertheless, a significant degree of liberalisation is under way in some countries, so if treasurers have access to the right local knowledge they can take appropriate advantage of this to implement effective Asian hedging strategies.

A further beneficial factor has been the way many Asian governments have reacted in the aftermath of the Asian currency crisis, of which one contributing factor was their dependence on foreign currency debt. In response, these governments have taken proactive steps in developing their local currency bond markets, which have consequently made substantial progress over the past decade. The corollary to this has been development of the onshore interest rate and cross-currency swap markets in these countries. Furthermore, in certain restricted markets there has also been significant progress in the evolution of offshore hedging instruments.

China

With a population of more than 1.3 billion, China is already the second largest economy in the world and the largest exporter. Given its pace of development, China is also a market that few international corporations can afford to ignore.

However, managing the risks associated with this can be challenging, especially since the regulatory regime in China is changing very rapidly. This makes keeping track of what is actually possible on the ground extremely important, which emphasises the need for a reliable and detailed source of local expertise. Risk management in China is also very much a case of two markets, the onshore and offshore, which differ appreciably.

Onshore Risk Management

Currency

The People's Bank of China (PBOC) maintains the RMB as a managed currency with reference to a basket of other currencies. Details of this basket have not been formally disclosed but it is commonly assumed to include USD, the Japanese yen (JPY), the euro (EUR), the Australian dollar (AUD), the Canadian dollar (CAD), the Singapore dollar (SGD), the Malaysian ringgit (MYR), THB and the Russian ruble (RUB), as these currencies represent China's major trading partners.

The onshore version of the RMB (also referred to as CNY) is highly regulated, but is undergoing significant liberalisation and is now partially convertible. The PBOC conducts fixings of the exchange rate at 9:15am Beijing time every business day, with the daily trading range of the onshore RMB being kept within a band of +/- 0.5% of the daily fixing exchange rate.

While this sounds relatively conservative, it still constitutes considerably greater currency volatility than pre-2005 when the RMB was by and large pegged to the USD. From the introduction of the managed float regime in 2005 until the middle of 2008 (when the Chinese government temporarily reintroduced the USD peg in the interests of stability) the currency appreciated significantly. The managed float regime was reintroduced in June 2010 and since then the currency has continued to appreciate.

However, it is important to note that since the managed float regime was reintroduced there has been considerably greater volatility in the exchange rate than previously (see Figure 1). This suggests that while in the long run the currency will continue to appreciate gradually (probably at approximately 5% per annum over the next two years) there will be more "ups and downs". Therefore, treasurers looking to determine an appropriate risk management strategy for the RMB need to be aware of the increasing significance of trade execution timing in this respect.

One positive point regarding onshore currency risk management was the February 2011 announcement by the PBOC and the State Administration for Foreign Exchange (SAFE) that RMB currency options would be introduced to the onshore market, with trading in these actually going live on 1 April 2011. The market is obviously still in the nascent stages and there are also various limitations. For example, buyside customers are only allowed to purchase options (no short selling), only European-style exercise calls/puts are available, and options such as barriers or digitals are not available.

Interest Rates

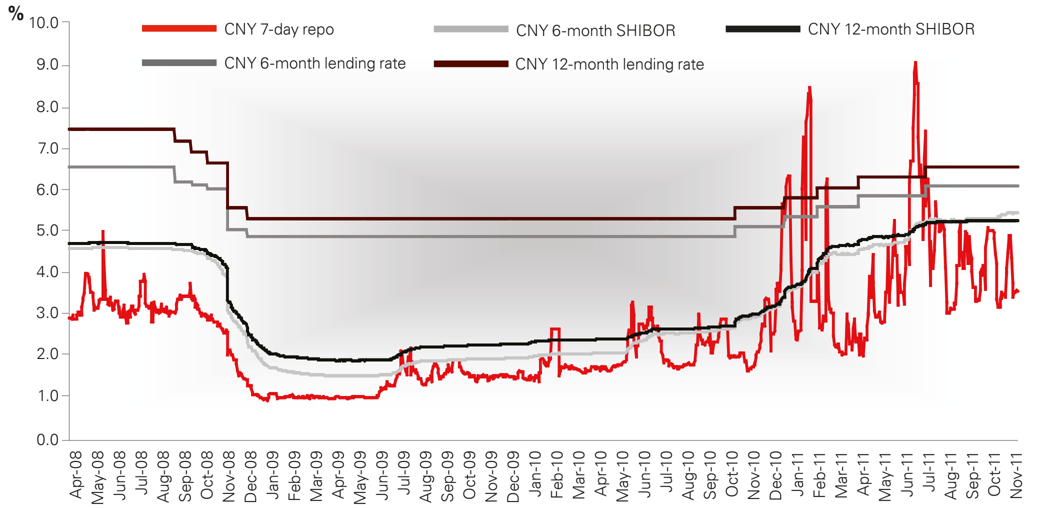
Onshore interest rates are also highly regulated, with both deposit and lending rates set and published by the PBOC. Onshore RMB lending in China cannot be conducted at less than 90% of the benchmark lending rate, while on the deposit side it is not permitted to exceed the benchmark rate. As regards risk management tools for interest rate risk, there is a reasonably developed market in interest-rate swaps, but the key challenge is the inherent basis risk. Most loans reference the floating-rate benchmarks issued by the PBOC, but available hedging instruments typically reference either the repo rate or the Shanghai Interbank Offered Rate (SHIBOR).

This is potentially problematic as the PBOC rate has typically been relatively stable until the recent interest rate rises (see Figure 2). By contrast, the SHIBOR has been more responsive to the market environment, while the seven-day repo rate (arguably the most liquid because it reflects the prevailing money market environment) is even more volatile. Nevertheless, despite these limitations on the effectiveness of the available interest rate management tools, the upward trend in Chinese interest rates definitely makes a coherent strategy for interest rate risk management advisable.

Offshore Risk Management

The offshore RMB (commonly referred to as CNH) market in Hong Kong differs considerably from its onshore counterpart and is probably the most liquid trading centre for the currency. The Chinese government appears to be using the Hong Kong market as a controlled test environment for the progressive internationalisation of the currency.

Figure 2: China – Historical Movements of Onshore Local Rates



Source: HSBC, Bloomberg

Currency

At present there is a two-tier currency market in Hong Kong. In order to accommodate the RMB trade settlement programme, the PBOC and Hong Kong Monetary Authority (HKMA) have agreed that for qualified trade settlement transactions the foreign exchange element can be squared with the RMB clearing bank in Hong Kong, which is Bank of China (Hong Kong), which in turn can tap the onshore RMB market. Therefore, for trade purposes the exchange rate that applies is the same as that applicable for onshore RMB. However, there is also very strong demand in Hong Kong for the currency for other purposes (such as investment) to which offshore RMB rates apply.

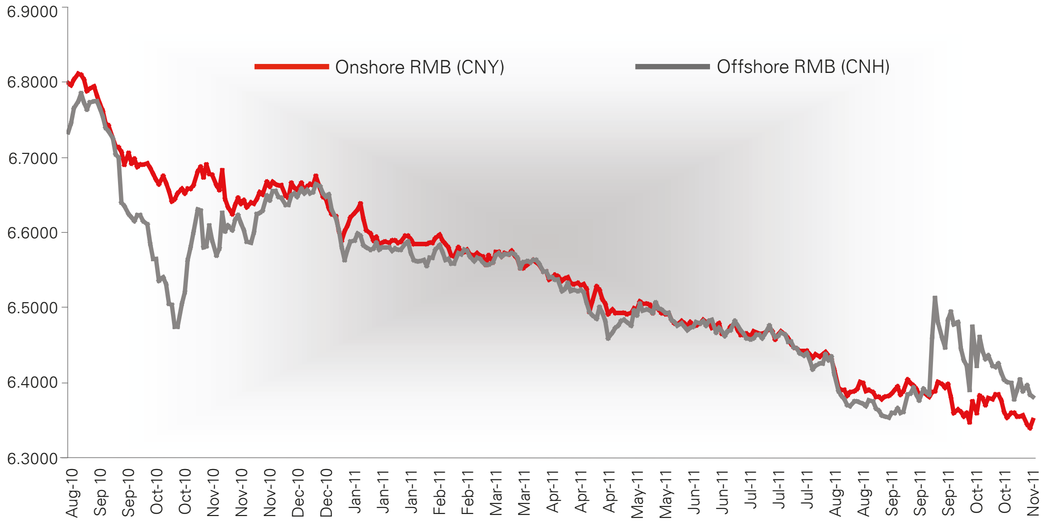
The level of demand in this non-trade market sometimes drives significant divergence between onshore and offshore rates. Figure 3 shows the relative movement in these rates, with October 2010 being a prominent example of this sort of divergence, as demand in the non-trade market made the offshore rate nearly 1,000 pips more expensive than its onshore cousin. More recently there have been occasions where the reverse has been true and onshore rates have been higher due to specific technical factors.

One of the most significant recent developments for those looking to hedge RMB currency exposures has been the emergence of the offshore market for deliverable forwards. At the shorter end of the curve, this is already sufficiently liquid to cover most day-to-day requirements. In addition, deliverable FX spot, FX options and currency swaps are available, while fairly liquid non-deliverable versions of these products are also available.

Interest Rates

The offshore market allows for considerable flexibility in terms of tailoring hedging instrument features to specific requirements and because the offshore market is effectively "free", there are also no associated documentation requirements. In addition, there is an active non-deliverable interest rate swap market (mainly dominated by institutional players), plus a deliverable offshore RMB interest rate swap market. It

Figure 3: Relative Movement of Onshore and Offshore Renminbi (RMB) Rates



Source: HSBC, Bloomberg

is anticipated that the offshore market will at some point overtake the non-deliverable market in terms of activity and the two markets will effectively converge.

However, one important point to bear in mind is that the considerable challenges around basis risk that apply to the onshore market also apply offshore because offshore interest rate hedging instruments reference similar benchmarks.

India

Currency

The Reserve Bank of India (RBI) follows a central bank policy similar to China's as regards floating currency rates. While India does not use a strict band in the same way as China, it is generally understood that the RBI thinks in terms of the real effective exchange rate. As with China, this involves the currencies of the country's main trading partners – USD, EUR, JPY, the pound (GBP), RMB and the Hong Kong dollar (HKD). However, there have been some deviations from this real effective exchange rate policy because the RBI has made fairly frequent interventions in the FX market to maintain currency stability.

The onshore market for FX in India is regulated and documentation is required before treasuries are able to tap the market. In terms of liquidity and instant availability, India is relatively well-developed: spot, forward and option markets are all reasonably liquid. However, as with China, the option market is regulated and restricted: only calls and puts are available. Option combination strategies are allowed, but it is not possible to enter into option combinations that result in receipt of net premium, as this is considered speculative. Barrier options are also currently not permitted, although the RBI is considering this situation, so these may be allowed in the future.

Interest Rates

As regards interest rate hedging, India is more advanced than China, with a well-developed and reasonably liquid onshore interest rate swap market. By comparison, the offshore market is slightly less liquid and because a lot of the necessary instruments are available onshore anyway, the need to expand the offshore market is not so acute.

South Korea

Currency

The Bank of Korea (BOK) applies a floating-rate currency regime, so from a technical perspective the KRW is similar to currencies such as EUR and JPY in terms of hedging instrument availability, which was not always the case. Prior to the Asian currency crisis, the KRW was regulated, but the government has subsequently devoted considerable effort to liberalising the FX market. Although the final phase of this liberalisation was put on hold after the financial crisis of 2008, in comparison with many other Asian countries the market is generally considered to be relatively open already.

However, restrictions were put in place in October 2010 to prevent overexposure on FX positions, by only permitting corporations to hedge up to 100% of their underlying exposure. The measure was introduced because the BOK discovered that some corporates had suffered substantial losses because they had over-hedged their exposure during the most volatile periods of the financial crisis – in some cases up to 250%.

Individuals and resident companies can hold unlimited amounts of foreign currency, both locally or abroad, and offshore investors can access the onshore deliverable market to hedge their investments upon confirmation of the existence of these investments by their custodian banks.

Interest Rates

Interest rate hedging instruments are also relatively accessible in Korea. Offshore there is an active non-deliverable interest rate swap market, while onshore interest rate swaps, options and futures are available.

Vietnam

Vietnam is often regarded as a microcosm of China in terms of being a combination of a socialist political ethos and market economic policies. The country has made efforts similar to China's to move away from primarily low-cost production to more value-added industrial activity, and has actually managed to lure some manufacturing activity away from China's Pearl River Delta. Vietnam benefits competitively from a very favourable demographic profile, with a young and relatively educated workforce.

Currency

The State Bank of Vietnam (SBV) maintains strict currency controls and manages the VND tightly, using a regime based upon a daily fixing and a permitted trading band. The trading band is imposed on both USD/VND spot and forward rates. The SBV devalued the VND by 9% in February 2011 by moving its daily fixing rate from 18,932 to 20,693 and has also narrowed its trading band from +/- 3% to +/- 1%.

Onshore USD liquidity is occasionally in short supply thereby causing market USD/VND rates to trade outside the official trading band. This limited availability of USD liquidity means that the real market rate is actually higher than the official onshore ceiling rate, which creates appreciable distortions.

As a result, it is advisable for companies to take a flexible approach with regard to currency in their commercial contracts, so as to allow them scope to settle their obligations in foreign currencies other than USD when onshore USD liquidity is thin. The SBV does not regulate other currency pairs such as EUR/VND and HKD/VND, so in terms of managing currency risk, using a currency other than USD is one possible solution.

Hedging instruments are heavily regulated. There is an onshore deliverable forward market, but liquidity is extremely thin beyond three months. Onshore currency swaps exist but are highly illiquid and require advance documentary proof of an underlying commercial transaction. An onshore option market did exist, but was banned in 2009 because the SBV was concerned about excessive option speculation in the VND market. In the offshore market, non-deliverable forwards and currency swaps are available, as are non-deliverable currency options on a case-by-case basis.

Interest Rates

The onshore interest-rate market is primitive, with very limited hedging instruments available. Onshore interest rate swaps exist, but the market is relatively illiquid and the lack of a useful floating rate benchmark is hindering its further development. The offshore interest rate market currently lacks any instruments for interest rate hedging.

Making the Right Choices

As Figure 4 illustrates, Asia is extremely diverse in terms of market characteristics and hedging possibilities. At one end of the spectrum of markets examined above is South Korea, which is a well-established, liquid and sophisticated market in which it is relatively easy to conduct risk management for both currency and interest rates.

At the other end of the spectrum is Vietnam, where markets are relatively undeveloped, illiquid and only offer a limited range of hedging instruments. Somewhere in the middle lie China and India, which are both working hard on market development, as well as introducing more onshore and offshore risk management instruments.

Figure 4: Summary – Foreign Exchange (FX) and Rates Market

Country	Foreign Exchange		Rates	
	Onshore	Offshore	Onshore	Offshore
China	Spt, DF, CCS, FXO	Spt, DF, DFXO, DCCS, NDF, NDCCS, NDFXO	CNY IRS	NDIRS, CNH IRS
India	Spt, DF, CCS, FXO	Spt (buy INR only) NDF, NDCCS, NDFXO	IRS (OIS), FRA	NDIRS
South Korea	Spt, DF, CCS, FXO	NDF, NDCCS, NDFXO	IRS, IRO, futures	NDIRS
Vietnam	Spt, DF, CCS	NDF, NDCCS, NDFXO	IRS	Not available

Source: HSBC

Due to this market diversity, when it comes to picking the right instruments for managing FX and interest rate risk, it is important to consider a number of points:

- Pricing: In certain markets, such as RMB, it has typically – though not always – been less expensive to purchase the currency onshore. So corporations able to produce documentation proving genuine trade or other business requirements will find it worthwhile to do so in order to access the onshore market for local currency purchases. Obviously those looking to sell local currency will obtain a better rate offshore.
- Liquidity: Liquidity in the onshore market is usually better than offshore. This is certainly the case for India and Vietnam, but arguably may soon not be so for the RMB, as the offshore RMB market in Hong Kong continues to develop strong liquidity.
- Flexibility: Onshore markets in Asia are usually more highly regulated than their offshore counterparts. So in terms of documentation requirements and product availability, onshore hedging is usually less flexible.
- Accounting/tax/basis risk: There are basis risks to be aware of when using the offshore non-deliverable as opposed to the onshore deliverable market.

Conclusion

Asia encompasses a wide range of regulatory regimes and market dynamics. In addition, volatility can often be high, making a coherent hedging strategy essential. Designing and implementing such a strategy is therefore heavily dependent upon comprehensive local knowledge. This knowledge must span both shifting regulatory requirements as well as the practicalities of finding the most appropriate hedging instruments in terms of liquidity, pricing and flexibility that are actually available in the specific marketplace.

China's Changing Business Environment

Ian Lewis, Partner, Mayer Brown JSM, China

- No longer just a manufacturing base, China is attracting interest due to its expanding domestic market, providing new opportunities for foreign and domestic companies alike.
- China's legal framework has been transformed to reflect the next developmental phase, as the country looks beyond investment dollars and focuses on indigenous innovation.
- Foreign investors should re-examine their strategies in the light of the conditions likely to prevail over the next decade, such as the "go west" policy and healthcare system reforms.
- A challenging but expanding market, China continues to offer opportunities for investors who follow some basic rules for navigating through its complexities and safeguarding their interests.

Anyone involved in business with China over the past 30 years has experienced great change. The business environment has changed dramatically over the past few decades and the legal framework has been transformed. The plastic toy manufacturers that moved into China in the 1980s found cheap labour and a simple legal framework with which to build a profitable export-based business. Chinese companies were hungry for investment dollars at a time when government policy had begun to change as China began its move away from a centrally planned socialist system to a modern economy with a strong private sector driven as much by market forces as government objectives.

The continued expansion of manufacturing in the 1990s assisted the development of Chinese coastal cities and led to an export boom and greater urbanisation that lifted millions of Chinese out of poverty. The successes of China in attracting mass manufacturing after its accession to the World Trade Organisation (WTO) a decade ago has resulted in China becoming the workshop of the world.

China is now a much changed country with a number of world class cities and infrastructure that is the envy of many Western governments. Disposable income amongst the Chinese people has increased to such an extent that many families have moved from near poverty to middle class comfort in a single generation. China is no longer just a manufacturing base but is now attracting interest due to its expanding domestic market, providing new opportunities for foreign and domestic companies alike.

Adapting to Change

Foreign investors that are still focused on low margin/low quality goods that were so successful 20 or 30 years ago are now facing hard times. Manufacturing and real estate costs have increased and China is no longer necessarily a source of cheap labour (particularly in the larger cities). The RMB is appreciating at a time when many currencies in China's key export markets are falling in value. Demand overseas has been hit by the effects of recession and debt burdens as well as low consumer confidence. It has been important for businesses to adapt to change.

Although some sectors have suffered, generally China as a whole has not. China is one major economy that is expanding rapidly (while Japan, the UK, the US and Europe are struggling to recover from recession). China's practice of setting itself five-year plans was once seen as a throwback to a socialist style centrally planned economy but in recent years it has received more respect as China is able to adjust its objectives and priorities as well as review progress. China has continued to change in recent years and further change and adjustment is expected. There are good reasons for foreign investors to re-examine their strategies in the light of the conditions that are likely to prevail over the next decade.

A Complex Market

> "... **it is important to be prepared before making an investment – getting the details right on day one can save investors a great deal of money.**"

Although awareness of what is likely to come is important, it is equally essential to remember some basic rules that have served foreign investors well for many years and that still apply as much today as they did 20 years ago. In particular, it is important to note the following:

- The China market is complex and it is important to be prepared before making an investment – getting the details right on day one can save investors a great deal of money. It is important to understand the legal structures available, the requirements of relevant regulations and government policies relating thereto. It is important to know what is prohibited (e.g. publishing), what activities can be undertaken with a Chinese partner (e.g. certain types of e-commerce) and what activities are open 100% to foreign ownership (e.g. trading/distribution).

- As China has become more rule-based and Chinese law has become more complex and demanding, a good compliance policy is more important than ever. The impact of legislation with cross-border relevance such as the US Foreign Corrupt Practice Act and the UK Bribery Act have also made it increasingly important to ensure that international standards are applied equally in China as elsewhere.

- It is important to ensure that investors understand the business culture, the way negotiations are undertaken in China – at the same time it is important not to fall into the trap of accepting very short form documentation and relying solely on relationships or taking shortcuts without investigating the risks and potential legal consequences involved.

- Investors must recognise that change is not "single speed". A single Chinese market of 1.3 billion people does not exist, in that the business environment differs from place to place within the country. Attitudes, policies and interpretations of the law in major cities such as Beijing and Shanghai may be different from the environment found in second or third tier cities. There may also be local regulations that are applicable in some parts of the country but not others. Certain economic development zones may provide a simplified legal environment and approval processes that can be advantageous to investors in certain sectors.

The Changing Nature of Reform

"Some investors have made the mistake of believing that the legal environment in China will continue to open up and become more favourable to foreign investors."

Some investors have made the mistake of believing that the legal environment in China will continue to open up and become more favourable to foreign investors. This belief arose largely because during the years following China's accession to the WTO, there were a large number of reforms as a result of commitments made by the Chinese authorities during WTO negotiations. Although entry into the WTO provided a clear roadmap for the opening up of the Chinese economy, it is important to remember that China agreed to WTO reforms only to the extent documented at the time and further reform beyond this is far less certain.

Most of the original WTO commitments have now been honoured and whereas WTO-driven changes were concessions made in response to the demands of the international community, future change will be driven according to what the Chinese authorities see as being in China's interest. This will not necessarily be consistent with the demands of foreign investors, and the belief that all and any investment is encouraged is naive. The view that China remains hungry for investment dollars is also outdated. In many cases, Chinese companies have sufficient capital for their needs and Chinese companies are becoming stronger. China has refocused its objectives and is now looking beyond cash.

Innovated in China

China is becoming more focused on innovation rather than basic manufacturing. China wants the goods it produces to be innovated in China rather than just made in China.

There are a number of concerns that have led to China's desire to be more selective in the sort of investment it encourages. For example, the effects of 30 years of industrialisation and industrial pollution on the environment have raised a number of concerns and China is hungry for green technology. There is also a feeling that foreign investors have succeeded at the expense of local industry and that China is simply not generating the skilled labour and new technology that foreign investment should have delivered – instead, foreign companies are often seen as taking the best talent and retaining modern technology within the foreign sector.

This trend towards innovation is nothing new. China changed direction some years ago by encouraging more high quality products. This, however, failed to satisfy all of China's objectives as much of the technology used in high-end products continues to be foreign owned – imported tools or licensed technologies that result in significant royalties being paid to offshore Western interests. China's new five-year plan introduces further change. It focuses on energy saving technology, cloud computing, biotechnology, new areas of manufacturing previously dominated by foreign providers (e.g. aeroplanes) and environmental products such as electric motorcars. Furthermore, China has encouraged Chinese-made products that do not contain foreign-owned technology, and this policy of indigenous innovation has caused some concern among many of China's trading partners.

Protecting Investors' Interests

Although the push for Chinese-owned technology may appear to be an unwelcome development in policy, it should be remembered that many other world markets have for many years been difficult to enter due to a combination of regulatory requirements and domestic competition. China is not the first country to be accused of taking protectionist measures. This policy also needs to be viewed alongside China's other commitments.

China has for example, announced that it intends to join the WTO Agreement on Government Procurement, which is a treaty that ensures non-discriminatory access to government purchases. China has also extended significant comfort to investors through bilateral investment treaties (BITs). BITs mitigate certain risks associated with investment and can provide an effective way to resolve a dispute once it has arisen. A BIT is a treaty established between two countries to encourage investments by one state's investors in the other by providing a promise at the state level of appropriate investment treatment and guarantees to investors. BITs generally include substantive guarantees regarding treatment of investors, which should be:

- fair;
- equitable;
- non-discriminatory; and
- not less favourable to domestic investors or investors from third-party states.

> **"China offers the second most comprehensive investment treaty programme in the world, second only to Germany."**

Some BITs also provide protection from expropriation (i.e. a direct act resulting in taking of property, or nationalising industries). An investor directly benefits from these commitments as they establish direct rights for an investor to take legal action against the host state, which can be enforced to reduce the impact of political or legal changes and risks.

China offers the second most comprehensive investment treaty programme in the world, second only to Germany. By way of comparison, the US has to date entered into BITs with 40 countries compared with 100 listed that have been entered into by China.

Future Opportunities

Although China may become a more challenging market for some foreign investors to enter, it is nevertheless an expanding market. China is encouraging domestic demand and the size of the domestic market will continue to increase. The policy of developing so-called second and third tier cities and the "go west" policy will mean that opportunities will remain significant. The drive towards urbanisation will see cities continue to expand in size over the next decade and beyond.

> **"Although China may become a more challenging market for some foreign investors to enter, it is nevertheless an expanding market."**

Notwithstanding the indigenous innovation policy and other measures that China is likely to take to assist domestic growth, there will continue to be demand for foreign brands. There is no indication that China is going to roll back past reforms, and access to the China market is not going to be withdrawn.

The increasingly international nature of many of China's companies will likely result in concerns about investment and the level of governmental control of businesses will continue to change over the years. Within the next few decades, China is likely to have financial interests in many global corporations and current policy is likely to evolve as China's role in the global economy develops.

China is also going to have a very different set of problems going forward than what it is experiencing at present. One example of this is an aging population, which is likely to become an issue of concern after 2030. By 2050, China's population growth will have peaked and a growing portion of its population will be elderly and in need of care. In addition, China is currently experiencing serious healthcare issues and is keen to provide its population with a modernised healthcare system. The very ambitious China Healthy 2020 programme will likely provide new areas of opportunity for foreign investors in areas such as housing for the elderly, pharmaceuticals, medical instruments and other healthcare facilities.

Learning from the Past, Preparing for the Future

China has been changing consistently – the business environment is drastically different from 30 years ago, and there is no reason to think that the pace of change will slow down. It is important for investors to recognise the nature of the China market and the direction that China is likely to take over the next decade and beyond. China has never been an easy market and this is unlikely to change. Opportunities to work with Chinese companies will likely become increasingly cross-border. Recognising these opportunities and adapting to the changing business and legal environment within China will be vital to foreign investors looking to capitalise on the opportunities that will become available.

Trends and Developments in RMB: Myth or Reality in the Making?

- Much progress has been made in terms of renminbi (RMB) internationalisation.
- Still, some corporate treasurers remain sceptical about the future prospects and practicality of RMB as a settlement currency.
- A more appropriate attitude is pragmatism, in light of expanding market adoption and evidence of sustained commitment to the programme by the Chinese authorities.
- However, matters such as the complete opening up of the RMB capital account may prove challenging, and Hong Kong will remain the primary offshore RMB centre for some time to come.

Thomas Poon, Head of Business Planning and Strategy, Hong Kong, HSBC

As became apparent during HSBC's 2011 Asia Corporate Forum tour, for many corporations outside Asia – and even Asian corporations outside Hong Kong – awareness of renminbi (RMB) internationalisation is often low. Even where corporations are aware of the process, they do not necessarily see it as a particularly pressing matter for their consideration, even when they are already doing business with counterparties in Asia, or even China. Other corporations also question the Chinese government's true level of commitment to the internationalisation process.

While it is important not to overstate the case, the actual progress made to date and the prospects for future RMB internationalisation merit a considerably more positive response. The process is still at an early stage, but there is no question that the Chinese government has demonstrated a phased and committed approach to internationalisation, and continues to do so. From a corporate perspective, a degree of pragmatism is needed as regards how long the process is likely to take. A transition from a closed to a reserve currency is obviously a major step, and one of the most demanding stages in that process – the complete opening up of the capital account – is yet to come. However, the announcement in October 2011 regarding RMB-denominated foreign direct investment (FDI) is the clearest sign yet that the Chinese government is willing to tackle this challenge.

RMB in Hong Kong

While a degree of pragmatism over future progress is advisable, it cannot be denied that progress to date – and specifically the response to that progress in the Hong Kong market – has been impressive. This has been particularly apparent from the growth in CNH (the offshore variant of RMB traded in Hong Kong) trade volumes, deposit balances and the offshore bond market.

For example, in the first half of 2010, total CNH trade volume was approximately RMB27.3bn, but during the corresponding period in 2011, it leapt to RMB803.5bn. The deposit market has also shown impressive growth: total RMB deposits in Hong Kong at the end of June 2010 stood at RMB89.7bn, but by the end of June 2011, they had risen to RMB553.6bn.

In addition, the offshore RMB bond market has also been picking up rapidly. In the whole of 2010, there were 16 RMB offshore bond issues in Hong Kong amounting to RMB35.8bn in value, but in just the first six months of 2011 there were 38 issues with a total value of RMB42.7bn.[1]

These increasing levels of offshore RMB activity are being supported by growing bank participation. According to the Hong Kong Monetary Authority, there were 154 banks participating in Hong Kong RMB clearing at the end of 2010, but this had risen to 180 by mid 2011.

Impressive as these various figures are, one of the most striking RMB statistics is the percentage of China's total trade flows that the RMB now accounts for. In the first quarter of 2011, cross-border RMB-denominated trade flow between China and the rest of the world (including Hong Kong) was RMB360.3bn (some 6.9% of China's total trade volume). However, in the second quarter of 2011, it rose to RMB597.3bn, thereby accounting for approximately 10% of China's total trade volume. While the bulk of this activity is related to trade with Hong Kong, the rate of growth and the significant proportion of total China trade now accounted for by the RMB clearly illustrates the substantive progress already made and the prospects for further growth. A significant shift is clearly underway.

RMB Deliverable Forwards – Liquidity, up to a Point

Despite this progress, some overseas corporate treasuries remain sceptical. One specific example of this has been their attitude to the RMB deliverable forwards now legally available in Hong Kong. Certain treasuries remain unimpressed and prefer to continue using non-deliverable RMB forward contracts instead.

Total liquidity now available in the deliverable RMB forward market makes this stance appear illogical, with daily turnover now typically in the USD500m to USD700m range. Combine this with the spot deliverable market (resulting in a total of USD3bn in daily turnover) and it looks likely that deliverable market liquidity will soon overtake that of its non-deliverable cousin. Given the relative simplicity of deliverable forwards in terms of hedge accounting, it seems likely that an increasing number of treasurers will see the merits of switching from non-deliverable forwards.

However, one important caveat is that while liquidity in RMB deliverable forwards out to around six months is already adequate for most purposes, beyond that date it remains thin. The development of a longer-dated deliverable forwards market will largely depend upon increasing cross-border bidirectional flows of a longer-term capital account nature, rather than short-term trade flows.

A number of factors will influence this, including FDI/outbound direct investment (ODI) to/from the Mainland and shareholder loans. Another related factor is the absence of sufficient longer dated issuance in the offshore RMB bond market where the proceeds are translated to other currencies.

1 *Bond issuance figures do not include certificates of deposit denominated in RMB issued by Chinese financial institutions.*

While the question of foreign exchange (FX) translation will obviously depend upon individual circumstances, the fundamental shortage of longer dated issuance is showing early signs of improvement. To date, the majority of issues have been in the two to three year maturity range, although there have been some longer issues out to ten years from the Chinese government or quasi-government entities. The reason that most commercial issuers have, to date, tended to focus on these shorter maturities is that they coincide with many investors' views regarding the probable timeline for RMB appreciation. Therefore, investors see bonds in the two to three year maturity range as good vehicles for effectively creating long positions in the RMB to benefit from this anticipated appreciation.

However, Volkswagen completed an offshore RMB bond issue in May 2011 with a maturity of five years and Air Liquide has made an issue that includes a seven-year tranche – the longest yet from a multinational issuer. Therefore – assuming reasonable FDI/ODI/shareholder loan activity – it seems logical to expect that liquidity in longer dated deliverable RMB forwards will improve in the not too distant future.

Commitment

Despite the progress to date, some commentators and treasurers remain unconvinced as to the extent of the Chinese government's commitment to RMB internationalisation. Recent events provide considerable reassurance on this point. For example, measures announced by China's Vice Premier Li Keqiang on 17 August 2011 will take RMB internationalisation to the next stage, as well as boosting Hong Kong's position as the premier market for offshore RMB activity. Some of the measures announced are highly significant, such as RMB-denominated FDI and the long-awaited RMB Qualified Domestic Institutional Investors (QFII) programme, which will enable the completion of the "flow back" mechanism of RMB from Hong Kong to China.

Detailed regulations for the RMB-denominated FDI measures were subsequently issued by China's Ministry of Commerce (MOFCOM) and the People's Bank of China (PBOC) on 14 October 2011. The regulations announced by the PBOC also allow cross-border shareholder loans in RMB, subject to the foreign debt registration with the State Administration of Foreign Exchange (SAFE). This represents serious evidence of commitment. Historically, the Chinese government has been extremely cautious about opening up the capital account, so opening up RMB FDI into China is a major step – particularly in currently volatile currency markets where "hot money" is frequently switching location.

Based upon the details issued by MOFCOM, any FDI of less than RMB300m (approximately USD50m) can be approved at just the provincial level, without requiring case-by-case approval from MOFCOM headquarters in Beijing.[2] On a practical note, the changes bring RMB FDI very much in line with existing arrangements for FDI in foreign currencies, so there should be reasonable consistency in the application process across provinces. The actual application timeline will obviously depend upon the individual proposal, but a range of between one and two months would seem likely in the majority of cases.

2 *Certain restricted industries – such as shipbuilding, steel, cement and alumina – are excluded from the new RMB FDI measures.*

Restoring the Balance

Apart from their wider significance, these measures will also have a major effect in freeing up the offshore RMB market and stimulating further activity/liquidity. To date, an issue for many banks has been a plethora of RMB deposits, but extremely restricted channels in which to reinvest them. This has created significant balance sheet imbalances. RMB loan activity that might otherwise assist in rectifying this has also been extremely low, as overseas treasuries are predictably unwilling to borrow in what is widely perceived as a currency only likely to appreciate in the short- to medium-term.

By effectively creating a channel by which RMB accumulated in Hong Kong can flow back to the Mainland, this situation should improve substantially. Apart from enabling banks to increase their RMB transaction volumes in Hong Kong, the measures also open up a means for overseas investors and corporations to obtain substantially better rates of return than are currently available in Hong Kong in deposits and other instruments.

Timing

The timing of the RMB internationalisation drive could hardly be more felicitous for the Chinese government. With both the euro zone and the US mired in severe economic issues that have implications for their currencies, the opportunity for the RMB to make an initial claim to reserve status may never again be so good.

China's relative economic strength and the FDI-related initiatives recently announced are a sound basis for the RMB to become a credible alternative for international trade settlement, investment and as a reserve currency. Ultimately, this situation could be the precursor to a multi-polar currency regime consisting of USD, EUR and RMB.

Overseas Interest: Government

While some corporate treasuries may still be RMB sceptics, it is interesting to observe several major business centres taking a far more positive and proactive line. Hong Kong may be regarded as the natural home for offshore RMB activity, but both Taiwan and Singapore have recently expressed strong interest in also becoming offshore RMB centres. There have also been claims in the financial press that China is interested in supporting RMB trading in London.

If these possibilities actually become a reality, it will be a major step forward for RMB internationalisation. Nevertheless, even if this happens, two things still seem almost certain: any evolution of the RMB into a reserve currency is likely to be a marathon rather than a sprint, and Hong Kong will remain the primary offshore RMB centre for some time to come.

Hong Kong's dominance is understandable in the light of the close relationship between the PBOC and the Hong Kong Monetary Authority. This makes Hong Kong the ideal test bed for steps towards RMB internationalisation. At present, Hong Kong's focal position benefits the market as a whole by concentrating liquidity as it grows and extends along the yield curve. This situation effectively minimises hedging costs and inefficiencies for all types of participant, including corporate treasuries.

The critical point is that new centres must add to the total offshore RMB liquidity pool, rather than merely cannibalising existing Hong Kong liquidity. One credible possibility is some form of hub and spoke structure emerging, with Hong Kong as the hub and other satellite markets as the spokes. Markets such as London, New York, Singapore and Taiwan would trade with Hong Kong for offshore settlement.

Whatever the eventual outcome, it is nevertheless highly significant that governments around the world appreciate the implications of RMB internationalisation and wish to ensure their participation. The fact that they are prepared to state this publicly only serves as further positive third-party endorsement of RMB internationalisation.

Overseas Interest: Corporate

Apart from the possible commercial benefits, corporations outside the US and euro zone have an additional reason for adopting RMB settlement, which is increasingly reflected in market surveys. At present, these corporations will typically use a third-party currency for their China trade (usually the US dollar, but sometimes the euro). This involves an additional set of hedging costs, as two transactions are required rather than one. Switching to RMB settlement obviously removes one of these transactions, thereby reducing hedging costs.

It is intriguing to observe how this is increasingly reflected in survey responses, not just from multinationals, but also from small and medium-sized enterprises. A recent HSBC survey of these smaller entities highlighted a decided open-mindedness towards RMB settlement. More specifically, 57% of companies surveyed in Hong Kong said they would consider switching to RMB settlement or were actively interested in doing so.

Conclusion

While recent initiatives by the Chinese government and RMB internationalisation progress to date are definitely significant, it is important not to overstate the case. While there is clear evidence of sustained commitment to the programme by the Chinese authorities and equally clear evidence of enthusiastic market adoption, which continues to expand, this does not mean that the RMB will be a reserve currency tomorrow. It seems clear that this will happen at some point, but predicting any timeline requires a similar level of realism and pragmatism to that currently demonstrated by the Chinese government.

Market Realities

An interesting illustration of how far the RMB has already come in terms of internationalisation was 23 September 2011. The looming crisis in Europe triggered a selloff in Asian currencies including CNH (the Hong Kong offshore variant of the RMB, as opposed to its onshore counterpart, CNY).

While those anticipating continual CNH appreciation were doubtless discommoded, the Hong Kong market's overall reaction was a welcome indication of its stability. (Of course, those participants looking to buy CNH with which to pay onshore Chinese suppliers also benefited from cheaper CNH.) Despite the volatility during the trading session, the CNH market continued to function normally, thereby demonstrating the growing maturity of a market that is little more than a year old – behaviour that should reassure all participants.

The other important underlying point here is this was a timely reminder that market participants should not assume that RMB appreciation is a permanent one-way bet. CNH in the offshore market will behave in much the same way as any other freely convertible currency by being subject to the same ebbs and flows caused by fluctuating supply and demand.

Asia Pacific Payment Infrastructure: Open for Business

- Payment systems in Asia Pacific have changed significantly over the past decade.
- Payment infrastructure in individual countries is keeping pace with other economic initiatives, such as attracting foreign direct investment (FDI).
- A number of countries in Asia Pacific are following the trend of decline in use of paper payment instruments seen in developed markets.
- Support by central banks and regulators is expected to continue driving growth in electronic payments, but other environmental factors are also likely to play a part.

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In common with other regions around the globe, payment systems in Asia Pacific have changed significantly over the past decade. Various drivers, such as technological developments and consumer demand for greater choice and convenience, have contributed to this welcome trend. However, one of the most notable factors has been changing global transaction flow as companies have sought to extend and diversify their trading relationships. No longer is it just a case of West buying from East, as new South-South links are growing rapidly. Furthermore, countries such as China are preventing over-dependence on exports by encouraging the development of a domestic consumer market. The net result of all this activity has been an influx of advanced capabilities that has seen payment processing in the region move far beyond what was possible as little as five years ago.

This expansion and diversification of global trading relationships has raised the question in the minds of many central banks and regulators in Asia Pacific of whether or not their existing payment infrastructure is sufficient to support this new cross-border activity. This shift has also driven companies to rethink their approach to connectivity (the theme of this year's Guide) in order to make and receive payments from these new trading partners. Domestic corporations seeking to improve their own efficiency have put pressure on their banks in this regard. This is true particularly in the case of large corporations that appreciate that the streamlined financial connectivity required to achieve process efficiency will not be accomplished by legacy clearing methods. Within the financial industry, banks have increasingly found themselves experiencing competition from non-bank payment institutions, which has driven the banks to demand an infrastructure within which they can compete effectively.

Post-crisis Divergence

Another factor that has strongly influenced the evolution of payment infrastructures has been the financial crisis. This has affected how central banks and participating institutions work, as well as highlighting Asia Pacific as a comparatively resilient region in terms of economic activity. As a result, foreign direct investment (FDI) by both governments and corporates into Asia Pacific economies has increased in the past two years, which will ultimately have a positive impact on the general market environment.

The economic divergence between Asia Pacific and other more developed markets is certainly supported by the statistical evidence. Investment in Europe peaked in 2007 and has continued to decline since the financial crisis of 2008. By contrast, South East Asia and Pacific countries saw investment levels grow until 2008, dip in 2009, but then return to their 2007 levels.[1] Relatively speaking, these countries had a 9% share of global investment in 2007, but as of 2010 had a 21% share.

In view of these developments, it is only logical to expect the payment infrastructure in Asia Pacific to evolve to a level where it can adequately support this increased level of business activity. This is already being borne out in reality as central banks in the region are pushing ahead with enhancements in this area.

Paper: Still Present, But For How Much Longer?

Although paper and cheque transactions persist, there is considerable evidence of decline in use of paper payment instruments in developed markets.[2] A similar picture applies in other markets where the shift to electronic payment mechanisms is driving greater e-payment volumes and flat or declining cheque volumes.

A number of countries in Asia Pacific are following this trend. For instance, in Australia cheques accounted for less than 12% of value and 5% of volume of non-cash payments in 2010 – down from 17% (value) and 11% (volume) in 2005. Furthermore, the number of cheques written in 2009 was less than half that of 2000. In Korea, cheque volumes have declined by some 35% over the past five years, while in China the fall over the same period has been 25%.

Although India has seen its cheque volumes remain relatively flat, cheque payments are still the dominant payment mechanism in some small cities not covered by electronic payments systems and among small and medium enterprises. Nevertheless, the country has also experienced exceptional growth in electronic transactions. For example, the NEFT electronic clearing system started with overnight settlement capabilities, and as participating banks increased their technological capabilities, near real-time settlement (within two to three hours) has also been achieved. NEFT payments more than doubled between 2009 and 2010, with transaction volumes leaping from 32.2 million to 66.3 million. ECS, another e-payment system in India, saw its volumes increase from 88.4 million to 98.1 million. This growth disparity would seem to suggest that consumers have a preference for the quicker settlement times that NEFT can provide in comparison with ECS.

1 *World Bank Statistics.*
2 *Bank of International Settlements, Red Book, September 2011.*

Figure 1: Paper Versus Electronic Payments in Key Asia Pacific Markets

Payment Volumes (in Millions)	2006	2007	2008	2009	2010
Electronic					
Korea	1,949	2,212	2,360	2,464	2,667
Australia	1,654	1,788	1,922	2,030	2,172
Japan	1,361	1,398	1,402	1,415	not available
China	167	259	355	474	478
India	153	225	294	347	456
Hong Kong	80	98	86	92	97
Singapore	80	84	85	88	96
Cheques					
Korea	1,153	1,186	1,104	931	752
Australia	450	418	371	333	291
Japan	134	124	112	96	not available
China	1,189	978	882	876	897
India	1,367	1,460	1,397	1,379	1,381
Hong Kong	130	139	121	113	114
Singapore	83	85	83	78	77

Source: HSBC

Various factors are contributing to this electronic trend in the region, but the major point is that it benefits a broad range of participants. End users enjoy improved transaction settlement times, regulators obtain better visibility and control over the financial risk in payment settlement systems, and processing banks are able to benefit from lower costs through efficiencies and straight-through processing. In general, electronic payments require significantly lower resources to complete and facilitate automation and efficiency, which is obviously of importance to those large corporations and banks processing higher volumes of transactions.

Some regulators and central banks are encouraging electronic payments by making their use mandatory for certain categories of transactions. For example, in India the central bank has made it obligatory to route any payments greater than INR1m electronically. In Malaysia, the central bank also demands that payments among government and statutory bodies, capital markets and the insurance industry have to be made electronically. This sort of support by central banks and regulators is expected to continue driving growth in electronic payments, but other environmental factors are also likely to play a part.

Is Change Inevitable?

The manual handling, physical transportation and other processes involved in processing paper payment instruments make their relative inefficiency self-evident. In countries with a large geographical footprint and multiple clearing zones, clearing of paper instruments can easily take ten days and in some cases considerably longer. An additional irritant is the lack of certainty over timelines – will the cheque clear in three days or eight or 17? Central banks and regulators are well aware that this sort of situation is unattractive to overseas companies considering new business locations and can offset the effect of other measures intended to encourage FDI.

Nevertheless, the introduction of electronic payments is not without its challenges. In some countries, the threshold for low-value payments is still set at levels that push many electronic payments into the high-value clearing system, where the costs compare unfavourably with paper instruments. With multiple systems and various settlement times, on top of disparate pricing, customers running shared service centres and payment factories have found the current situation challenging. Lack of global and regional standards and multiple clearing system models have resulted in user experience variations by country, functional capabilities, data requirements and clearing/settlement rules (such as value dates and returns/rejections).

In a majority of Asia countries, there is no domestic electronic clearing facility for foreign currencies; hence, payments payees/recipients are often dependent upon correspondent banks to clear funds in a timely manner. These various considerations, to some extent, impede the transition in Asia Pacific towards electronic payments. The good news is that central banks and regulators in the region have strong competitive reasons for responding, while they also have the advantage of being able to review best practices already adopted in Europe/North America and implementing those that are affordable.

Cheque Truncation: The Way Ahead?

One of the most prominent examples of these best practices that is being implemented in various Asia Pacific countries is cheque truncation, which dispenses with the need for physical handling of cheques and is thus a welcome development. While long-term growth in electronic payments may be inevitable, introducing steps in the meantime to improve the efficiency of cheque clearing is clearly worthwhile.

There have been a number of cheque truncation initiatives in Asia Pacific recently, following in the footsteps of countries like Hong Kong and Singapore, which implemented cheque truncation in mid-2003, as well as Malaysia where the initiative went live in 2008. In India, the Cheque Truncation System (CTS) was implemented as a pilot project in the National Capital Region (Delhi) in February 2008. The roll-out of the project to other clearing centres (starting with Chennai) is already under way. Another country where this sort of project has now been completed is Korea, which initiated truncation of promissory notes and current account cheques exchanged through the Seoul Clearing House in late 2009, and has now completed its nationwide deployment.

Other countries in the region, such as Bangladesh and Thailand, have now also started their own cheque truncation projects:

- Bangladesh: In the past 12 months, Bangladesh's paper clearing system has moved from a completely manual interchange of paper cheques and reports to a national, fully automated, image-based cheque truncation system alongside the Bangladesh Electronic Fund Transfer Network (BEFTN). The Bangladesh Automated Cheque Processing System (BACPS) has gone live recently and is intended to revolutionise the processing of cheque payments in Bangladesh by reducing the payment cycle from around 21 days down to a few hours. In doing so, the process has been further improved by increasing security, traceability, and accountability. A central image archive is also provided so that member banks can enquire on their own items that have passed through the clearing system, which in turn allows them to provide improved customer service.

- Thailand: Bank of Thailand (BOT) started the Imaged Cheque Clearing and Archive System (ICAS) project in 2011 using advanced imaging technology to achieve fast and efficient cheque clearing. The old cheque clearing process, which required instruments to be transported between depositary banks and paying banks for verification before payment could be authorised, has been burdened by high operating and transportation costs.

Incentives and Infrastructure

An interesting trend in the migration to electronic payments in Asia Pacific has been the way that some central banks have started regulating the price that the issuing banks can charge for electronic payments. This is intended to promote the use of electronic payments by presenting them as an attractive alternative low-cost payment option. Specific examples of this have been India, which has done this for both its NEFT and RTGS system, Singapore, which has introduced this for its new G3 real-time payments, and Malaysia, where the threshold amount for low-value e-payment was increased. This has effectively converted previously high-value payments to low-value payments, thereby reducing costs and at the same time demonstrating increasing confidence in Malaysia's low-value payments system.

There have also been several prominent examples of countries making significant investment in clearing infrastructure in order to facilitate the move to electronic payments:

- Bangladesh: Bangladesh Bank (the central bank) launched the country's BEFTN on 28 February 2011, but at present is only permitting credit transactions on the platform among the 40 participating banks. However, once BEFTN is fully deployed, it will be able to process a wide variety of credit transfer applications, including payroll, foreign and domestic remittances, social security, dividends, retirement, expense reimbursement, bill payments, corporate payments, government tax payments, veterans' payments, government licences and person-to-person payments.

- Singapore: Singapore's G3 Real Time Payments (RTP) initiative has focused on two principal areas: real-time payments (low value RTGS) and bulk payments (ACH). RTP features include payer-to-beneficiary payment completion within five minutes (up to a maximum of SGD10,000) and payment completion within 15 seconds between participating banks, which are obliged to be able to receive and credit payments 24/7. The Singapore ACH for bulk payments has also been enhanced to provide support for additional details that will facilitate payment identification and invoice reconciliation.

- Thailand: Thailand has offered a direct debit service (ACH Debit) to cash management customers for nearly a decade. However, because it is available only by bilateral arrangement between certain foreign and local banks, the service is not widely used. The Bank of Thailand (BOT) is aware of this situation and now intends to deploy the system on a national level. A concrete timeline for this has not yet been published, but the objective is to devise a direct debit structure during 2012.

- India: The National Payments Corporation of India has undertaken a project to implement an ACH system focusing on the collections side. In due course the new centralised ACH solution is expected to consolidate the Electronic Clearing System (ECS) and provide a framework for the removal of local barriers/inhibitors and the harmonisation of standards/practices. This platform will have a national footprint that will cover more than 82,000 bank branches, and is expected to be launched in the first half of 2012.

Cross-border Solutions

As mentioned earlier, a common problem for many companies doing cross-border business in Asia has been the settlement of foreign currency payments. These either had to pay via cross-border remittance (costly, and requires supporting documents for countries with foreign exchange (FX) restrictions) or via an alternative route using foreign currency cheques, which is inconvenient and inefficient.

A number of countries have already responded to this challenge by introducing new clearing mechanisms for foreign currency payments. One of the most interesting examples of this is Thailand, where the authorities have partially relaxed FX restrictions by raising the value threshold above which supporting documentation for FX transactions is required from USD20,000 to USD50,000. They now also permit Thai companies holding export proceeds in foreign currencies to transfer funds from their foreign currency deposit accounts to counterparties in Thailand for payment of goods or services.

Developments intended to facilitate foreign currency payments are also underway in Korea and Hong Kong. Korea introduced a new domestic foreign currency remittance system in October 2010 that uses the Korea Financial Telecommunications and Clearing Institute (KFTC) network. The system operates on a real-time basis and is led by a consortium of banks (Kookmin Bank, Shinhan Bank, Woori Bank and Korean Exchange Bank). In Hong Kong, both real-time gross settlement and low-value payment systems have been introduced for renminbi (RMB). In addition to enabling the business community to transact in RMB, this development is also expected to cement Hong Kong's ambition to be a financial hub in the region.

Conclusion

The recent developments in payment infrastructure across Asia Pacific are clearly significant and it is encouraging to observe that central banks and regulators in the region appear committed to their long-term continuation. This is obviously advantageous for consumers and smaller companies, but larger corporations and multinationals have perhaps most to gain. With their increasing focus on automated connectivity and processing, Asia Pacific's migration towards electronic payments will deliver considerable large scale efficiencies for these larger corporations. In addition, the prospect of greater pan-regional transparency relating to payment activity will ultimately deliver major gains to corporate treasury, as tasks such as cash forecasting and timely investment/redeployment of surplus cash will become considerably easier and more effective.

Taking Control of Controls

Katharine Morton, Managing Editor, EuroFinance, UK

- Treasury is ideally situated to be the gatekeeper of corporate controls, however, there need to be good internal controls already in place.
- Fraud occurs when three elements of the fraud triangle are present – opportunity, rationalisation and pressure/incentive.
- Good corporate governance includes several aspects, from setting and implementing controls to accountability and enforcement.
- Policies that work best are those that are simple and well communicated.

Corporate governance is one of the classic hard-to-define elements of finance. Good corporate governance, like "mom" and "apple pie", is seen by all parties as a good thing. Bad corporate governance is frequently blamed, after the event, for all sorts of bad things. There are some smart frauds – and many more very simple ones. For treasurers, though, corporate governance, for all its nebulous qualities, is impinging on day-to-day treasury activities. The old "not my department" phrase isn't going to wash – not in the face of increasingly serious consequences for compliance or regulatory failure.

Not Just a Corporate Buzzword

In today's climate, investors and other stakeholders such as suppliers increasingly want comfort that your company is behaving in a transparent way. For example, telecommunications group Bharti Airtel has grown in a very short period of time from operating in just one country, India, to 19 – of which 16 are in Africa. "As a company, we promote transparency and corporate governance of the highest standards," says Bharti Airtel group treasurer Harjeet Kohli. "We believe good corporate governance to be the first eligibility criteria for seeking investors' help and attention." Kohli also heads investor relations at Bharti Airtel.

Corporate governance is not just some company-level buzzword but percolates down to each department including the central treasury and investor relations, Kohli adds. "Investors want complete transparency, detailed levels of disclosure. Our company is [possibly the only company on the globe] which does IFRS full-scope audit every quarter. We focus on corporate governance at all levels, be it accounts, internal procedures and their audit. As an example, our unit does a Sarbanes-Oxley audit on a voluntary basis."

What about those treasuries that are not front-line to investors and the capital markets? Is corporate governance still a treasury concern? "Treasury as the keeper of the cash is usually the final gatekeeper and the strongest line of defence, but prior to cash leaving the business many other internal controls have to come into play," says D'Shorne Human, compliance manager and country treasurer at Alstom Power in Johannesburg.

Setting and Implementing Controls

Alexandra Wrage, president of Trace International, a non-profit advisory association that works with companies to raise their anti-bribery compliance worldwide, points out, "Good governance boils down to controls. The board should know the company's tolerance for risk: you have to figure out your appetite for risk at different levels, and then set your controls accordingly."

> **Controls are in place to protect both the organisation and the individuals operating within the organisation.**
> **Adrian Bates, GlaxoSmithKline**

As Adrian Bates, assistant treasurer of operations at GlaxoSmithKline points out, "Controls are in place to protect both the organisation and the individuals operating within the organisation."

The difficulty comes with how well communicated and implemented those controls are. Wrage says, "We'll see a company with 'hard and fast' policies such as, 'No third-party suppliers can be paid without a written agreement in place and only after appropriate due diligence' – but then they don't synchronise that with AP [accounts payable]. Then AP goes and pays whatever comes in through the door: it's such a basic failure of control, but it happens all the time."

It's a relatively familiar story. As one treasurer relates, someone transferred a lot of money out of one of his company's master accounts. Who was it authorised by? Somebody with the same name, title and extension number as someone in the finance department. The only reason it was spotted at all was because a sharp-eyed person realised a Gmail account had been set up in that same name by someone with access to the company's telephone list.

Technology's Supporting Role

Could that have all been solved by good systems? Technology has certainly been a boon to some aspects of control. Many treasury management systems (TMS) take security as key. Corporate governance is seen as being built in. "It's helpful that you can only see what it is you can do within the system, which builds in a layer of security," says Bates at GlaxoSmithKline.

With TMS, and electronic bank account management (eBAM) and in-house compliance IT systems, there are other risks. "The pipeline may be completely secure, but every time you tap into or out of any system, control shifts to the access point, and away from where it should reside," says Wrage.

Early warning signs are useful to flag problems. Kohli at Bharti says, "Irrespective of varied levels of automation, all of the opcos [operating companies] do 'daily' cash reports to treasury. [This] allows a daily visibility for management decision-making and in the context of governance, allows early sign of any control issues that could lead to fraud and any other issues; early warning signs will inevitably show in analysing the daily cash reports."

The Fraud Triangle

What is best practice for finance departments when it comes to avoiding fraud and bribery? "We believe that fraud happens when three elements of the fraud triangle are present," says Human. Those three elements are opportunity, rationalisation and pressure/incentive:

- Opportunity is the circumstances that provide the chance to carry out a material misstatement in the financial statements.
- Rationalisation is an attitude or set of ethical values that allows one or more individuals to knowingly and intentionally commit a dishonest act, or a situation in which individuals are able to rationalise committing a dishonest act.
- Pressure or incentive can be on management or other employees materially to misstate the financial statements.

"A continuous effort is undertaken to attempt the reduction of these three elements by means of assessing the finance environment and implementing risk-based internal controls to minimise such potential exposures to an acceptable level," Human says.

> **Good corporate governance structures usually provide for a direct line to the head of internal audit for any concerned employee by means of anonymous tip-off or whistle-blower contact numbers.**
>
> **D'Shorne Human, Alstom Power**

What should be the reporting line for corporate governance? "Good corporate governance structures usually provide for a direct line to the head of internal audit for any concerned employee by means of anonymous tip-off or whistle-blower contact numbers," says Human. "For general reporting it is always good to have the basic independent review function and segregate conflicting duties in the processing and approval cycle. And in addition to this, a review is seldom useful unless the reviewer/approver has sufficient technical knowledge or experience to adequately assess the information/transaction presented to him or her."

Closing the Gaps

Good whistle-blowing systems are helpful. "People also need to be comfortable highlighting issues immediately," Kohli points out. "As we speak, with a widespread multi-country coverage, [the] treasury department is developing a whistle-blower policy for early escalation of issues. Our company rotates auditors – firms and individuals – every few years. Each operating company treasury unit has internal audits and we are now planning to institute peer audits, which apart from escalating governance and standards will also help replicate successful policies and practices across geographies and, of course, highlight any gaps expeditiously."

> **"... we are now planning to institute peer audits, which apart from escalating governance and standards will also help replicate successful policies and practices across geographies ..."**
>
> **Harjeet Kohli, Bharti Airtel**

Many multinationals operate under multiple corporate governance regimes. Alstom is no exception. In South Africa, Human believes that enforcement of good corporate governance is entrenched. "By implementing the guidance given in King III [South Africa's governance guidelines that have been incorporated into the new Companies Act], Sarbanes-Oxley and/or the Loi de Sécurité Financière [France's Financial Security Act, Alstom being a French-listed company], an appropriate internal control environment can be created which could be conducive to the reporting of accurate, valid and complete financial information. Continuous monitoring of these controls by bodies such as an audit committee via internal audit functions and the like can provide assurance that good corporate governance is still in force." He is quick to add, "There should be no question as to whether corporate governance can be enforced; it is imperative!"

Wrage at Trace International says that all it takes is an hour and a half or so for everyone to sit down and explain policies. But those policies do have to be simple. No fancy 400-page catch-all documents in legal jargon that nobody understands issued as diktat from on high with no explanations. It's the gaps between departments, between headquarters and the front line where the "bad guys" get through, particularly in challenging countries. "Good, well-run companies often have good policies within silos, but it's across the silos where breakdowns occur," she says.

Accountability and Enforcement

For bribery in particular, the bottom line is that once the opportunity for bribery has been established (often via interaction with an external player) somebody within the company has to generate enough money before they can pay the bribe. Those steps can include falsifying invoices and setting up shell companies. "The key is to follow the money. Bribery requires a transfer of something of value," Wrage says. Those fake invoices often involve payments for things that are difficult to dispute, such as translation fees or consulting fees or fake intermediary bank flows. "Fraudsters aren't very imaginative," she quips.

In almost every case where Wrage sees outbound bribery, there is inbound theft (embezzlement). That's particularly so where third parties have commissions as incentives. It's not always the big-ticket multi-million deals with kickbacks that are the main issue. One company undertook an exercise to extrapolate the small "agency commission" bribes across its entire organisation and found that the little frauds added up to USD20m. The exposure to risk is equally worrying. For every country that has anti-bribery laws, there exist penalties, including death.

The old Confucian saying, that the fish rots from the head, applies to corporate governance too – and it's not that authorities will simply be focused on anyone buying fake invoices from a dealer in a kiosk in, say, Shanghai. They will be more concerned with the manager supervising and signing off on them, and their manager too. The authorities will always go for the biggest possible fish they can. How do you enforce corporate governance and who gets the stick, even if unfairly? "The ultimate responsibility for implementing good corporate governance rests with the directors of the company (legal entity in the country), being the ones accountable to the shareholders for their investments," says Human.

Keeping it Simple

There is only a finite amount of information you can gather about third parties whether they are contractors or suppliers. Intelligence agencies have a word for getting to the bottom of checking your counterparty: "humint" (human intelligence) gathering. For every system, it needs somebody to talk to somebody else, and make a judgement.

> **... the key is for the company to identify the gaps and work to fill them. This isn't complex stuff. Find out where it originates, follow it through, and find where it ends.**
>
> **Alexandra Wrage, Trace International**

"People make a lot of money making things more complicated and procedures more elaborate than they need to be in relation to the risk posed," says Wrage. After all, there's a whole industry around it, finding problems and fixing them. "There aren't any companies operating in more than 100 countries without some problems, but the key is for the company to identify the gaps and work to fill them. This isn't complex stuff. Find out where it originates, follow it through, and find where it ends."

After all, to avoid paying the lawyer (billing at USD750 an hour) who asked one company for 10 years of email traffic in order to find problems, it's got to be worth having simple controls in place.

In sum, keep it simple, modest, and easy to communicate to everybody. No weird and complicated controls for their own sake. And anyway, that 400-page document that nobody has read? You can bet that if there is a fraud, and your company falls short of the processes that have been elaborately laid out in it, it will be held up as evidence of "bad controls".

A version of this article appears in *Treasury Perspectives* (www.treasuryperspectives.com), a EuroFinance publication.

Market Analysis

Market Analysis: Introduction

The following pages contain an introductory guide to the cash management environment in 19 countries and territories in Asia Pacific: Australia, Bangladesh, Brunei, China, Hong Kong SAR, India, Indonesia, Japan, Korea, Macau SAR, Malaysia, Mauritius[1], New Zealand, the Philippines, Singapore, Sri Lanka, Taiwan, Thailand and Vietnam. For the purposes of this guide, "Asia Pacific" is defined as the abovementioned 19 markets.

Each market analysis includes some basic facts and trade statistics. Unless otherwise indicated, the data sources are:

- For population, gross domestic product (GDP) and inflation rate: The International Monetary Fund's World Economic Outlook database, September 2011 edition. GDP has been calculated using the purchasing-power parity method and is denominated in current international dollars[2], while inflation rates are based on average consumer prices.[3]
- For total exports, total imports, total trade and total trade with Asia: The International Monetary Fund's Direction of Trade Statistics online database, accessed 15 November 2011. Exports are calculated using free on board (FOB) prices; imports are calculated using cost, insurance and freight (CIF) prices.[4]
- For major exports, major imports, major markets and major suppliers: The World Trade Organization's Trade Profiles, October 2011 edition.
- For the clearing systems holidays 2012 list: All public holiday information – including dates and spellings – has been obtained from public notifications issued by the respective government authorities.

The information provided is accurate as of 15 November 2011.

If you have any questions about cash management or trade and supply chain in any of these markets, please contact HSBC; local contact details are shown at the end of each market analysis.[5]

1 *Mauritius is included due to its status as a key offshore financial centre for emerging Asian nations (i.e. India) and Africa.*
2 *The current international dollar is a hypothetical unit of currency that the World Bank defines as having the same purchasing power over GDP as a US dollar has in the US. Therefore, an international dollar would buy in the cited country a comparable amount of goods and services that a US dollar would buy in the US.*
3 *The statistics for Macau have been obtained from the Statistics and Census Service of Macau (www.dsec.gov.mo/e_index.html). The gross domestic product figures have been calculated using current prices and are in US dollars.*
4 *The statistics for Taiwan have been obtained from the Taiwan government's Bureau of Foreign Trade (eweb.trade.gov.tw).*
5 *The market analysis in this section is provided for general informational purposes only. Although the information has been gathered from sources generally believed to be reliable, HSBC accepts no responsibility as to its accuracy and completeness. Please seek professional confirmation before taking any action based on the information contained herein.*

Market Analysis: Australia

Overview	
Population	22.2 million (2010)
Total area	7,692,024 sq km
Capital	Canberra
Major language(s)	English
Time zone	GMT + 10 hours
Currency	Australian Dollar (AUD)
Central bank	The Reserve Bank of Australia
Gross domestic product (GDP)	883.8bn (2010); 1.2% real growth rate (2010 est.); 39,764 per capita (2010)
Inflation rate (consumer prices)	2.9% (2010)

Trade			
Total exports	USD211.8bn f.o.b. (2010)	Total imports	USD214.2bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 12.7% Fuels and mining – 61.1% Manufactured – 12.6% (2010)	Major imports (% by product group)	Agricultural – 5.9% Fuels and mining – 15.3% Manufactured – 72.3% (2010)
Major markets (% of total)	China – 25.3%, Japan – 18.9%, Korea – 8.9%, European Union – 7.9%, India – 7.1% (2010)	Major suppliers (% of total)	China – 18.7%, European Union – 18.3%, US – 11.1%, Japan – 8.6%, Thailand – 5.2% (2010)
Total trade	USD426.0bn (2010)	Total trade with Asia	USD284.4bn (2010)

Banking System and Bank Accounts

- The central bank of Australia is the Reserve Bank of Australia (RBA), which is responsible for monetary policy. Other significant RBA roles include maintaining financial system stability and promoting the safety and efficiency of the payments system.
- As of November 2010, there were 58 banks active in Australia with four main domestic banks: National Australia Bank Ltd, Australia & New Zealand Banking Group Ltd, Westpac Banking Corporation and the Commonwealth Bank of Australia.

- The following types of bank accounts are currently available:

Account type	Local current[1]	Local savings	Foreign current[2]	Foreign savings
Resident	Yes	Yes	No	Yes
Non-resident	Yes	Yes	No	Yes
Credit interest	Yes	Yes	No	Yes

1. Cheque books are optional.

2. Cheque books are not available on foreign currency accounts.

Clearing Systems and Payment Instruments

- There are four major payment clearing systems in Australia:

Clearing system	Comments
Australian Paper Clearing System (APCS)	APCS is an automated clearing house for cheques, payment orders and other paper-based payment instructions.
Bulk Electronic Clearing System (BECS)	BECS manages the conduct of exchange and the settlement of bulk electronic low-value transactions in a similar fashion to the paper-based instructions in APCS.
Consumer Electronic Clearing System (CECS)	CECS is for proprietary card-based automated teller machine (ATM) and electronic funds transfer at point of sale (EFTPOS) transactions.
High-Value Clearing System (HVCS)	HVCS is integrated with the real-time gross settlement (RTGS) clearing system. HVCS is for high-value electronic payment instructions.

- In Australia, there is only one clearing zone. Cheques are processed overnight for credit to the account with funds held for a minimum of three working days. Interest is calculated on the balance of the account and therefore earns interest for deposited funds even though they have not cleared.

Legal, Company and Regulatory

- Australia has nine legal systems – the eight state and territory systems and one federal system.
- The primary regulatory bodies that regulate financial services in Australia are:
  - The Australian Prudential Regulation Authority (APRA), which undertakes prudential supervision of deposit-taking institutions, insurance and superannuation funds;
  - The Australian Securities and Investments Commission (ASIC), which is responsible for market integrity, consumer protection and corporations; and
  - AUSTRAC is responsible for customer identification, reporting, record keeping and other requirements under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006. It receives information on the movement of cash and other forms of payment in and out of Australia.

Liquidity, Currency and Tax

- There are no restrictions on currency movements or cash concentration in Australia; notional pooling and cash concentration are permitted on a single and/or multi-currency basis. Functionality depends upon banking partner capability, but more developed banks can offer fully automated cash concentration solutions and (for notional pooling) considerable flexibility in determining interest rates applicable to participating accounts.
- Australia does not have an active commercial paper market, therefore treasuries looking for more than just the overnight cash rate on surplus liquidity tend to use term deposits.
- Offshore companies will incur withholding tax as per non-residents in the table below.

Tax	Comments
Interest withholding tax	• Residents: 46.5% without tax file number, Australian business number, or tax exemption certificates. • Non-residents: 10% flat rate – no tax-free threshold applies for non-residents.
Corporate tax	30%
Value-added tax or equivalent	A goods and services tax (GST) applies in Australia at the rate of 10% on the price of taxable supplies. Since most of the banks' products are "financial supplies", no GST should apply in the majority of cases. However, there are a few products supplied by banks, which are "taxable supplies" and will attract GST.

Market Watch

No recent or anticipated change of significance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	2 January*
Australia Day	26 January
Good Friday	6 April
Easter Monday	9 April
Anzac Day	25 April
Queen's Birthday	11 June
Christmas Day	25 December
Boxing Day	26 December

** Substitute public holiday because 1 January is a Sunday.*

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HSBC Trade and Supply Chain Tel: [61] (2) 9006 5100 E-mail: tradeandsupplychain@hsbc.com

Market Analysis: Bangladesh

Overview	
Population	164.4 million (2010)
Total area	143,998 sq km
Capital	Dhaka
Major language(s)	Bengali and English
Time zone	GMT + 6 hours
Currency	Taka (BDT)
Central bank	Bangladesh Bank
Gross domestic product (GDP)	260.5bn (2010); 0.4% real growth rate (2010 est.); 1,585 per capita (2010)
Inflation rate (consumer prices)	8.1% (2010)

Trade			
Total exports	USD14.6bn f.o.b. (2010)	Total imports	USD27.8bn c.i.f. (2010)
Major exports (% by product type)	Agricultural – 5.3% Fuels and mining – 1.3% Manufactured – 93.3% (2010)	Major imports (% by product type)	Agricultural – 21.5% Fuels and mining – 9.8%, Manufactured – 68.0% (2010)
Major markets (% of total)	European Union – 51.2%, US – 25.7%, India – 4.0%, China – 3.5%, Canada – 1.7% (2010)	Major suppliers (% of total)	China – 15.6%, India – 13.2%, European Union – 9.7%, Kuwait – 7.2%, Indonesia – 5.1% (2010)
Total trade	USD42.4bn (2010)	Total trade with Asia	USD14.0bn (2010)

Banking System and Bank Accounts

- Bangladesh Bank (BB) is the central bank of Bangladesh. It has legal authority to supervise and regulate the banking sector and issue the country's currency. It also formulates and implements monetary policy and manages foreign exchange (FX) reserves.
- The banking system of Bangladesh consists of BB as the central bank, four state-owned commercial banks (which hold 22% of the industry's assets and 30% of deposits), five government-owned specialised banks, 30 domestic private banks and nine foreign banks.

- For locally incorporated companies, the opening of a bank account requires the following documentation:
  - board resolution;
  - certified copy of the company's memorandum and articles of association;
  - copy of the company's certificate of incorporation;
  - trade licence;
  - tax identification number;
  - complete account opening form with signature card;
  - list of directors with address (if not included in the memorandum of association);
  - Form XII;
  - transaction profile;
  - address verification documents (phone, gas, electricity bill, etc.);
  - photographs, legal photo identification documents and Personal Information Forms of all signatories, directors, principal shareholders and beneficial owners: and
  - other mandatory documents required for particular types of businesses/signatories, e.g. a non-governmental organisation (NGO) needs NGO Bureau approval, an expatriate wanting to work locally needs a work permit, etc.
- In the case of foreign corporations, the board resolution, company's memorandum and articles of association, certificate of incorporation and list of directors must be attested by the Bangladesh High Commission (Embassy) from the corporation's country of origin.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	Yes[1]	No
Non-resident	Yes	Yes	Yes	No
Credit interest	No	Yes	Yes[2]	No

1. Can only be opened subject to travel history and local exchange control regulations, and with special permission from BB.

2. Interest applicable only on non-resident foreign currency term deposit accounts and resident foreign currency accounts.

3. Customers may open a short notice deposit account, which is an interest-bearing current account, subject to regulations from the central bank, about seven days' withdrawal notice for earning interest.

- Non-resident BDT accounts can be opened by companies resident outside Bangladesh, subject to adherence to guidelines of BB.

Clearing Systems and Payment Instruments

Clearing system	Comments
BB clearing houses	Operate in Dhaka and BB branches in seven other cities.
Sonali Bank's clearing houses	Operate in 31 towns where there are no BB branches.
BB large-value cheque settlement system	For items with value BDT500,000 and above (same-day clearing and clearable within specific clearing area).
BB foreign currency clearing system	Based in Dhaka – clears and settles foreign currency cheques and pay orders.

(table continues)

Bangladesh Electronic Fund Transfer Network (BEFTN)	A platform for settlement of transactions initiated through the BEFTN.

There are also a limited number of clearing systems in upcountry rural locations. In these collection areas, beneficiary bank representatives physically take cheques to the drawee bank for clearing. If cheques are deposited on Day D, clearing through clearing systems will be completed on Day D+1. Upcountry collection cheques will clear between Day D+3 and Day D+5.

Legal, Company and Regulatory

- Apart from BB, other important regulators include the Board of Investment, which handles applications relating to foreign direct investment, the Register of Joint Stock Companies (RJSC), which handles the creation of new companies, the National Board of Revenue (the tax authority) and The NGO Affairs Bureau (NGOAB).
- Operating a foreign company as a branch or liaison office in Bangladesh requires permission. Applications involve submitting a range of information to the Board of Investment, including:
    - corporate details, such as name, address, nationality, place of incorporation;
    - shareholding details, including authorised capital, paid-up capital (equity/preference), directors' details, shareholders' details and nationality;
    - nature of business activity – whether trading, commercial, industrial, consultancy, etc.;
    - details of any existing government permission to operate business;
    - address where business will operate;
    - target date of operation and the period for which permission is sought;
    - sources of financing for the proposed business;
    - whether any surplus earnings will be remitted abroad;
    - proposed organisation set up with details of any foreign personnel to be employed and details of government approval for their employment; and
    - any other information as required by the Board of Investment

Liquidity, Currency and Tax

- Single currency domestic cash concentration is allowed, but this can only be done for accounts held with HSBC Bangladesh. Cross-border cash concentration is not allowed.
- Typical local investment instruments for surplus liquidity include short-term deposits, time deposits and notice accounts.
- Outward remittance of foreign currency is highly regulated by BB and FX hedging instruments are not available.
- Corporate income tax is levied at 37.5% (for some sectors, the tax rates are slightly different). A 10% withholding tax on interest earned and an excise duty is applied to all bank accounts. No distinction is made between offshore and onshore accounts.
- A 15% value-added tax is levied on all banking services charges/commission earned.

Market Watch

- BB has undertaken a project to modernise the country's payments and clearing system, known as the Bangladesh Automated Clearing House (BACH).
- BACH will be implemented in two phases:
    - Phase 1 – Bangladesh Automated Cheque Processing System (BACPS)
    - Phase 2 – Bangladesh Electronic Fund Transfer Network (BEFTN).

- Phase 1 (BACPS) has been implemented and went live in Bangladesh in November 2010. The main features of BACPS are the adoption of a new cheque design standard with a magnetic ink character recognition (MICR) code line and the exchange of cheque-image and data instead of paper cheques for the purpose of clearing and settlement.
- Phase 2 (BEFTN) has been implemented and went live on 28 February 2011, which has enabled electronic fund transfers between accounts held with different banks. Through the BEFTN, upon receiving customer instructions, banks can send electronic data to BACH for both credit and debit operations. Banks can also use BEFTN for bank-to-bank payments. Currently, only BDT accounts can use the BEFTN.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Eid-e-Miladunnabi*	5 February
Shaheed Day and International Mother Language Day	21 February
Birthday of the Father of the Nation Bangabandhu Sheikh Mujibur Rahman	17 March
Independence Day and National Day	26 March
Bangla New Year	14 April
May Day	1 May
Buddha Purnima*	4 June
Bank Holiday	1 July
Shab-e-Barat*	6 July
Janmashtami	9 August
National Mourning Day	15 August
Shab-e-Quadr*	16 August
Eid-ul-Fitr*	19-21 August
Durga Puja	24 October
Eid-ul-Azha*	26-28 October
Ashura*	25 November
Victory Day	16 December
Christmas Day	25 December
Bank Holiday	31 December

** Subject to appearance of the moon.*

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Market Analysis: Brunei

Overview	
Population	417,000 (2010)
Total area	5,765 sq km
Capital	Bandar Seri Begawan
Major language(s)	Malay, English, Mandarin and other Chinese Dialects
Time zone	GMT + 8 hours
Currency	Brunei Dollar (BND)
Central bank	Autoriti Monetari Brunei Darussalam (AMBD)
Gross domestic product (GDP)	20.2bn (2010); 0.02% real growth rate (2010 est.); 48,333 per capita (2010)
Inflation rate (consumer prices)	0.4% (2010)

Trade			
Total exports	USD8.3bn f.o.b. (2010)	Total imports	USD3.1bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 0.1% Fuels and mining – 96.4% Manufactured – 3.3% (2010)	Major imports (% by product group)	Agricultural – 17.2% Fuels and mining – 3.0% Manufactured – 79.3% (2010)
Major markets (% of total)	Japan – 30.6%, Indonesia – 19.8%, Korea – 15.1%, Australia – 12.2%, US – 6.7% (2010)	Major suppliers (% of total)	Malaysia – 21.6%, Singapore – 17.4%, Japan – 12.8%, European Union – 10.8%, US – 9.0% (2010)
Total trade	USD11.4bn (2010)	Total trade with Asia	USD10.6bn (2010)

Banking System and Bank Accounts

- The Autoriti Monetari Brunei Darussalam (AMBD) was established in January 2011 and acts as the Central Bank of Brunei.
- Brunei currently has a total of eight banks; two local and six foreign.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings[1]	Foreign current[2]	Foreign savings
Resident	Yes	Yes[3]	Yes[2]	Yes[3]
Non-resident	Yes	Yes[3]	Yes[2]	Yes[3]
Credit interest	No	Yes[3]	No	Yes[3]

1. Subject to approval.

2. Overdrafts are not permitted and cheque books are not available for foreign currency current accounts.

3. Statement saving accounts only.

Clearing Systems and Payment Instruments

- A popular domestic payment instrument in Brunei is the cashier's order; in the absence of a central clearing system, the banks meet daily at the HSBC offices where these orders are exchanged. Clearing typically takes two or three days. Cheques are also commonly used and have the same clearing period, unless the payer and receiver use the same bank, in which case, value is same-day. Telegraphic transfers and drafts are also available.
- The manual nature of the clearing process means that an early daily cut off time of 9:30am is necessary; any payments arriving after that time are processed on the following business day.

Legal, Company and Regulatory

- The AMBD is responsible for the regulation, licensing and general supervision of all financial institutions in Brunei as well as the formulation and implementation of monetary policies and the regulation of currency issuance and guidelines.
- There are few restrictions on the type of business that can be set up in Brunei. However, businesses considered as affecting public interests directly – such as banks, finance companies, money lenders and travel agents – must obtain special licences from the appropriate government authorities. All companies with businesses in Brunei must be registered with the Registrar of Companies and have a registered place of business.

Liquidity, Currency and Tax

- Liquidity management techniques such as notional pooling or cash concentration are not generally practised, even on an in-country basis.
- There are no exchange control laws in Brunei. Previous legislation was repealed in 2000.

Market Watch

No recent or anticipated change of significance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year 2012	2 January
Chinese New Year	23 January
Prophet Muhammad's Birthday Anniversary	6 February
28th National Day	23 February
Royal Brunei Armed Forces Anniversary	31 May
Isra' Mi'raj*	18 June
Bank Half Yearly Closing	30 June
His Majesty's 66th Birthday	16 July
1st Day of Ramadhan*	21 July
Anniversary of Revelation of Al-Quran*	6 August
Hari Raya Aidil Fitri*	20-21 August
Hari Raya Aidil Adha*	27 October
1st Day of Muharram 1434*	15 November
Christmas Day	25 December
Bank Year-end Closing	31 December

** Subject to change.*

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Market Analysis: China

Overview	
Population	1.3 billion (2010)
Total area	9.60 million sq km
Capital	Beijing
Major language(s)	Putonghua (Mandarin)
Time zone	GMT + 8 hours
Currency	Renminbi (RMB)
Central bank	The People's Bank of China
Gross domestic product (GDP)	10,119.9bn (2010); 13.6% real growth rate (2010 est.); 7,544 per capita (2010)
Inflation rate (consumer prices)	3.3%

Trade			
Total exports	USD1.6tr (2010)	Total imports	USD1.4tr (2010)
Major exports (% by product group)	Agricultural – 3.3% Fuels and mining – 3.0% Manufactured – 93.6% (2010)	Major imports (% by product group)	Agricultural – 7.8% Fuels and mining – 26.7% Manufactured – 64.1% (2010)
Major markets (% of total)	European Union – 19.7%, US – 18.0%, Hong Kong – 13.8%, Japan – 7.7%, Korea – 4.4% (2010)	Major suppliers (% of total)	Japan – 12.6%, European Union – 12.0%, Korea – 9.9%, Taiwan – 8.3%, Hong Kong – 7.6% (2010)
Total trade	USD3.0tr (2010)	Total trade with Asia	USD1.2tr (2010)

Banking System and Bank Accounts

- The People's Bank of China (PBOC) is the central bank of China. Its main aim is to formulate and implement monetary policy and to safeguard financial stability. The PBOC also regulates interbank lending and bond markets.
- The banking sector is dominated by the "Big Four" state-owned banks: Industrial and Commercial Bank of China, China Construction Bank, Bank of China and Agricultural Bank of China. By the end of the five-year transitional period since China's entry to the World Trade Organization, many of the

barriers to foreign bank operations in China have been removed. With local incorporation, foreign global banks, e.g. HSBC, Citigroup, Standard Chartered Bank and Deutsche Bank, etc. have made significant direct investments in China.

- A resident company is allowed to open one basic RMB account and, in principle, as many general RMB accounts as it wishes. General accounts cannot be used for cash withdrawal and payroll.
- Types of foreign currency accounts: There are various regulatory requirements applicable to the opening and operation of foreign currency accounts. Different types of foreign currency accounts are opened for different purposes, and the operation of these accounts is subject to regulatory restrictions in relation to these specific purposes.
- The following types of bank accounts are currently available:

Foreign account types	Inflows	Outflows	Comments
Capital account	To receive capital injections and capital increases	Payments for current account items and approved capital expenditure	In principle, only one account can be opened with a bank located in the same region as the company and is subject to State Administration for Foreign Exchange (SAFE) approval
Settlement account	Collections for foreign currency current items (i.e. goods-trade and/or service-trade related items)	Current account items and items approved by SAFE	No SAFE approval is required
Foreign debt special account	To receive loan proceeds from overseas	As specified in the loan agreement, but cannot be used to repay RMB loans	Foreign debt registration and SAFE approval required for account opening
Foreign debt special loan repayment account	Transferred from other foreign currency accounts, or conversion from RMB	Repayment of the foreign currency loan principal and interest	Foreign debt should be repaid through a foreign debt special account, unless otherwise approved by local regulators
Foreign currency loan account (including loan account and repayment account)	To receive the loan proceeds from onshore foreign currency loans by banks or through entrusted loans	Usage of loan is subject to loan agreement	In principle, conversion to RMB is not allowed unless otherwise approved by SAFE
Foreign investment special account (applicable to foreign companies)	To temporarily receive funds related to direct China investment	Payment of expenses and anything associated with direct investment in China.	• One account only. SAFE's approval is required for account opening • Used for designated

(table continues)

		SAFE's approval is required for each payment and conversion	purpose and every transaction requires SAFE approval • Unused funds can either be transferred to the respective capital account (when a correspondent foreign invested entity is set up) or paid out to the foreign investor

- The following types of bank accounts are currently available:

Account type	RMB accounts	Foreign accounts
Resident	Yes	Yes
Non-resident	Yes (Upon approval by PBOC)	Yes

- All resident accounts are interest bearing. Details of RMB and foreign currency accounts are as follows:
  - RMB deposits: The ceiling interest rates are promulgated by PBOC.
  - Foreign currency deposits: The ceiling interest rates are promulgated by PBOC for short-term deposits (current account, 7-day call deposit, 1/3/6/12 months time deposit) with amounts less than USD3m or equivalent and USD, YEN, EUR or HKD as deposit currencies. Otherwise, favourable interest rates can be offered to customers at the bank's sole discretion.
- Non-resident accounts:
  - RMB deposits: The interest rate promulgated by PBOC for RMB current account deposit shall apply for non-resident RMB accounts of all tenors.
  - Foreign currency deposits: The exact offered rate is at the bank's sole discretion.

Clearing Systems and Payment Instruments

Local RMB payment

- The China National Advanced Payment System (CNAPS) is the main clearing system for RMB settlement in China, which comprises a high-value payment system (HVPS) and a bulk electronic payment system (BEPS):
  - HVPS: This is a real-time gross settlement system that has covered all cities in China since June 2005. Payments made via HVPS between the banks with direct membership can take a few seconds or minutes, regardless of their geographic locations. CNAPS HVPS has become the most popular and important clearing channel in China. There is no amount limit via HVPS.
  - BEPS: This is a low-value clearing system (similar to an automated clearing house or general interbank recurring order) that has been implemented throughout China since 2006. It uses the CNAPS architecture and caters to ordinary credit and debit transactions as well as bulk payments and collection processing with transaction amounts of no more than CNY50,000. As with HVPS, BEPS caters to both in-city and cross-city transactions.
- In-city local clearing systems: HSBC also has membership of most of the local clearing systems where it has a presence. Hence, HSBC can provide customers with access to the in-city clearing

houses to facilitate low-cost in-city clearing. This is particularly crucial if the customer has a lot of in-city payments/collections.

- In China, there are numerous instruments that can be used for in-city and cross-city payments, as well as underlying clearing mechanisms that will determine how quickly and efficiently funds will be credited to recipients' bank accounts.

RMB payment	Priority	Amount	Selected channel
In-city	Low	No more than CNY50,000	BEPS / Local clearing system
		Any amount	Local clearing system
	High	Any amount	HVPS
Cross-city	Low	No more than CNY50,000	BEPS
		Any amount	Bank draft/cheque
	Low/High	Any amount	HVPS

RMB cross-border payment

RMB payment	Destination	Selected channel
Outward payment	To overseas account	Telegraphic transfer
	To domestic account	CNAPS – HVPS
Inward collection	From overseas account	Telegraphic transfer
	From domestic account	CNAPS – HVPS

International and domestic foreign currency payment

- For international and domestic foreign currency payments, the following clearing channels are available for payments in China:

Foreign currency payment	Currency	Telegraphic transfer	Agent bank clearing	Foreign currency real-time gross settlement
Overseas	Australian dollar, Canadian dollar, Danish kroner, euro, Hong Kong dollar, Singapore dollar, sterling, Swedish krona, Swiss franc, US dollar, Japanese yen, Malaysia ringgit, Russian ruble and Norwegian krona	Yes	No	No

(table continues)

Cross-city	Australian dollar, Canadian dollar, Danish kroner, euro, Hong Kong dollar, Singapore dollar, sterling, Swedish krona, Swiss franc, US dollar and Japanese yen, Malaysia ringgit, Russian ruble and Norwegian krona	Yes	Australian dollar, euro, Canadian dollar, Hong Kong dollar, Singapore dollar, sterling, US dollar and Japanese yen	No
In-city	Hong Kong dollar and US dollar	Yes	Yes	No
	Australian dollar, Canadian dollar, euro, Singapore dollar, sterling and Japanese yen	Yes	Yes	No
	Other currency	Yes	No	No
In-city real-time gross settlement	Hong Kong dollar, US dollar and euro (subject to local clearing system capability)	No	No	Yes (Shenzhen, Ningbo and Suzhou only)

Legal, Company and Regulatory

- The China Banking Regulatory Commission (CBRC) formulates supervisory rules and regulations governing banking institutions, while the State Administration of Foreign Exchange (SAFE) is the government bureau in charge of China's balance of payments and foreign exchange positions.

Liquidity, Currency and Tax

- Direct inter-company financing is strictly prohibited in China while an entrusted loan is the only instrument available to facilitate indirect inter-company financing. Essentially, an entrusted loan is a mechanism whereby a Chinese legal entity can borrow/lend money from/to another Chinese legal entity, through a financial institution as an intermediary. Entrusted loans are the main foundation for building up domestic cash concentration solutions.

- The practice of planning and managing working capital domestically through RMB cash concentration techniques has been widely accepted. The focus of concentration has changed from the traditional needs of concentrating all cash positions at pool header to the efficient use of internal cash while minimising potential tax liabilities.
- The domestic foreign currency cash concentration solution, which shares the same mechanism as the RMB pair, has become more focused recently and requirements have been relaxed rapidly, especially since the new regulations promulgated by SAFE in 2009. Unlike the RMB pair, domestic foreign currency cash concentration is subject to SAFE approval.

- Key cash concentration tax considerations include:
  - Stamp duty: In a cash concentration agreement, the pool header company sets up a revolving credit facility for a bilateral entrusted loan relationship with each subsidiary. The borrower (the pool header company or subsidiaries) can borrow or lend as much as it wishes as long as the amount is within the revolving credit facility during the prescribed period. All participants, including commercial banks, pay stamp duty according to the amount of the revolving credit facility at the time the cash concentration master agreement was signed. The current domestic stamp duty for such contracts is 0.005%.
  - Business tax: In cash concentration, there are typically deposits and withdrawals of the entrusted loans taking place every day between the pool header company and subsidiaries. Business tax is normally 5% with surtax of 0.05% to 0.10% levied on entrusted loan interest income.
  - Corporate income tax: Any interest earned from an entrusted loan involved in cash concentration is subject to corporate income tax, which is standardised at 25% throughout the country. The interest cost due to the entrusted loan may not be deducted from taxable income if the ratio of affiliate loan to owners' equity exceeds the prescribed limit that is stipulated in Article 46 of the Corporate Income Tax Law of China or the interest rate of entrusted loan exceeds the correspondent bank lending of the same loan tenor. As of now, the aforementioned ratio is set as 5 for financial institutions (FI) and 2 for non-FI corporates.
- Apart from the tax mentioned above, other tax considerations include the following:
  - A Chinese resident company is liable for income tax on its worldwide income. Non-residents are liable for income tax on Chinese-sourced income.
  - Information on loans, interest and related expenses has to be disclosed and reported when filing annual tax returns.
  - Withholding income tax is imposed at 10% for non-resident companies, unless a double tax treaty offers a lower tax rate.

Cash repatriation from China

- SAFE has eased restrictions on offshore lending:
  - The move is aimed at encouraging enterprises set up in China with capital strength to make additional investments offshore.
  - Eligible companies may extend foreign exchange (FX) loans to offshore borrowers via direct lending or entrusted loans.
  - It reduces the requirements for offshore lending, expands sources of funds, and simplifies verification and remittance of offshore lending.

Applicable SAFE regulations	SAFE Regulation No. 24 issued on 9 June 2009	SAFE Shanghai Regulation No. 32 issued on 8 March 2010
Domestic lender	Incorporated in China	Member of foreign invested multinational corporation (MNC) group and registered in Shanghai Pudong New District
Overseas borrower	Subsidiaries or joint-stock enterprises of domestic lender	Member of same MNC group (e.g. parent of domestic lender or affiliate companies)

■ Traditional cash repatriation methods from China in accordance with different business types:

Method	Key documentation required	Other considerations	Frequency
Dividend repatriation	• Audit report • Capital verification report • Board resolution for dividend declaration • Corporate income tax duly paid	• With distributable profits • Registered capital paid on time • Prior year losses set off • Last year's interim dividend possible but not common	Once a year (or twice at most)
Service fees (not relating to intangible assets)	• Service agreement • Invoice • Tax clearance certificate	• Registration of agreement normally not required • Clearance with tax bureaus required • Management fee may not be tax deductible	No restriction
Repayment of shareholder loan	• Loan agreement registered with SAFE • SAFE approval for loan repayment • Tax clearance certificate for loan interest	• SAFE approval for repayment of loan principal and interest required • Loan repayment should abide by terms of loan agreement	In accordance with relevant terms of loan agreement
Trade between overseas and People's Republic of China (PRC) entity	• Sales and purchase agreement • Invoice • Customs declaration documents • Other supporting documents required by SAFE per business type	Registered in the list of "Eligible customers for outward payment due to import business".	No restriction
Royalty payments/ technical service fees	• Licensing agreement • Invoice • Approval or registration certificate issued by PRC authorities • Tax clearance certificate	• Registration with relevant authorities required • Special audit report on the sales amount is required if the royalty is related to sales commission • Charging basis and payment terms acceptable to approval and tax authorities	No restriction
Capital reduction	• Board resolutions • Approval from original approval authorities • SAFE approval notice	• Cash to extract is capped under paid-up registered capital • Registered capital after reduction cannot be lower than statutory minimum • Resistance from local government • Need to notify creditors and announce publicly	N/A
Offshore lending	• Loan agreement • SAFE approval notice	Subject to local SAFE approval	N/A

Market Watch

- In December 2010, SAFE extended the pilot scheme that allows companies registered in China to keep export proceeds in overseas bank accounts from six cities and provinces to the whole of China. Meanwhile, all companies that meet the requirements specified in the SAFE circular (Circular No: Huifa [2010] 67) can apply for joining the pilot scheme, which will help them simplify their payment and receipt process, enhance liquidity management and obtain low-cost financing from overseas banks.
- In September 2011, SAFE and other regulators announced a pilot scheme to reform FX controls over trade related transactions. The scheme will significantly simplify trade related foreign currency payment and receipt processes of companies that are classified as "A-Category" by SAFE. The pilot scheme will be implemented from 1 December 2011, covering Jiangsu, Shandong, Hubei, Zhejiang (excluding Ningbo), Fujian (excluding Xiamen), Dalian and Qingdao.
- In August 2011, RMB cross-border settlement was expanded to the whole of China, after being extended to 20 cities and provinces in June 2010. This is a step forward in RMB internationalisation.
- In October 2011, China's Ministry of Commerce (MOFCOM) and the PBOC separately announced a rule that permits foreign investors to make foreign direct investment (FDI) in China with RMB, which expands the channels for overseas-acquired RMB funds to flow back into China. Before these rules, RMB FDI was subject to MOFCOM and PBOC approval on a case-by-case basis. Under the new regulations, foreign investors can use RMB to contribute capital for entities set up in China, or acquire companies registered in China. Meanwhile, a foreign invested entity can borrow RMB debt from its parent, offshore affiliates and offshore financial institutions, within its foreign debt quota.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	1-3 January
Chinese Spring Festival	22-28 February
Ching Ming Festival	2-4 April
Labour Day	29 April-1 May
Dragon Boat Festival	22-24 June
Mid-Autumn Festival and National Day	30 September-7 October

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Market Analysis: Hong Kong SAR

Overview	
Population	7.1 million (2010)
Total area	1,104 sq km
Capital	n/a
Major language(s)	Cantonese and English
Time zone	GMT + 8 hours
Currency	Hong Kong Dollar (HKD)
Central bank	Hong Kong Monetary Authority (regulator)
Gross domestic product (GDP)	327.2bn (2010); 0.4% real growth rate (2010 est.); 45,944 per capita (2009 est.)
Inflation rate (consumer prices)	2.3% (2010)

Trade			
Total exports	USD390.4bn f.o.b. (2010)	Total imports	USD433.5bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 2.0% Fuels and mining – 2.1% Manufactured – 93.1% (2010)	Major imports (% by product group)	Agricultural – 4.7% Fuels and mining – 5.2% Manufactured – 88.1% (2010)
Major markets (% of total)	China – 52.4%, European Union – 11.4%, US – 10.7%, Japan – 4.1%, India – 2.5% (2010)	Major suppliers (% of total)	China – 44.7%, Japan – 9.3%, European Union – 7.3%, Singapore – 7.0%, Taiwan – 6.6% (2010)
Total trade	USD823.9bn (2010)	Total trade with Asia	USD598.9bn (2010)

Banking System and Bank Accounts

- The Hong Kong Monetary Authority (HKMA) is the government authority in the Hong Kong Special Administrative Region (SAR) responsible for maintaining banking and monetary stability.
- Hong Kong has one of the highest concentrations of banking institutions in the world; 69 of the 100 largest banks globally have operations there. As of September 2011, there were 196 authorised institutions operating in Hong Kong.
- The following types of bank accounts are currently available:

Account type	Local current[1]	Local savings	Foreign current[1]	Foreign savings
Resident	Yes	Yes	Yes[1]	Yes
Non-resident	Yes	Yes	Yes[1]	Yes
Credit interest	No	Yes	No	Yes

1. Hong Kong dollar (HKD), US dollar (USD) and renminbi (RMB) cheque books are available.

Clearing Systems and Payment Instruments

Within the local clearing environment, there are three payment settlement types operating: real-time gross settlement (RTGS) payments, paper cheque clearing and electronic clearing.

Clearing system	Comments
RTGS payments: HKD, USD, euro (EUR) and RMB	• Clearing House Automated Transfer System (CHATS) payments are interbank electronic payments settled on a RTGS basis, i.e. as opposed to end-of-day net settlement. • RTGS provides payment-versus-payment (PVP) settlement for foreign exchange (FX) trades to mitigate settlement risk. PVP settlement currencies include HKD, USD, EUR and RMB, and also between USD and ringgit (MYR), USD and Indonesian rupiah (IDR). • CHATS is operated by Hong Kong Interbank Clearing Ltd (HKICL), a company jointly owned by the HKMA and the Hong Kong Association of Banks (HKAB).
Paper cheque clearing: HKD, USD and RMB	• Cheque image presentation for clearing is used for cheques below HKD100,000. Settlement of cheques is on a D+1 basis (D being the cheque deposit date). In Hong Kong, cheque clearing is available for HKD, USD and RMB cheques.
Electronic clearing	• In September 2010, the RMB Central Clearing and Settlement System (CCASS) was implemented to support settlement of RMB-denominated securities.
Cross-border clearing	• In March 2009, a cross-border linkage arrangement was established between Hong Kong and mainland China to allow for two-way cross-border RTGS settlement of HKD, USD and EUR. • Two-way cross-border cheque clearing is available between Hong Kong and Guangdong province, including Shenzhen, in mainland China. Between Hong Kong and Shenzhen, the service applies to HKD and USD cheques, and between Hong Kong and Guangdong for USD cheques only. • One-way clearing of RMB cheques is available for cheques drawn on banks in Hong Kong and presented to banks in Guangdong province, including Shenzhen. Also available is one-way clearing for HKD cheques drawn on banks in Hong Kong and presented to banks in Macau.

Legal, Company and Regulatory

English common law and rules of equity form the basis of the legal system in Hong Kong. As specified in the Basic Law, the common law, rules of equity, ordinances, subordinate legislation and customary law previously in force before July 1997 have remained unchanged, except for any that contravene the Basic Law, and are subject to any future amendment by the legislature of the Hong Kong SAR.

Liquidity, Currency and Tax

- Hong Kong is relatively relaxed in terms of regulation of liquidity management: single currency, multi-currency, cash concentration and notional pooling are all permitted. There are no restrictions on FX and currency movements.
- However, careful tax efficiency considerations should be reviewed, with particular regard to the physical movement of funds among legal entities with onshore accounts. Due to the absence of withholding tax in Hong Kong's taxation frameworks, inter-company interest income sourced from an onshore account may be taxable and interest payments may not be tax deductible. As a result, cross-border movement of funds with offshore legal entities is generally preferable, as the receipt of interest income offshore is not likely to be subject to tax. (Obtaining independent advice on the accounting, tax, and legal consequences of entering into any liquidity management arrangement is recommended.)
- The standard rate of corporate profits tax is currently 16.5%.
- Popular deposit instruments for short-term HKD liquidity are time deposits and enhanced money market statement savings accounts.

Market Watch

- For the first half of 2011, RMB800bn of China's Trade was settled via Hong Kong, which is more than double that of the whole of 2010. The FX market has gone from being non-existent to seeing over USD3bn in daily turnover in spots and forwards. It is now on a par with the previously dominant RMB non-deliverable forward (NDF) market, and is already one of the top offshore FX markets in Asia. Hong Kong's role as an offshore RMB clearing centre was affirmed by China's Vice-Premier Li Keqiang's visit to Hong Kong in August 2011, wherein new measures were announced, including:
  - launch of the "mini-Qualified Foreign Institutional Investor (QFII)" scheme;
  - foreign direct investment to mainland China in RMB allowed for Hong Kong enterprises;
  - plans for an exchange-traded fund (ETF) that will enable mainland China investors to access stocks listed in Hong Kong;
  - approval for mainland companies to issue RMB bonds in Hong Kong; and
  - nationwide expansion of the RMB trade settlement scheme.

  All these new measures will increase the integration between mainland China and Hong Kong and further develop the offshore RMB market.
- On 25 July 2011, Hong Kong Exchanges and Clearing Limited (HKEx) introduced a T+2 finality arrangement for money settlement in CCASS for the Hong Kong securities market. Under T+2 finality, securities and money settlement is completed and finalised on T+2 (two business days after the trade), which is supported by a new interbank bulk settlement run in the evening of T+2 that is introduced by Hong Kong Interbank Clearing Limited (HKICL). The new arrangement reduces overnight credit risk of the securities market and aligns the money settlement arrangement in Hong Kong with international best practices by bringing finality of securities and money settlement on the same day.
- There are ongoing discussions between the HKMA and the central banks of other countries/regions (including the Middle East and various East Asian countries) regarding the feasibility of establishing links between the RTGS systems of these countries to facilitate settlement activities across the region.
- HKICL implemented the RMB Autodebit and Autocredit System on 21 March 2011, adopting a cloning approach to replicate the functionalities of the existing Autopay System in HKD. HKICL also

launched an initiative in early 2011 in which all member banks will use Direct Debit Authorisation Exchange (DDAE) to exchange DDA instructions by file transfer via HKICL instead of delivery of hard copy reports between member banks. This initiative has significantly improved the security and operational efficiency of DDA information exchange between member banks.

Clearing Systems Holidays 2012

Days on which the USD, RMB and EUR clearing systems are not in operation in 2012:

Holiday	Date
Every Saturday and Sunday	
The first day of January	1 January

Days on which the HKD clearing system is not in operation in 2012:

Holiday	Date
Every Saturday and Sunday	
The day following the first day of January	2 January
Lunar New Year's Day	23 January
The second day of the Lunar New Year	24 January
The third day of the Lunar New Year	25 January
Ching Ming Festival	4 April
Good Friday	6 April
The day following Good Friday	7 April
Easter Monday	9 April
Buddha’s Birthday	28 April
Labour Day	1 May
Tuen Ng Festival	23 June
The day following Hong Kong SAR Establishment Day	2 July
The day following Chinese Mid-Autumn Festival	1 October
The day following National Day	2 October
Chung Yeung Festival	23 October
Christmas Day	25 December
The first weekday after Christmas Day	26 December

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Market Analysis: India

Overview	
Population	1.2 billion (2010)
Total area	3.29 million sq km
Capital	New Delhi
Major language(s)	Hindi and English, with more than 20 other official languages
Time zone	GMT + 5.5 hours (New Delhi)
Currency	Indian Rupee (INR)
Central bank	Reserve Bank of India (RBI)
Gross domestic product (GDP)	4,057.8bn (2010); 5.5% real growth rate (2010 est.); 3,408 per capita (2010 est.)
Inflation rate (consumer prices)	12.0% (2010)

Trade			
Total exports	USD223.2bn f.o.b. (2010)	Total imports	USD328.7bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 10.7% Fuels and mining – 25.4% Manufactured – 63.9% (2010)	Major imports (% by product group)	Agricultural – 5.4% Fuels and mining – 38.8% Manufactured – 44.5% (2010)
Major markets (% of total)	European Union – 20.5%, UAE – 14.4%, US – 10.8%, China – 5.9%, Hong Kong – 4.0% (2010)	Major suppliers (% of total)	European Union – 14.4%, China – 11.5%, UAE – 7.4%, US – 6.0%, Saudi Arabia – 5.4% (2010)
Total trade	USD551.9bn (2010)	Total trade with Asia	USD177.0bn (2010)

Banking System and Bank Accounts

- The Reserve Bank of India (RBI) is the central bank of India and the main regulator for banks. India's commercial banking sector is made up of public sector banks including the State Bank of India group and 20 other nationalised banks, private sector banks and foreign banks. Although the public sector banks have a large network of branches, the Indian private sector banks are fast catching up in terms of revenue, size and business growth.

- Cross border transactions are subject to Foreign Exchange Management Act (FEMA) regulations. The RBI is responsible for administration of the FEMA.
- Customers who are not incorporated in India and have branches, liaison or project offices in India, are regulated by Section 6(6) of FEMA 1999. These companies may require prior approval of RBI to establish a branch, liaison or project office in India – such an office may open a bank account in India.
- The permissible debits and credits to such accounts depend on the business form – branch/liaison or project office – and are guided by FEMA provisions.
- The following types of bank accounts are currently available:

Account type	Local currency	Foreign currency
Resident	Yes	Yes
Non-resident	Yes	No

Clearing Systems and Payment Instruments

Clearing system	Comments
Real-Time Gross Settlement (RTGS)	• Electronic payments instructions are processed in real time and on a gross basis. • Intended for systemically important payments, such as treasury, interbank, statutory and high-value customer payments. • Minimum amount permitted for transfer is INR200,000. • Credit is received within two hours of transaction. • More than 45,000 branches enabled on RTGS.
National Electronic Funds Transfer (NEFT)	• NEFT is an electronic funds transfer system between banks using the Structured Financial Messaging Solution (SFMS) messaging application. • Intended for day-to-day payment requirements of customers, such as payment to suppliers. • Runs on a centralised clearing and settlement system supported by the RBI and is aimed as a substitute for cheque payments. • More than 70,000 branches enabled on NEFT.
National Electronic Clearing Service (NECS)	• Enables large-volume transfers of small-value transactions. • Intended for salary, interest, dividend, commission and other bulk repetitive payments. • Institutions and corporations disbursing interest or dividends to their investors use this payment mode. • Works on a one-day cycle. (i.e. T+1 settlement). • Transaction details and settlement details are captured on diskettes for data transfer. • More than 52,000 branches enabled on NECS.

- Cheques remain the most common method of payment in India. Currently there are 1,149 local clearing houses across the country, with those in Indian metropolitan areas being controlled by the central bank, while clearing in non-metropolitan areas and smaller towns is usually run by state-owned banks.

- Historically, the clearing systems have been local and confined to a defined jurisdiction covering all the banks situated in the area under a particular zone. However, with the introduction of the Speed Clearing Service and the cheque truncation system, clearing houses are now empowered to process instruments from other jurisdictions and areas.
- In addition, regulators are encouraging electronic payments through NEFT, RTGS and NECS, as well as direct credits within the bank.

Legal, Company and Regulatory

- Apart from the RBI, other important regulatory bodies in India include:
  - the Securities Exchange Board of India (SEBI), which regulates capital market activities;
  - the Central Board of Excise and Customs;
  - the Central Board of Direct Taxes, which provides essential inputs for policy and planning of direct taxes in India, and is responsible for administration of direct tax laws through the Income Tax Department; and
  - the Insurance Regulatory and Development Authority (IRDA), which regulates the insurance industry.
- Requirements for establishing a company in India are governed by the Companies Act, 1956. Among others, the key requirements include the following provisions:
  - Private companies should have a minimum paid-up capital of INR100,000 or such higher paid-up capital as may be prescribed. A public company should have a minimum paid-up capital of INR500,000 or such higher paid-up capital as may be prescribed. Please note that exact capital requirements vary according to industry sector.
  - A company may be formed by any seven or more persons (in the case of a private company any two or more persons) by subscribing their names to a memorandum of association and otherwise complying with the requirements of the Companies Act as regards registration.
  - No company shall be registered by a name that, in the opinion of the central government, is undesirable. A name that is identical to or too closely resembles the name by which a company in existence has been previously registered, or a registered trade mark or a trade mark that is the subject of an application for registration of any other person under the Trade Marks Act, 1999, may be deemed to be undesirable by the central government.
  - As regards the incorporation of a subsidiary company in India of a foreign company, the usual provisions of the Companies Act apply as regards incorporation and other day-to-day corporate matters. However, investment in India by a foreign company by way of incorporating a subsidiary must also comply with the government's current foreign direct investment policy and other regulatory requirements.

Liquidity, Currency and Tax

- Under the provisions of the Foreign Exchange Management Act, 1999, foreign companies in India are authorised to remit profits, royalties, dividends and capital, subject to foreign exchange controls administered by the RBI. Remittances are permitted only after accounts have been audited and due taxes have been paid. Foreign exchange hedging is permitted; however, deposits in foreign currency are restricted by the central bank.
- Only single currency cash concentration is allowed in India and in a cash concentration structure, interest payable by one participating company to another is subject to withholding income tax.
- Cash concentration across legal entities (pool versus main) can trigger significant tax implications, based on legal status and holding structure of the participating entities. Any advance or loan given by

a closely held company to either its shareholder(s) holding 10% or more of the voting power or any other company in which such shareholder(s) has substantial interest, is assumed as taxable dividends in the hands of the receiving company to the extent the lending company possesses accumulated profits. Two relevant exceptions to this rule are:

- where lending forms a substantial part of the lending company's business; and
- where the lending company is a listed company or is a subsidiary of a listed company.

- Tax deductibility of the cost of funds for the lending company may be impacted where it is utilised to fund other group entities. Also, interest payable between such group companies will be subject to withholding tax at 20% (plus surcharge and cess as applicable) on a gross basis, which will create cash flow gaps. Interest income arising from the pooling will be taxable at 30% (plus surcharge and cess as applicable). If any of the lending entities are on an income-tax holiday, such interest income may not be covered by the holiday.
- Notional pooling is not permitted in India.
- Common investment instruments used by corporates for surplus liquidity include term deposits, cluster deposits and mutual funds. (The previous alternative of exchange earner's foreign currency (EEFC) deposits ceased to exist as of 31 October 2008.)
- Corporate tax rates are as follows:

Company	Regular tax	Tax rate (inclusive of applicable surcharge and cess)
Domestic company	(a) Where total income is more than INR10m (b) Where the total income is equal to or less than INR10m	32.445% 30.90%
Foreign company	(a) Where total income is more than INR10m (b) Where the total income is equal to or less than INR10m	42.024% 41.20%

- Withholding tax rates for foreign companies (subject to surcharges and cess wherever applicable) are as follows:[1]

Source of income	Withholding tax rate for non-treaty foreign companies	Withholding tax rates for US companies carrying out business in India under the India–US tax treaty
Dividends	Dividends referred to in Section 115-O of the Income Tax Act are exempt. Any income received in respect of units of a mutual fund specified under Section 10(23D) or the specified company is also exempt. In other cases the rate is 20%.	15% if at least 10% of the voting stock of the company paying the dividend is held by the recipient. In other cases, the rate is 25%.
Interest income	20% on money borrowed in foreign currency.	10% if the loan is granted by a bank or similar financial institution, including insurance company. In other cases, the rate is 15%.

(table continues)

Royalties	10% where the agreement is made on or after 1 June 2005. For agreements made prior to 1 June 2005, there are different rates depending on the date when the agreement was made.	10% for equipment rental and for ancillary or subsidiary services thereto. In other cases, 15%.
Technical services	10% where the agreement is made on or after 1 June 2005. For agreements made prior to 1 June 2005, there are different rates depending on the date when the agreement was made.	10% for equipment rental and for ancillary or subsidiary services thereto. In other cases, 15%.
Other income	40%, plus surcharge and cess as applicable.	Nil if treaty benefit is available, the income is in the nature of business income and the recipient company does not have permanent establishment in India. Otherwise, the tax rate is 40%, plus surcharge and cess as applicable.
1. In case the foreign company has not obtained a Permanent Account Number (PAN), the withholding tax would be at the above mentioned rates or 20%, whichever is lower.		

Market Watch

India is undergoing significant changes and improvements to its clearing infrastructure. Some major developments and initiatives include:

- Increased use of electronic clearing systems, with significant growth in the use of NEFT and RTGS: In line with the RBI's vision for an increased role for electronic payments in India, the RBI is upgrading and promoting electronic payments systems. This is evident in the percentage growth in the volume and value of electronic payments compared to paper payments, as shown below.

Year-on-year growth	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010
Paper volume	14%	10%	6%	7%	-5%	-2%
Paper value	-10%	8%	6%	11%	-5%	-17%
Electronic volume	37%	25%	33%	41%	25%	10%
Electronic value	109%	35%	61%	342%	38%	65%

Source: RBI website

- Phasing out of paper-based high-value clearing: RBI discontinued High Value Clearing on March 31, 2010. Statutory payments, such as direct and service tax, excise and customs duty, state sales tax (VAT, CST, etc.) are already required to be made electronically.
- Cheque truncation system: Under the cheque truncation system, instead of the physical instrument, an electronic image of the cheque is sent to the drawee branch along with the relevant cheque-related information. This effectively reduces the turnaround time for the processing of cheques, along with the associated cost of transit and delay in processing, etc. and speeds up the process of cheque realisation. The cheque truncation system is currently live in the National Capital Region (New

Delhi and four surrounding states). In September 2011, a pilot scheme for the system has also been started at Chennai.

- Interbank Mobile Payment Service (IMPS): IMPS is currently live in 28 banks and offers an instant, 24/7, interbank electronic fund transfer service through mobile phones. IMPS allows customers to use mobile instruments as a channel for accessing their bank accounts and allows high interbank fund transfers in a secured manner with immediate confirmation features.
- Effective 1 April 2012, RBI has directed banks to dishonour cheques/drafts/etc. that are presented beyond three months from the date of such instruments, against the current norm of six months

Clearing Systems Holidays 2012

Clearing systems holidays in India are location specific. Visit the Government of India's official website (http://india.gov.in/calendar/calendar.php) for information about the government's list of public holidays.

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Market Analysis: Indonesia

Overview	
Population	237.6 million (2010)
Total area	1.90 million sq km
Capital	Jakarta
Major language(s)	Bahasa Indonesia (official), Dutch, English and 300 regional languages
Time zone	GMT + 7 hours (West); GMT + 8 hours (Central); GMT + 9 hours (East)
Currency	Indonesian Rupiah (IDR)
Central bank	Bank Indonesia
Gross domestic product (GDP)	1,033.0bn (2010); 1.4% real growth rate (2010 est.); 4,347 per capita (2010)
Inflation rate (consumer prices)	5.1% (2010)

Trade			
Total exports	USD157.8bn f.o.b. (2010)	Total imports	USD135.7bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 22.8% Fuels and mining – 39.4% Manufactured – 37.0% (2010)	Major imports (% by product group)	Agricultural – 11.9% Fuels and mining – 24.5% Manufactured – 63.6% (2010)
Major markets (% of total)	Japan – 16.3%, European Union – 10.9%, China – 9.9%, US – 9.1%, Singapore – 8.7% (2010)	Major suppliers (% of total)	China – 15.0%, Singapore – 14.9%, Japan – 12.5%, European Union – 7.3%, US – 6.9% (2010)
Total trade	USD293.5bn (2010)	Total trade with Asia	USD201.3bn (2010)

Banking System and Bank Accounts

- The central bank is Bank Indonesia (BI), whose position is regulated by statute. As a public legal entity, BI has the authority to issue policy rules and regulations; while as a civil legal entity, BI is able to represent itself in and outside the court of law.
- There are 120 commercial banks with more than 14,347 branches in Indonesia. These consist of state-owned banks, local private banks (foreign exchange (FX) licensed, and non-FX licensed banks),

foreign banks and the regional development bank or Bank Pembangunan Daerah. Furthermore, there are 1,682 rural banks with over 4,074 branches.

- The following types of bank accounts are currently available:

Type of corporate entity	Non-interest bearing current account		Interest-bearing current account		Savings account	Credit facility
	IDR	Foreign currency	IDR	Foreign currency		
Resident	Yes	Yes	Yes	Yes	Not applicable	Yes
Non-resident	Yes	Yes	Yes	Yes	Not applicable	No

- Foreign companies can open IDR current accounts.

Clearing Systems and Payment Instruments

Domestic funds transfer

- Low-value funds transfer via Sistem Kliring Nasional (SKN): There are 125 conventional banks and 18 banks with syariah licence registered as direct members of the SKN clearing system. SKN is design for low-value payment settlement (below IDR100m) that runs on a net settlement system. The clearing system was enhanced in the second quarter of 2010 and enables participant banks to monitor their balance position at BI in real time, resulting in the settlement of SKN transactions on an almost real-time basis compared to two settlement cycles daily when it was first introduced in 2005.
- High-value funds transfer via the real-time gross settlement (RTGS) system: There are 125 conventional banks, 24 banks with syariah licence as well as five non-bank entities registered as direct members of the RTGS clearing system. The RTGS system allows for real-time high-value IDR funds transfer between registered participant banks in Indonesia. All fund transfers above IDR100m are made via RTGS. RTGS is centralised at BI's headquarters in Jakarta. Banks whose headquarters are located in Jakarta have the option of registering as direct members of the RTGS system. For banks whose headquarters are located outside Jakarta or banks that are not registered as direct members, access to RTGS is via a correspondent bank with direct RTGS membership.

Domestic cheque clearing

- Intercity clearing: There are 55 banks registered as direct members of the intercity clearing scheme, which was introduced by BI in 2002 to shorten cheque collection times. Intercity clearing enables registered bank members to clear cheques issued by any registered member via its headquarters, regardless of whether the cheque instrument itself was issued by one of its remote branches. Corporate customers receiving upcountry cheques on a regular basis will have the cleared funds credited to their corporate account (if the issuing bank is a registered member of intercity clearing) one day after the clearing date. Therefore, cheques issued and deposited to a bank branch that is a direct member of intercity clearing will be processed on a local clearing basis, thereby making cleared funds available to accounts more quickly.
- Upcountry cheque clearing – Inkaso: Cheques issued by non-members of intercity clearing must be cleared in the same city as the issuing branch, which has been designated as an upcountry cheque

collection (Inkaso) processing centre. The processing of upcountry cheques should take a maximum of 27 working days

Legal, Company and Regulatory

- Apart from BI, there are several other regulatory bodies that have influence over the banking system. The Indonesian Capital Market and Financial Institution Agency – Badan Pengawas Pasar Modal dan Lembaga Keuangan (BAPEPAM-LK) – and Indonesia Stock Exchange also have a significant regulatory role, particularly in relation to the settlement of marketable securities and related accounts.
- An Indonesian limited liability company is established by two or more parties in a notarial deed and obtains its legal entity status after approval by the Minister of Laws and Human Rights. The minimum authorised capital is IDR50m, of which 25% has to be paid when submitting an application.
- Any company with foreign investment participation has to obtain approval from the Indonesian Coordinating Board – Badan Koordinasi Penanaman Modal (BKPM). The government has in force a prohibition list that prevents certain types of business from being owned by foreign corporations.
- On 15 August 2011, the Minister of Finance issued regulation No. 130/PMK.011/2011 on the Exemption or Reduction of Corporate Income Tax. The tax holiday facilities described in the regulation are:
  - corporate income tax (CIT) exemption for five to 10 years starting from the fiscal year in which commercial production starts; and
  - an additional 50% CIT reduction for two years after the end of the initial CIT exemption period.

  The parties eligible to enjoy these tax facilities are taxpayers who:
  - operate in pioneer industries including base metals, oil refineries and/or base organic chemicals sourced from natural oil and gas, machinery, renewable resources and communications equipment;
  - have a new authorised capital investment plan of a minimum of IDR1tr (USD119m);
  - deposit at least 10% of the capital investment plan amount above in banks located in Indonesia, which should not be withdrawn before the realisation of the capital investment plan; and
  - have the status of a legal entity in Indonesia, the approval of which should have been obtained no more than 12 months before the effective date of this regulation.
- Established in 2004, the Indonesia Deposit Insurance Corporation – Lembaga Penjamin Simpanan (LPS) – is responsible for insuring all depositors' funds. The LPS determines the maximum amount secured under this deposit insurance scheme.
- On 31 May 2011, the Indonesian Parliament (DPR) passed a new currency law whose key provision requires the mandatory use of IDR in the following transactions conducted in Indonesia:
  - all transactions that have a purpose of payment;
  - settlement of obligations that have to be satisfied with a cash payment; and/or
  - other financial transactions.

  Exemptions apply to:
  - certain transactions related to the implementation of the state budget;
  - receipt or disbursement of offshore grants;
  - international commercial transactions;
  - bank deposits in foreign currencies;
  - offshore loan transactions; and
  - transactions in which both payer and beneficiary agree for the payment or settlement of obligation in a foreign currency.

  Violators of this regulation are subject to imprisonment for a maximum of one year and a maximum penalty of IDR200m (USD 25,000), which applies to individuals and companies alike.

- On 30 September 2011, PBI No. 13/20/PBI/2011 was issued by BI in relation to the FX proceeds from export – Devisa Hasil Ekspor (DHE). The summary of the regulation is as follows:
  - All DHE must be received by exporters through FX banks (banks with a Devisa licence) in Indonesia.
  - The receipt of DHE through an FX bank must be within 90 calendar days after the date of the export notification form – Pemberitahuan Ekspor Barang (PEB).
  - Exporters must provide information as stated in the PEB that relates to the DHE to the FX bank within three working days after the DHE is received, which will be further submitted to BI.
  - Exporters who receive DHE by way of an issuance of a letter of credit (LC), consignment, open account or collection whose due date exceeds or equals 90 calendar days after the date of PEB must provide a written statement along with the required supporting documents within 14 calendar days after the date of PEB to the FX bank,which will be further submitted to BI.
  - DHE received by the exporter must be matched with the PEB value. If differences are identified, the exporter should provide a written statement along with supporting documents to the FX bank by the fifth day of the following month.
  - Where the difference between DHE and the PEB value is due to an administration fee of 10% of the PEB's value or a maximum equivalent of IDR10m, the exporter no longer needs to submit the supporting documents as it is considered in line with the PEB value.

Liquidity, Currency and Tax

- IDR may not be remitted outside Indonesia.
- IDR transfer to non-resident accounts is restricted unless there is valid underlying economic activity. For daily amounts up to IDR500m, the underlying economic reasons must be stated in the fund transfer; for amounts above IDR500m, documentation in support of the underlying economic reasons in Indonesia must be supplied.
- Resident and non-resident account holders are required to fill in a code for central bank FX monitoring purposes for any foreign currency transfer with a value equal to or greater than USD10,000.
- Under BI Regulation Number: 10/28/PBI/2008, the following apply to FX purchase transactions:
  - Purchases of foreign currency against IDR by a resident/non-resident of a value not exceeding USD100,000 should be accompanied with a formal signed declaration with stamp duty, stating that the FX purchase transaction against IDR does not exceed USD100,000 or its equivalent per month across all banks in Indonesia.
  - For purchases of foreign currency against IDR above USD100,000 or equivalent per month across all banks in Indonesia, the following documents should be submitted:
    — statement letter;
    — copy of tax identity (this does not apply for non-residents); and
    — documents evidencing the underlying transaction.
- Banks are only permitted to conduct FX derivative transactions of foreign currency against IDR to non-residents of up to USD1m or equivalent per individual transaction and each bank's outstanding gross position, unless those transactions are conducted for hedging purposes as part of an investment in Indonesia with a time frame of no less than three months, merchandise exports and imports by means of LCs, and/or domestic trade by means of domestic LCs (where supporting documents are required). Derivative transactions are restricted to forwards, swaps and options.
- Non-residents are not entitled to credit facilities in local currency and/or foreign currency. However, this restriction is not applicable to the following:
  - syndicated credit, with conditions that the lead bank is a prime bank, credit is being extended for project financing in the real sector for productive ventures in Indonesia, and the contribution of

foreign banks acting as syndicate members is greater than the contribution of domestic banks;
- credit cards and consumer loans;
- intra-day overdrafts in IDR and foreign currency, with the condition that it is supported by authenticated documents showing confirmation of same-day incoming remittances; and
- IDR and foreign currency overdrafts liable to administrative charges negotiated by foreign parties of claims from the agency appointed by the government for the management of bank assets within the framework of Indonesian bank restructuring, for which payment is guaranteed by a prime bank.

- Notional pooling is permitted: however, its use is not widespread.
- Time deposits are the most commonly used instrument for the investment of short-term surplus liquidity, although treasury bills are also used. Government bonds (and, to a lesser extent, mutual funds) are used for longer-dated liquidity. Most liquidity is at the short end of the curve, typically between one to three months.
- Interest is subject to withholding tax of 20% or a lower applicable tax treaty rate.
- Starting in July 2009, settlement of tax payments through Bank Persepsi, which were previously performed twice a week by banks, changed to same-day settlement. For late settlement, banks are penalised 1% daily of the total tax payment.
- On 3 September 2010, BI rolled out a new required reserve ratio/loan-to-deposit ratio (RRR/LDR) tie-up policy in which banks had a grace period of half a year till 1 March 2011 to keep their LDR within the 78-103% band. Banks that abided by this enjoyed a 2.5 percentage point rebate on the RRR.
- Starting 1 November 2010, the primary reserve requirement, whereby banks have to deposit cash amounts with the central bank, increased from 5% to 8%. The secondary reserve requirement, which banks can fulfil in the form of government bonds, remains unchanged at 2.5%.

Market Watch

It is advisable to hold discussions with the central bank and the tax authorities before embarking on any notional pooling schemes or, at least, solicit an opinion from a suitable advisor.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	1 January
Lunar Chinese New Year	23 January
Birth of Prophet Mohammad	4 February
Nyepi – Balinese New Year	23 March
Good Friday	6 April
Vesak Day	5 May
Ascension Day	17 May
Ascension of Prophet Mohammad	16 June
Indonesian Independence Day	17 August

(table continues)

Eid Al Fitr*	19 August
Eid Al Adha	26 October
Islamic New Year	15 November
Christmas Day	25 December

**Mass leave related to Eid Al Fitr is subject to government announcement.*

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Market Analysis: Japan

Overview	
Population	127.6 million (2010)
Total area	377,930 sq km
Capital	Tokyo
Major language(s)	Japanese
Time zone	GMT + 9 hours
Currency	Yen (JPY)
Central bank	Bank of Japan (BOJ)
Gross domestic product (GDP)	4,323.5bn (2010); 5.8% real growth rate (2010 est.); 33,885 per capita (2010)
Inflation rate (consumer prices)	-0.7% (2010)

Trade			
Total exports	USD771.7bn f.o.b. (2010)	Total imports	USD694.0bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 1.3% Fuels and mining – 4.3% Manufactured – 88.4% (2010)	Major imports (% by product group)	Agricultural – 11.2% Fuels and mining – 36.7% Manufactured – 50.0% (2010)
Major markets (% of total)	China – 19.4%, US – 15.6%, European Union – 11.3%, Korea – 8.1%, Taiwan – 6.8% (2010)	Major suppliers (% of total)	China – 22.1%, US – 10.0%, European Union – 9.6%, Australia – 6.4%, Saudi Arabia – 5.2% (2010)
Total trade	USD1.5tr (2010)	Total trade with Asia	USD740.6bn (2010)

Banking System and Bank Accounts

- The central bank is the Bank of Japan (BOJ), which controls monetary policy. There are approximately 730 banks in Japan, including 57 foreign banks.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current[1]	Foreign savings
Resident	Yes	Yes	Yes	Yes
Non-resident	Yes	Yes	Yes	Yes
Credit interest	No	Yes	No	Yes

1. Foreign currency cheque books are not available in Japan.

- Account opening procedures for non-resident companies are broadly the same as for local companies. If the entity concerned is not a subsidiary, then different documents will be required, such as a certified copy of commercial registration that has been verified by the relevant embassy.

Clearing Systems and Payment Instruments

- There are five clearing and settlement systems operating in Japan, each of which is intended for different settlement purposes:

Clearing system	Comments
Bank of Japan Net (BOJNet)	BOJNet is the interbank clearing system. It allows banks with accounts with BOJ to transfer funds online between these accounts. BOJNet is owned by the BOJ.
Foreign Exchange Yen Clearing System (FXYCS)	FXYCS is the cross-border JPY clearing system. All clearing services involving non-residents are provided through this system. The cut-off time is 2:00pm.
Zengin System (domestic funds transfer system)	This is an electronic funds transfer system between domestic JPY accounts. The cut-off time is 3:25pm. The sixth-generation Zengin System commenced operations in November 2011 and introduced real-time gross settlement (RTGS) for fund transfers of over JPY100m. (XML format is optional.) Zengin System is managed by Zengin-Net.
CLS (Continuous Linked Settlement)	CLS is a process by which a number of the world's largest banks manage clearing and settlement of foreign exchange transactions between themselves, their customers, and other parties..
Tokyo Clearing House and 121 local clearing houses	Tokyo Clearing House is where paper-based items such as promissory notes and cheques are exchanged for clearing. Transactions in Osaka are cleared through the agent bank.

Bank-neutral system	Comments
ANSER (Automatic Answer Network System for Electronic Request)	ANSER is not a local clearing system, but part of the de facto public infrastructure run by NTTData in the local banking industry for bank-neutral, real-time Zengin data interchange. ANSER is mostly used for intra-day, cross-bank cash concentration of resident JPY liquidity. The cut-off time is 3:00pm.

Legal, Company and Regulatory

- The Financial Services Agency (FSA) acts as the regulator for the banking and financial sector in Japan.
- Residency status is determined by the existence of a permanent establishment in Japan. Branches of foreign incorporated companies are considered as residents, in addition to companies' Japanese subsidiaries.
- Non-residents are in most instances not subject to any reporting requirements to the Japanese authorities. Residents must comply with the authorities' reporting requirements for non-trade related transactions involving non-residents for any amount over JPY30m or equivalent. The reports are submitted to the Ministry of Finance via BOJ.
- The Financial Instruments and Exchange Law came into effect on 30 September 2007. This law regulates how financial institutions can sell high-risk products. Similar rules were instituted into banking law with regard to the handling of non-JPY deposits. As a result, customers are classified as either professional or amateur. Foreign corporations are regarded as professional by default, but have the option to be switched to amateur status. (Banks are required to give notice of this option before handling transactions.) If a foreign corporation opts for amateur status, then the bank is required to provide it with a document containing charges and risk information, together with an explanation of the product.
- Corporations incorporated in Japan are classified as professional by default in certain cases, such as if the corporation's paid-up share capital is JPY500m or more or if its stock is listed.
- There has been discussion in the market on whether lender registration is required for inter-company loans between sister companies in Japan. However, according to the Money-Lending Business Control and Regulation Law in Japan, the FSA clearly states in a letter dated 26 June 2008 that for companies that conduct inter-company lending, i.e. JPY sweeps, with other sister companies, lender registration is required.
- The Fund Settlement Law came into effect in April 2010 allowing non-banking businesses to start providing money remittance services. The law was enacted to regulate all money transfer businesses including non-banks to protect consumers from this risk. The law is expected to encourage increased competition, product innovation and pricing reduction for cross-border remittances of retail customers.
- In order to repatriate overseas income, the tax regulations have been amended to exclude dividends from overseas subsidiaries in a tax write-off. This became effective in the 2009 accounting year in Japan.

Liquidity, Currency and Tax

- Cash concentration is permissible. Notional pooling is now being prepared.
- Deposits are typically used as the investment instruments of choice for liquidity structures. However, as current interest rates in Japan are low, onshore cash concentration in JPY is not actively practised as corporations prefer to seek higher-yield possibilities in other locations/currencies.
- As mentioned, with reference to the Money-Lending Business Control and Regulation Law in Japan, the FSA has clarified that inter-company lending/sweeping between sister companies would require lender registration.
- The maximum effective tax rate – after amalgamating corporation tax, inhabitants' tax and enterprise tax, and allowing for business tax deductions – is 40.87%.
- A withholding tax of 20% applies to dividends (reduced to 7% for listed shares except for individuals holding more than a certain ratio of an outstanding number of shares), inter-company loan interest

and royalty payments to non-residents. A 15% withholding tax is applied to all bank deposit interest and bond interest to non-residents, but there are more than 59 bilateral double taxation treaties in place that can reduce the withholding tax rate. To comply with transfer-pricing regulations, all inter-company transactions must be made at arm's length.

- A 5% consumption tax applies to banking charges associated with domestic transactions and must be an element of any quoted price.

Market Watch

- BOJ has adopted a zero interest rate policy since 5 October 2010 by cutting its key interest rate to virtually zero. The target rate for unsecured overnight call loans was reduced to 0-0.1% from 0.1%. The decision underscores growing worries about the Japanese economy troubled by strong yen and falling prices.
- On 11 March 2011, an earthquake and tsunami caused extensive and severe structural damage in Japan, including heavy damage to roads and railways in many areas. BOJ offered JPY15tr (USD183bn) to the banking system on 14 March in an effort to normalise market conditions. Many electrical generators were taken down, and at least three nuclear reactors in Fukushima suffered explosions after cooling system failure. Early estimates placed insured losses from the earthquake alone at USD14.5bn-34.6bn. The overall cost could exceed USD300bn, making it the most expensive natural disaster on record.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	1 January
New Year's Day Observed	2 January
Bank Holiday	3 January
Coming-of-Age Day	9 January
National Foundation Day	11 February
Vernal Equinox Day	20 March
Showa Day	29 April
Showa Day Observed	30 April
Constitution Memorial Day	3 May
Greenery Day	4 May
Children's Day	5 May
Marine Day	16 July
Respect-for-the-Aged Day	17 September
Autumnal Equinox Day	22 September

(table continues)

Health Sports Day	8 October
Culture Day	3 November
Labor Thanksgiving Day	23 November
The Emperor’s Birthday	23 December
The Emperor's Birthday Observed	24 December
Bank Holiday	31 December

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Market Analysis: Korea

Overview	
Population	48.9 million (2010)
Total area	99,678 sq km
Capital	Seoul
Major language(s)	Korean
Time zone	GMT + 9 hours
Currency	Won (KRW)
Central bank	Bank of Korea
Gross domestic product (GDP)	1,466.1bn (2010); 2.0% real growth rate (2010 est.); 29,997 per capita (2010)
Inflation rate (consumer prices)	3.0% (2010)

Trade			
Total exports	USD471.1bn f.o.b. (2010)	Total imports	USD425.3bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 2.0% Fuels and mining – 9.1% Manufactured – 88.2% (2010)	Major imports (% by product group)	Agricultural – 6.3% Fuels and mining – 36.9%, Manufactured – 56.4% (2010)
Major markets (% of total)	China – 23.8%, European Union – 12.8%, US – 10.4%, Japan – 6.0%, Hong Kong – 5.4% (2010)	Major suppliers (% of total)	China – 16.8%, Japan – 15.3%, European Union – 10.0%, US – 9.0%, Saudi Arabia – 6.1% (2010)
Total Trade	USD896.4bn (2010)	Total trade with Asia	USD461.4bn (2010)

Banking System and Bank Accounts

- The central bank is the Bank of Korea (BOK). The Financial Supervisory Service regulates the banking sector.
- Since the 1997 Asian financial crisis, there has been consolidation in Korea's banking industry. At the instigation of the government, many major domestic banks merged to improve their financial health. Notable examples are Citibank's merger with Hanmi Bank and Standard Chartered's merger with

Korea First bank. The crisis also brought tighter regulations in the banking industry, especially in the way financial transactions were conducted among businesses.

- At present, there are around 15 domestic banks, the largest of which dominate the local market, while foreign banks have been more successful in providing offshore business.
- Documentation requirements for opening bank accounts are not particularly onerous and include standard items such as certificates of business registration.
- The following types of bank accounts are currently available:

Account type	Local current[1]	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	Yes	Yes
Non-resident	Yes[1]	Yes[1]	Yes	Yes
Credit interest	No[2]	Yes	No[2]	Yes

1. To encourage local currency deposits, the government permits non-residents to open two types of local currency accounts under the current regulations: a non-resident free won account — savings account (NRF) and current account (NCA) — or a non-resident won account. For the non-resident free won account, non-residents are free to remit funds abroad without underlying documents, although local deposit/withdrawal/transfer is restricted. For the non-resident won account, non-residents can make local deposits/withdrawals, although remitting funds abroad is restricted.

2. Due to BOK regulations, no interest is paid on current accounts.

Clearing Systems and Payment Instruments

Clearing system	Comments
High-value clearing system (BOK-Wire)	• The Bank of Korea Financial Wire Network (BOK-Wire) is an online network that connects the central bank and participating financial institutions for real-time gross settlement (RTGS) across current accounts held with BOK. The cut-off time is 3:00pm. It is normally used for payments over KRW1bn.
Local foreign currency clearing system	• There are two kinds of local foreign currency clearing systems in Korea. One is a clearing system provided by Korea Exchange Bank, Kookmin Bank, Shinhan Bank and Woori Bank through their CLS (Continuous Linked Settlement) memberships using the SWIFT network. The cut-off time is 3:00pm for US dollars and euros, and 9:50am for Asian currencies. The other system uses Korea Financial Telecommunications and Clearings Institute (KFTC) infrastructure instead of the SWIFT network. • Since 22 October 2010, KFTC has started a real-time foreign currency payment and clearing service similar to the local currency payment and clearing system using KFTC infrastructure; most local banks and some foreign banks have joined with KFTC as members for real-time foreign currency payment and clearing. The cut-off time is 4:30pm.
Retail payment clearing system	• The retail payment systems comprise the cheque clearing system, the bank giro system, the Online Funds Transfer (OFT) system, the Electronic Financial Information Network (EFIN) system, the interbank cash dispenser/automated teller machine (CD/ATM) system, the Electronic Funds Transfer at Point of Sale (EFTPOS) system, and the Cash Management Service (CMS) system.

(table continues)

	• All these payment systems are managed by KFTC, a non-profit clearing and financial data relay centre established and jointly owned by member banks. • The cut-off time for banking services via the OFT system is 4:00pm, and 11:30pm for the EFIN and CD/ATM systems.

Legal, Company and Regulatory

- In addition to BOK, the Ministry of Strategy and Finance is responsible for formulating rules and regulations relating to the banking and finance sector and the economy as a whole.
- When foreign investors wish to set up a subsidiary in Korea by acquiring newly issued/outstanding stock of a company, they must submit the required declaration form through an FX designated bank and take the necessary procedures for capital injection advised by the bank. The minimum level of injection for foreign direct investment companies is KRW50m.
- Branches of foreign corporations must designate an FX bank through which to channel working capital, and repatriate the branch's retained earnings so that the overseas head office can manage its money.

Liquidity, Currency and Tax

- Transactions between resident and non-resident accounts and cross-border payment transfers are highly regulated under the Foreign Exchange Transaction Regulation (FETR). To comply with the FETR, any underlying documents must be submitted to the designated FX bank for the transaction. However, there is no restriction or limit regarding exchange into KRW or other foreign currencies.
- FX regulations on non-resident accounts in local currency are as follows:

Account type	General regulations
Non-resident free won account	• Deposits from overseas and repatriation of funds out of Korea are allowed without restriction. • Local payments/collections are generally not allowed except for the transactions permitted by local FX regulations (e.g. a result of normal trading activities).
Non-resident won account	• Local deposits and withdrawals are allowed without restrictions. • Repatriation of funds out is not allowed except for transactions permitted by local FX regulations.

- HSBC Korea offers notional pooling between residents. Although HSBC conducts a thorough investigation, customers are requested to seek independent advice on legal/regulatory/tax implications.
- HSBC Korea provides cash concentration between residents. However, customers should be aware of negative tax implications on inter-company lending for non-business purposes.

Market Watch

The government is continuing its policy of gradual deregulation, as witnessed by legislation such as the Financial Investment Services and Capital Market Act promulgated in 2007 and the government's intention to raise the shareholding cap on non-financial company ownership of banks.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Lunar New Year's Day	23-24 January
Anniversary of Independence Movement	1 March
Legislative Election Day	11 April
Buddha's Birthday	28 May
Memorial Day	6 June
Independence Day	15 August
Chuseok Holiday (Harvest Festival)	1 October
National Foundation Day	3 October
Presidential Election Day	19 December

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Market Analysis: Macau SAR

Overview	
Population	552,300
Total area	29 sq km
Capital	n/a
Major language(s)	Cantonese, Portuguese and English
Time zone	GMT + 8 hours
Currency	Pataca (MOP)
Central bank	The Monetary Authority of Macau (AMCM)
Gross domestic product (GDP)	USD22.3bn (2010), 26.4% real growth rate (2010 est.), USD51,214 per capita (2010)
Inflation rate (consumer prices)	2.8% (2010)

Trade			
Total exports	USD87.0m f.o.b. (2010)	Total imports	USD5.5bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 2.1% Fuels and mining – 12.1% Manufactured – 81.9% (2010)	Major imports (% by product group)	Agricultural – 17.0% Fuels and mining – 11.1% Manufactured – 65.6% (2010)
Major markets (% of total)	Hong Kong – 30.4%, China – 11.4%, US – 11.0%, European Union – 5.6%, Vietnam – 2.7% (2010)	Major suppliers (% of total)	China – 30.5%, European Union – 22.2%, Hong Kong – 10.3%, Japan – 8.5%, Switzerland – 7.4% (2010)
Total trade	USD6.4bn (2010)	Total trade with Asia	USD3.8bn (2010)

Banking System and Bank Accounts

- The Monetary Authority of Macau (AMCM) was established in 1989 with the function of a quasi-central bank and the power to supervise the financial system of the Macau Special Administrative Region (SAR), covering the banking and insurance sectors and other authorised institutions, such as money changers and cash remittance companies.
- At present, there are 28 banks in Macau: 12 are locally incorporated (including three banks with headquarters in Macau and nine subsidiaries of overseas banks) and 16 are branches of overseas

banks. With the exception of two offshore banks, all banks in Macau are fully licensed retail banks.

- On the insurance side, there are 24 insurance companies, 11 of which are life companies while the remaining 13 are involved in non-life business. Eight are local companies and the rest are branches of overseas companies.
- The authority for the supervision, coordination and inspection of insurance activities rests with the Chief Executive, while the actual execution of these functions is carried out by AMCM through its Insurance Supervision Department.
- There are no particular restrictions on opening bank accounts in Macau. However, since Macau law is continental law (rather than common law) the Commercial Code applies to new company formations.
- For foreign corporations, a beneficial ownership declaration is required.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	Yes	Yes
Non-resident	Yes	Yes	Yes	Yes
Credit interest	No	Yes	No	Yes

Clearing Systems and Payment Instruments

- The local clearing system is owned, managed and run by the AMCM. Both MOP and Hong Kong dollar (HKD) domestic cheques can be cleared in two days. There is no settlement through the Macau clearing system on Saturday and Sunday.
- At present, Macau has no real-time gross settlement (RTGS) system or electronic automated clearing houses (ACHs). Therefore, most companies use the in-house ACH facilities of major banks for standing orders, direct debits and SWIFT payments. Cheques are also commonly used, denominated in either MOP or HKD. In the absence of RTGS and ACHs, clearing in Macau is mostly paper-based.

Legal, Company and Regulatory

- There are no exchange control regulations, except for renminbi (RMB) exchange. For local companies involved in exports, 40% of the relevant foreign currency transaction amount is surrendered to the government to exchange into MOP.
- The AMCM is the regulatory body responsible for supervising the banking and insurance sectors and other authorised institutions. This includes the supervision of bureaux de change. For banks registered as an overseas branch in Macau, there is no capital requirement.
- There are four basic steps to establishing a company in Macau:
  - Application regarding the admissibility of a trade name, which should be submitted to the Commercial Registry Office (CRCBM) and include a clear definition of the company's objectives.
  - Completion and signing of the company's memorandum and articles of association (which must be done within 60 days of obtaining the trade name). This can be done through the Macao Trade and Investment Promotion Institute's private notary, a Macau-registered lawyer, or by the applicant and certified by a notary.
  - Registration of the company (must be completed within 15 days of signing the memorandum of association) with the CRCBM, which requires submission of the following:
    — letter of application with verified signature;
    — company constitution document;

— list of shareholders with copies of their ID;
— list of board members;
— company board's letter of appointment;
— copy certificate of admissibility of the company's trade name; and
— list of names of the administrative board.

- Making a declaration of commencement of operation to the Macau Finances Services Bureau, which must include:
  — completed industrial tax form with verified signature;
  — list of shareholders with copies of their ID;
  — list of board members and their letters of appointment;
  — certificate of registration issued by the CRCBM;
  — copy of the memorandum and articles of association; and
  — payment of the industrial tax (see the Liquidity, Currency and Tax section).

Liquidity, Currency and Tax

- Macau has fairly "benign" banking regulations compared to other Asia-Pacific territories and countries. However, there are regulations that restrict liquidity management. For example, in-country notional pooling is only permitted subject to validation of enforceability right of set-off, while MOP cross-border notional pooling and MOP cross-border sweeping are not permitted.
- The following is a list of the key areas of taxation affecting companies with operations in Macau:
  - property tax – 16% of rental income;
  - industrial tax – a fixed fee of MOP300 on each business activity;
  - complementary (profits) tax – sliding scale tax rates averaging 12% on income over MOP300,000; and varying between 3% and 12% for income below this level;
  - professional tax of between 7% and 12% charged on the individual's annual income in excess of MOP120,000;
  - stamp duty of 3% on transfer of real estate worth over MOP4m; and
  - social security contributions – the monthly contribution made by the employer is MOP30 per resident employee and MOP45 per non-resident employee.
- There is no withholding tax in Macau.

Market Watch

After further relaxation of the RMB trade settlement scheme announced by the People's Bank of China (PBOC) in July 2010, the RMB business scope of banks in Macau has further expanded. However, compared to Hong Kong, services allowed in Macau are still more restricted and approval from the AMCM often needs to be sought on a case-by-case basis.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012 depend on the banking holidays listed below. Please note that all Saturdays and Sundays are non-banking days; holidays falling on Saturdays or Sundays are not shown in the list.

Holiday	Date
The day following the first day of January	2 January
Lunar New Year's Day	23 January
The second day of the Lunar New Year	24 January
The third day of the Lunar New Year	25 January
Ching Ming Festival	4 April
Good Friday	6 April
Easter Monday	9 April
Labour Day	1 May
Bank's Public Holiday	2 July
The Day following Chinese Mid-Autumn Festival and National Day	1 October
The Day following National Day	2 October
Chung Yeung Festival	23 October
All Soul Day	2 November
Macao SAR Establishment Day	20 December
Christmas Eve	24 December
Christmas Day	25 December
The first weekday following Christmas Day	26 December

Market Analysis: Malaysia

Overview	
Population	28.3 million (2010)
Total area	330,803 sq km
Capital	Kuala Lumpur
Major language(s)	Bahasa Malaysia, English, Mandarin and other Chinese dialects, and Tamil
Time zone	GMT + 8 hours
Currency	Ringgit (MYR)
Central bank	Bank of Negara Malaysia (BNM)
Gross domestic product (GDP)	416.5bn (2010); 0.6% real growth rate (2010 est.); 14,744 per capita (2010)
Inflation rate (consumer prices)	1.7% (2010)

Trade			
Total exports	USD198.9bn f.o.b. (2010)	Total imports	USD164.9bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 14.5% Fuels and mining – 17.8% Manufactured – 67.0% (2010)	Major imports (% by product group)	Agricultural – 9.7% Fuels and mining – 15.1% Manufactured – 73.2% (2010)
Major markets (% of total)	Singapore – 13.3%, China – 12.6%, European Union – 10.7%, Japan – 10.4%, US – 9.5% (2010)	Major suppliers (% of total)	Japan – 12.5%, China – 12.5%, Singapore – 11.4%, US – 10.6%, European Union – 10.2% (2010)
Total trade	USD363.8bn (2010)	Total trade with Asia	USD239.1bn (2010)

Banking System and Bank Accounts

- The financial industry is governed by the Banking and Financial Institutions Act of 1989 (BAFIA) and regulated by Bank Negara Malaysia (BNM), the central bank of Malaysia, which is responsible for monitoring and supervising the banking and financial systems of the country and administrating its exchange control regulations.

- Malaysia's banking sector has undergone consolidation in recent years. There are now eight local commercial banks, 16 foreign commercial banks, 15 investment banks, 17 Islamic banks and four international Islamic banks. An international offshore financial centre is located in Labuan, East Malaysia.
- The following types of bank accounts are currently available:

Account type		Purpose
Local currency accounts:	Current	Cheque book provided; non-interest-bearing account
	Savings[1]	No cheque book provided; interest-bearing account
	Time deposit	Interest-bearing account with various fixed maturity tenures ranging from one to 60 months
Foreign currency accounts:	Current	Cheque book provided; non-interest-bearing account
	Savings[1]	No cheque book provided; interest-bearing account
	Time deposit	Interest-bearing account with fixed maturity tenures of one, three, six, nine and 12 months

1. Corporates are prohibited from maintaining local and foreign currency savings accounts.

Clearing Systems and Payment Instruments

Clearing system	Comments
RENTAS (Real-Time Electronic Transfer of Funds and Securities)	• RENTAS is a nationwide, real-time gross settlement system (RTGS) for electronic domestic payments. • The current minimum amount for third party payments is MYR10,000 for conventional and Islamic accounts through manually initiated transactions. The minimum threshold limit for Internet banking channels is currently set at MYR10,000. There is no limit for accounts favouring RENTAS members' own accounts. • The limit is not applicable to payments in favour of BNM, federal ministries, state governments and other government bodies such as the Social Security Organisation, Employees' Provident Fund or any institutions specified by BNM.
CTCS (Cheque Truncation and Conversion System)	• Cheque truncation uses the electronic image and magnetic ink character recognition (MICR) data of the cheque and not the physical cheque to process clearing. Cheques are digitally transmitted, thus reducing time needed for payment transactions.
IBG (InterBank Giro)	• IBG, operated by MEPS (Malaysian Electronic Payment Services) since October 2000, involves an exchange of digitised transactions to effect payment orders that are less than MYR500,000 per transaction.

(table continues)

	• IBG services are currently available between participating banks that are MEPS members only. Transfer of funds between an external account[1] and resident account are allowed up to MYR5,000 per day in aggregate for any purpose.

1. An external account means a MYR account maintained with a financial institution in Malaysia by a non-resident or where the beneficiary of the funds is a non-resident.

Legal, Company and Regulatory

- In addition to BNM, other important regulatory/government bodies in Malaysia include:
  - Malaysia's Ministry of Trade & Industry (MITI);
  - Companies Commission of Malaysia (SSM);
  - Royal Malaysian Customs; and
  - The Inland Revenue Board.
- Incorporation of a local company in Malaysia includes the following procedures:
  - a name search with the SSM, using Form 13A; and
  - lodgement of incorporation documents, including:
    — memorandum and articles of association;
    — Form 48A, statutory declaration under oath by the promoter(s) of a company confirming, amongst other things, that he/she is not an undischarged bankrupt, has not been convicted/imprisoned of the prescribed offences and is consenting to act as a director of the company (minimum requirement of at least two directors resident in Malaysia);
    — Form 6, declaration of compliance with Companies Act requirements by the company secretary; and
    — Form 13A and a copy of the SSM letter approving the company's name.
- Registration of a foreign company in Malaysia follows a similar procedure in terms of name search, but the registration documents required include:
  - certified copy of the certificate of incorporation or registration of the foreign company in its home jurisdiction;
  - certified copy of the foreign company's charter, statute or memorandum and articles of association or other instrument defining its constitution;
  - Form 79, return by foreign company giving particulars of its directors and changes of particulars;
  - where the Form 79 includes directors resident in Malaysia who are members of the local board of directors, a memorandum by the foreign company stating the powers of the local directors;
  - memorandum of appointment or power of attorney authorising the person(s) residing in Malaysia, to accept service of process and notices on behalf of the foreign company;
  - Form 80, statutory declaration by agent of foreign company; and
  - Form 13A and a copy of the SSM's letter approving the company's name.

Liquidity, Currency and Tax

- Only local currency cash concentration and notional pooling are permitted in Malaysia. However, companies wishing to participate in cross-border foreign currency cash concentration can first apply for permission from BNM, under the Qualified Resident Company status, as per the BNM Foreign Exchange Administration liberalisation dated 18 May 2011 (effective from 1 June 2011). More information is available via BNM's website.

- In practice, comparatively few banks offer notional pooling because of the associated reserve requirements. Notional pool accounts are taken into account when calculating reserve requirements, so there is a cost to banks in terms of reserves they must set aside for what is effectively virtual money in the notional pool. Where banks do offer notional pooling this additional cost has to be covered. Therefore, unless there are significant countervailing considerations relating to matters such as inter-company lending/tax, notional pooling may not always prove cost-effective.
- Time deposits, wholesale money market deposits and repurchase agreements (repos) are available to companies looking for return on short- to medium-term liquidity. The Association of Banks in Malaysia (ABM) rules forbid banks from paying interest to corporates on current accounts and also forbid corporates from holding savings accounts. Repos are therefore the legally acceptable alternative. While longer term local currency commercial paper is available, liquidity and yield-to-risk options are limited.
- In its efforts to promote international trade and a conducive business environment in Malaysia, BNM has further liberalised the Foreign Exchange Administration Rules in allowing:
  - Trade settlement between residents and non-residents in MYR. Settlement by non-residents will be conducted via their MYR accounts maintained with licensed onshore banks, or by converting foreign currency into MYR with licensed onshore banks or appointed overseas branches of banking groups of the licensed onshore banks.
  - Borrowing of any amount in foreign currency by a resident company from its non-resident non-bank related company, in addition to its non-resident non-bank parent company.
  - Hedging for anticipated current account transactions to the cumulative amount received or paid in the preceding 12 months by residents with the licensed onshore banks by abolishing the limit.
  - Please refer to the BNM website for further information (www.bnm.gov.my).
- Types of income subject to withholding tax for non-residents include:

Payment type	Withholding tax rate
Contract payment[1]	10% and 3%
Interest[2]	15%
Royalty[2]	10%
Technical advice, assistance or services performed in Malaysia, rent/payment for use of moveable property	10%
Real estate investment trust (REIT):[3]	
(i) Other than a resident company	10%
(ii) Non-resident company	25%
(iii) Foreign institutional investors (e.g. pension funds, collective investment schemes)	10%

1. Where the non-resident has a permanent establishment in Malaysia.
2. Withholding tax rates may be reduced under the relevant double taxation agreement between Malaysia and the non-resident's jurisdiction.
3. The above withholding tax rate imposed on a REIT is effective from 1 January 2009 to 31 December 2011.

Market Watch

No recent or anticipated change of significance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012 are listed below. Note that holidays falling on a Sunday are observed on the following Monday.

Public holiday	Date
New Year	1 January
Chinese New Year	23-24 January
Federal Territory Day	1 February
Prophet's Mohammad's Birthday	5 February
Thaipusam*	7 February
Labour Day	1 May
Wesak Day	5 May
Malaysian King's Birthday	2 June
Hari Raya Puasa*	19 August
Hari Raya Puasa*	20 August
National Day	31 August
Malaysia Day	16 September
Hari Raya Haji	26 October
Deepavali	13 November
Awal Muharram	15 November
Christmas	25 December

** Subject to change.*

Market Analysis: Mauritius

Overview	
Population	1.3 million (2010)
Total area	2,040 sq km
Capital	Port Louis
Major language(s)	English (official language), French (widely spoken), Creole (local dialect)
Time zone	GMT + 4 hours
Currency	Mauritian rupee (MUR)
Central bank	The Bank of Mauritius
Gross domestic product (GDP)	18.2bn (2010); 0.02% real growth rate (2010 est.); 14,194 per capita (2010)
Inflation rate (consumer prices)	2.9% (2010)

Trade			
Total exports	USD2.0bn f.o.b. (2010)	Total imports	USD4.2bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 31.5% Fuels and mining – 1.0% Manufactured – 50.0% (2010)	Major imports (% by product group)	Agricultural – 23.1% Fuels and mining – 20.2% Manufactured – 56.1% (2010)
Major markets (% of total)	European Union – 63.7%, US – 10.9%, Madagascar – 5.5%, South Africa – 4.5%, Switzerland – 1.8% (2010)	Major suppliers (% of total)	European Union – 22.9%, India – 22.3%, China – 13.3%, South Africa – 8.4%, Japan – 3.3% (2010)
Total trade	USD6.2bn (2010)	Total trade with Asia	USD2.4bn (2010)

Banking System and Bank Accounts

- The central bank is the Bank of Mauritius, which acts as the local regulator for the banking industry. It does so within various acts of legislation, including the Banking Act 2004, Bank of Mauritius Act 2004, Companies Act 2001, Financial Intelligence and Anti Money Laundering Act 2002, Prevention of Terrorism Act 2002, Convention for the Suppression of the Financing of Terrorism Act 2003, Borrowers Protection Act 2007, Data Protection Act 2009 and Insolvency Act 2009.

- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	Yes[1]	Yes
Non-resident[2]	Yes	Yes	Yes[1]	Yes
Credit interest	No	Yes	No	Yes

1. Foreign currency cheque books are not available.

2. For opening of non-resident accounts, a letter of introduction from an acceptable bank may be required.

Clearing Systems and Payment Instruments

<table>
<tr><th>Clearing system</th><th>Comments</th></tr>
<tr><td>MACSS (Mauritius Automated Clearing and Settlement System)</td><td>This is a specially designed large-value interbank payment system, which is based on real-time gross settlement (RTGS) principles. It was introduced on 15 December 2000 and is operated by the Bank of Mauritius. The hours of operation are as follows:
<table>
<tr><td></td><td>Normal working day (except last working day of the month)</td><td>Last working day of the month</td></tr>
<tr><td>Start of day</td><td>9:30am</td><td>9:30am</td></tr>
<tr><td>Initial cut-off time</td><td>3:30pm</td><td>4:00pm</td></tr>
<tr><td>Final cut-off time</td><td>4:15pm</td><td>4:30pm</td></tr>
</table></td></tr>
<tr><td>Cheque Truncation System</td><td>The Bank of Mauritius officially launched the Cheque Truncation System for paper cheque clearing on 6 September 2011. However, the changeover from the manual exchange of cheques at the clearing house has not yet occurred, and is currently in a parallel run phase. The Bank of Mauritius is expected to keep the manual system until the end of 2011 when the clearing rules will be reviewed and agreed by all parties.</td></tr>
</table>

- Cash management solutions at a glance:

Investment product	Transaction management		Liquidity management
	Payments	Collections	
Time deposit Treasury bills	Cheques/demand drafts Electronic payments Corporate credit cards Direct debits Payments advising	Cash collection[1] Cheque collection[2]	Overdraft facilities[3] Auto-sweeping (in-country)

1. Cash management services are delivered via HSBCnet, HSBC's electronic banking systems.

2. Through branch network.

3. Subject to credit approvals.

- Payment capabilities and cut-off times for The Hongkong and Shanghai Banking Corporation (HBAP):

Electronic payments			
MACSS	GIRO/ACH	Payroll	International funds transfer
Yes	N/A	Yes	Yes
3:00pm	N/A	3:00pm	1:00pm/2:00pm

Applications for same day value payment in EUR should be received by 11:30am.

Applications for same day value of other foreign currency payments are subject to cut-off time related to the geographical location of the destination.

- Payment capabilities and cut-off times for HSBC Bank (Mauritius) (HBMU):

Electronic payments			
MACSS	GIRO/ACH	Payroll	International funds transfer
N/A	N/A	Yes	Yes[1]
N/A	N/A	4:00pm	4:00pm[1]

1. Depending on the currency of transfer.

Paper payments					
Local currency cheque	Foreign currency domestic cheque	Bank demand draft	Cheque outsourcing (via HSBCnet)	Petty cash	Payment advising
Yes	Yes	Yes	N/A	Yes	Yes
N/A	N/A	Available during branch hours	N/A	Available during branch hours	N/A

Legal, Company and Regulatory

- For non-banking financial services, the local regulator is the Financial Services Commission.
- The Companies Act 2001 provides for several types and categories of companies:
  - domestic company;
  - company holding a Category 1 Global Business Licence; and
  - company holding a Category 2 Global Business Licence.
- These companies may be:
  - Limited by shares: A company formed on the principle of having the liability of its shareholders limited by its constitution to any amount unpaid on the shares respectively held by the shareholder.
  - Limited by guarantee: A company formed on the principle of having the liability of its members limited by its constitution to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up.
  - Limited by both shares and guarantee: A company whose constitution limits its life to a period not

exceeding 50 years from the date of its incorporation. However, this period may be extended to a maximum of 150 years. Its constitution contains the specific matters as laid down in the law.

Liquidity, Currency and Tax

- Mauritius has free and liberal financial and money market policies with no exchange controls.
- Investment instrument options for surplus liquidity are simple; most companies use term deposits.
- Corporate income tax rate is 15%.
- There are two classifications of companies operating in the global business (offshore) sector:
  - GBC1: Category 1 Global Business Companies; and
  - GBC2: Category 2 Global Business Companies.
- Each classification has a different tax regime. A GBC1 is taxed on its chargeable income at the corporate income tax rate of 15%, but can claim a deemed foreign tax credit of 80%, thus resulting in an effective tax rate of 3%. This rate can be further reduced if the actual foreign tax paid on the chargeable income is higher. A GBC2 is tax-exempt.
- Capital gains are exempt in Mauritius.
- There is no withholding tax on interest, although there is a requirement for companies to deduct tax at 10% on interest payments to resident individuals and sociétés (partnerships).
- Profitable firms are required to spend 2% of their profits on corporate social responsibility (CSR) activities approved by the government or to transfer these funds to the government to be used in the fight against poverty.

Market Watch

Mauritius has a number of double taxation agreements already in place and is currently looking to establish more. The government is generally keen to provide incentives for the financial services industry to expand in the country. By establishing a favourable tax regime, the intention is to attract more foreign direct investment.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year	1 January
New Year	2 January
Chinese Spring Festival	23 January
Abolition of Slavery	1 February
Thaipoosam Cavadee	7 February
Maha Shivaratree	20 February
National Day	12 March
Ougadi	23 March

(table continues)

Labour Day	1 May
Assumption of the Blessed Virgin Mary	15 August
Eid-Ul-Fitr*	19 August
Ganesh Chaturthi	20 September
Arrival of Indentured Labourers	2 November
Divali	13 November
Christmas	25 December

* *The exact date of this festival is subject to confirmation as its celebration depends on the visibility of the moon.*

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Market Analysis: New Zealand

Overview	
Population	4.3 million (2009)
Total area	270,467 sq km
Capital	Wellington
Major language(s)	English and Maori
Time zone	GMT + 12 hours
Currency	New Zealand dollar (NZD)
Central bank	The Reserve Bank of New Zealand
Gross domestic product (GDP)	118.5bn (2010 est.); 0.2% real growth rate (2010 est.); 27,130 per capita (2010 est.)
Inflation rate (consumer prices)	2.3% (2010 est.)

Trade			
Total exports	USD31.4bn (2010)	Total imports	USD30.7bn (2010)
Major exports (% by product group)	Agricultural – 62.3% Fuels and mining – 8.6% Manufactured – 22.6%	Major imports (% by product group)	Agricultural – 11.0% Fuels and mining –17.5% Manufactured – 68.8%
Major markets (% of total)	Australia – 23.0%, China – 11.1%, European Union – 10.9%, US – 8.6%, Japan – 7.8% (2010)	Major suppliers (% of total)	Australia – 18.2%, China – 16.0%, European Union – 14.7%, US – 10.4%, Japan – 7.3% (2010)
Total trade	USD62.1bn (2010)	Total trade with Asia	USD38.7bn (2010)

Banking System and Bank Accounts

- The Reserve Bank of New Zealand (RBNZ) is the central bank of New Zealand. It is responsible for monetary policy, currency and the maintenance of the financial system. It also has a policy and operational role in respect of the in-country payment settlement systems.
- There are currently 21 banks registered in New Zealand. Due to the close economic ties between Australia and New Zealand, many of the local and international banks in Australia can also be found in New Zealand.

- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	Yes	Yes
Non-resident	Yes	Yes	Yes	Yes
Credit interest	Yes	Yes	Yes	Yes

Clearing Systems and Payment Instruments

New Zealand has a very developed and sophisticated cash management infrastructure. Its foundation is based on the foresight of local banks nearly 40 years ago, beginning with the creation of three centralised electronic clearing houses providing overnight settlement, securities trading, and interbank/high-value, same-day transactions. The benefits continue to accrue today, and over 90% of all payments are made electronically.

Clearing system	Comments
Interchange and Settlement Ltd (ISL)	• ISL is a low-value clearing system used for paper-based and overnight clearing files. Cheques, direct debits/credits and automatic payments are interchanged among the banks with value being given for the day the payment enters the system. • Single payments (also known as priority payments) are also cleared through ISL. These are interchanged and settled in the same manner as files – with value also given for the day the payment enters the system. • In 2012, overnight clearing files will be demised with all banks using SBI (Settlements before Interchange) intraday to settle clearing items.
Austraclear	• The primary real-time gross settlement (RTGS) system for settlement of securities trading and clearing transactions. • No minimum value requirement applies.
Same-day cleared payments (SCP)	• SCP is also used for RTGS transactions. It is commonly used for settlement of interbank, property and share transactions and some commercial payments. • No minimum value requirement applies.

Legal, Company and Regulatory

While New Zealand is a relatively deregulated environment in which to conduct business, corporates need to take into account the country's tax regulations, restrictions on cross-border transactions as well as flow of financial information in certain circumstances.

Liquidity, Currency and Tax

- New Zealand has no regulatory restrictions on pooling or cash concentration. However, while notional pooling and cash concentration are not restricted, in practice relatively few banks offer notional domestic currency pooling or cross-border cash concentration.

- There is limited commercial paper available, so most corporate surplus liquidity tends to be invested in money market and term deposits.
- While there are certain restrictions on cross-border transactions and the flow of financial information, there are no specific regulations governing foreign exchange transactions in New Zealand.
- Profits earned by a company are taxed at the company tax rate of 28% for the 2012/2013 income year.
- There is no capital gains tax in New Zealand.
- Withholding taxes levied in New Zealand vary according to domicile and category of payment (e.g. interest, dividends, royalties, etc.).

Market Watch

No recent or anticipated change of significance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Day after New Year's Day	2 January
Holiday in lieu of New Year's Day	3 January
Waitangi Day	6 February
Good Friday	6 April
Easter Monday	9 April
Anzac Day	25 April
Queen's Birthday	4 June
Labour Day	22 October
Christmas Day	25 December
Boxing Day	26 December

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Market Analysis: The Philippines

Overview	
Population	94.0 million (2010)
Total area	300,000 sq km
Capital	Manila
Major language(s)	Filipino and English
Time zone	GMT + 8 hours
Currency	Philippine peso (PHP)
Central bank	Bangko Sentral ng Pilipinas (BSP)
Gross domestic product (GDP)	368.6bn (2010); 0.5% real growth rate (2010 est.); 3,920 per capita (2010)
Inflation rate (consumer prices)	3.8%

Trade			
Total exports	USD51.6bn f.o.b. (2010)	Total imports	USD54.7bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 8.0% Fuels and mining – 6.2% Manufactured – 85.1% (2010)	Major imports (% by product group)	Agricultural – 11.7% Fuels and mining – 20.8% Manufactured – 67.0% (2010)
Major markets (% of total)	Japan – 15.2%, US – 14.7%, Singapore – 14.4%, European Union – 14.2%, China – 11.1% (2010)	Major suppliers (% of total)	Japan – 12.5%, US – 10.8%, Singapore – 9.3%, China – 8.5%, European Union – 7.3% (2010)
Total trade	USD106.3bn (2010)	Total trade with Asia	USD67.2bn (2010)

Banking System and Bank Accounts

- The Bangko Sentral ng Pilipinas (BSP), the primary regulator, issues policy guidelines for general bank supervision.
- There are 38 banks active in the Philippines, with all but three of the major local banks being majority-owned and controlled by the private sector. Foreign banks, of which there are 17, can operate as a branch or a subsidiary subject to the same regulations as the local commercial banks. The Philippines' banking sector is considered overpopulated, and the trend towards consolidation continues.

- Documentation requirements for opening corporate bank accounts include identification documents (Securities and Exchange Commission registration and articles of incorporation for corporations) to satisfy "know your customer" (KYC) requirements and a board resolution/secretary's certificate.
- If foreign corporations are registered to do business in the Philippines, there are no special requirements regarding their bank accounts. If they are not registered, then they are considered non-resident accounts and limitations in terms of repatriation of funds will apply.
- The following types of bank accounts are currently available:

Account type	Local current[2]	Local savings[2]	Foreign current[2]	Foreign savings[2]
Resident	Yes	Yes	Yes	Yes
Non-resident[1]	No	No	Yes	Yes
Credit interest	Yes	Yes	Yes	Yes

1. Accounts opened by non-resident companies must be funded by inward remittances of foreign currencies, or by over-the-counter deposits of local currency as long as there is proof that the source is income derived from a property or asset located in the Philippines.
2. Account types: CUN (current accounts) and SSV (savings accounts) are available.

Clearing Systems and Payment Instruments

Clearing system	Comments
Philippine Clearing House Corporation (PCHC) local cheque clearing	This is a paper-based clearing system operated by PCHC, which is the only entity authorised by BSP to clear cheques in Metro Manila and its integrated regions. Local currency cheques and cashier's orders take three working days to clear.
PCHC regional cheque clearing	Local currency cheques presented by banks and branches located in specific provinces are cleared through BSP and PCHC. These cheques will take four days to clear.
Provincial cheques for collection	Cheques presented through areas not mentioned in either local or regional clearing are mailed to these areas and cleared in approximately 30-45 working days. Such items are also referred to as out-of-town cheques.
PCHC PHP and US dollar (USD) foreign exchange clearing	Funds in local currency can be electronically transferred between member banks' head offices through PCHC end-of-day-netting. Electronic interbank transfers are now settled within 24 hours or by the next working day. The cut-off time is 4:00pm.
PDDTS (Philippines Domestic Dollar Transfer System)	The PDDTS has online, real-time and end-of-day batch netting transfer capabilities with final settlement on the same day. All USD transfers processed via the real-time gross settlement (RGTS) mode are delivered through PDDTS online. The cut-off time is 3:00pm.

(table continues)

PPS (Philippine Payment System or PhilPaSS)	The PhilPass is the Philippines' version of RTGS for PHP. Payments are sent via SWIFT and same-day transfer is provided within set cut-off times, with settlement on the same day via BSP. The cut-off time is 3:00pm.

- Clearing systems in the Philippines are owned and operated by the Banker's Association of the Philippines (BAP), which in turn is owned by BAP member banks.
- Many banks offer cheque outsourcing and low-value electronic payments. Some also offer on-site cheque-writers and payments advising.
- Banks with nationwide branch networks allow over-the-counter deposit of cheques and cash at any point in the network to a single account. Foreign banks, whose branch networks are not as extensive, will usually partner with local banks, enabling payments through the latter's branches into a central account. Both local and foreign banks offer collections outsourcing via a third-party courier. Electronic collections via direct electronic debit of accounts are implemented within a single bank as the country lacks the infrastructure to enable this seamlessly on an interbank basis.

Legal, Company and Regulatory

- Apart from the central bank, other relevant regulatory bodies include the Securities and Exchange Commission, the Insurance Commission and the Philippine Deposit Insurance Corporation.
- There are no minimum capitalisation requirements for companies in unregulated industries, but these do apply in the case of the financial services industry. This distinction also applies to local subsidiaries of foreign corporations.

Liquidity, Currency and Tax

- Some banks offer automated sweeping and cash concentration services. Overdrafts and, consequently, offsetting of negative and positive balances, are not allowed in the Philippines. Notional pooling is not allowed.
- The most common investment instruments for surplus liquidity are time deposits, but there is also some activity in commercial paper and other money market instruments.
- There are several restrictions and regulatory requirements that are intended to curb speculative attacks against PHP, which is not readily convertible into other currencies.
- Corporate income tax is levied at 32%, while a 20% withholding tax is applied to all interest income. Documentary stamp tax applies to all time deposit products. Any interest paid on a deposit account that is 50% higher than the regular CASA rates is also subject to documentary stamp tax. There are no offshore/onshore distinctions as regards corporate taxes.

Market Watch

In general, the regulatory landscape in the Philippines is fluid. Therefore any corporation contemplating direct foreign investment in the Philippines is well-advised to seek professional advice in advance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	1 January
Chinese New Year	23 January
Maundy Thursday	5 April
Good Friday	6 April
Araw ng Kagitingan	9 April
Labor Day	1 May
Independence Day	12 June
Ninoy Aquino Day	21 August
National Heroes Day	27 August
All Saints Day	1 November
Additional special (non-working) day	2 November
Bonifacio Day	30 November
Christmas Day	25 December
Rizal Day	30 December
Last Day of the Year	31 December

Note: The proclamations declaring national holidays for the observance of Eid'l Fitr and Eidul Adha shall hereafter be issued after the approximate dates of the Islamic holidays have been determined in accordance with the Islamic calendar (Hijra) or the lunar calendar, or upon Islamic astronomical calculations, whichever is possible or convenient. To this end, the National Commission on Muslim Filipinos (NCMF) shall inform the Office of the President on which day the holiday shall fall.

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Market Analysis: Singapore

Overview	
Population	5.1 million (2009)
Total area	705 sq km
Capital	n/a
Major language(s)	English, Malay, Mandarin and Tamil
Time zone	GMT + 8 hours
Currency	Singapore Dollar (SGD)
Central bank	Monetary Authority of Singapore (MAS)
Gross domestic product (GDP)	292.9bn (2010); 0.4% real growth rate (2010 est.); 56,694 per capita (2010 est.)
Inflation rate (consumer prices)	2.8%

Trade			
Total exports	USD353.6bn f.o.b. (2010)	Total imports	USD310.9bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 2.2% Fuels and mining – 17.3% Manufactured – 72.2% (2010)	Major imports (% by product group)	Agricultural – 3.5% Fuels and mining – 27.6% Manufactured – 64.9% (2010)
Major markets (% of total)	Malaysia – 11.9%, Hong Kong – 11.7%, China – 10.3%, European Union – 10.0%, Indonesia – 9.4% (2010)	Major suppliers (% of total)	European Union – 12.3%, Malaysia – 11.7%, US – 11.5%, China – 10.8%, Japan – 7.9% (2010)
Total trade	USD664.5bn (2010)	Total trade with Asia	USD419.6bn (2010)

Banking System and Bank Accounts

- The Monetary Authority of Singapore (MAS) is the central bank of Singapore. It formulates and executes Singapore's monetary policy, manages its foreign reserves and issues Singapore's currency and government securities. As supervisor and regulator of Singapore's financial services sector, it has prudential oversight over the banking, securities, futures and insurance industries.
- Singapore's three large local banking groups, DBS, UOB and OCBC dominate the local retail banking

scene. In order to liberalise the banking sector in Singapore, MAS has awarded qualifying full bank status to a number of foreign banks, which will allow them to open up to 25 sub-branches or offsite automated teller machines. Other foreign banks have been awarded wholesale bank status to allow them to serve commercial customers in Singapore.

- Documentation requirements for opening bank accounts for local corporations include items such as the necessary corporate authorisations, shareholder list, memorandum and articles of association, etc. However, for foreign corporations wishing to open bank accounts there are additional requirements, including:
  - certificate of incumbency issued by professional/registered agent or a director's declaration detailing particulars of the directors and principal shareholders;
  - certification letter from a certified public accountant/lawyer of a European Union/Financial Action Task Force member jurisdiction certifying that the information contained in the certificate of incumbency or director's declaration is correct and accurate;
  - certified true copy of certificate of good standing (for tax haven countries); and
  - letter of authorisation to debit account opening fee (for tax haven countries).
- The following types of bank accounts are currently available:

Account type	Local current	Local savings[1]	Foreign current	Foreign savings[1]
Resident	Yes	Yes	Yes	Yes
Non-resident	Yes	Yes	Yes	Yes

1. In Singapore, savings accounts are not offered to corporates.

Clearing Systems and Payment Instruments

- MAS governs the cheque and electronic clearing system in Singapore. All banks adopted the five-day clearing week system on 15 May 2006. There are three principal clearing systems in Singapore:

Clearing system	Comments
MAS Electronic Payment System (MEPS+)	MEPS+ is a real-time gross settlement (RTGS) system. It enables instantaneous and irrevocable transfer of funds (SGD) and Singapore government securities. The cut-off times are 4:30pm for electronic instructions and 3:30pm for paper instructions.
Cheque Truncation System (CTS)	The CTS is an image-based automated clearing system for SGD and locally issued US dollar cheques. It is operated by Banking Computer Services Pte Ltd (BCS). All banks participating in this clearing system use image-based technology to provide a cheque clearing service. The cheque deposit cut-off times are: • For SGD cheques: — Monday to Wednesday, 3:00pm. Funds available on the next banking day after 2:00pm; — Thursday, 3:30pm. Funds available the next banking day after 2:00pm; and

(table continues)

	— Friday, 3:30pm. Funds available the next banking day after 2:00pm. • For USD cheques: — Monday to Friday, 1:00pm. Funds available on the next banking day after 2:00pm.
eGIRO System (automated clearing house – ACH)	The eGIRO system is also operated by BCS. It is designed for electronic transfer of high-volume smaller-value payments. The cut-off time is 5:00pm.

Legal, Company and Regulatory

- Singapore's regulatory environment is among the least restrictive in the world and is complemented by a similarly competitive tax environment. Low withholding taxes and double taxation agreements with more than 50 countries provide a favourable environment for large corporates looking to establish regional treasury centres.
- MAS does not encourage the internationalisation of the SGD; therefore, restrictions apply to the extension of credit facilities that are denominated in SGD to non-resident financial institutions.
- The banking secrecy provisions of the Banking Act of Singapore prohibit the disclosure of customer information except in circumstances permitted in the Act.
- Singapore provides incentives (mainly tax-related) for locating a company's operational headquarters (OHQ) or a finance and treasury centre (FTC) in Singapore. There are also incentives for locating regional treasury centres (RTC), subject to pre-defined minimum criteria set out by the Singapore government.
- A foreign entity may invest in Singapore either through a locally registered branch or an incorporated subsidiary. There is no restriction on the percentage of equity ownership, nor any restriction on the repatriation of profits out of the country, so funds can easily be remitted in and out of Singapore.
- In general, there are no minimum capitalisation requirements in Singapore (except for financial institutions) and there are no thin capitalisation rules. Further information on regulatory requirements can be found at www.acra.gov.sg

Liquidity, Currency and Tax

- Singapore has a large number of treasury centres, managing foreign exchange and liquidity on behalf of the region. In general, there are no restrictions on liquidity management structures in Singapore, enabling complex structures to be put in place. This applies to both cash concentration and notional pooling on both a multiple- or single-currency basis. This enables large multinational companies to set up their regional liquidity centres and shared service centres in Singapore.
- A wide range of local yield enhancement options are available for surplus liquidity. Interest-bearing local and foreign currency current accounts are commonly used, as well as money market funds and structured deposits.
- Singapore's liberal financial system generally does not have any currency or capital controls. However, banks have to observe the government's policy of discouraging the internationalisation of the SGD (as mentioned earlier). MAS's policy on the non-internationalisation of the SGD essentially restricts the lending of SGD by banks in Singapore to non-resident financial institutions for the purpose of speculation in the SGD currency market:

- Banks in Singapore may not extend aggregate SGD credit facilities exceeding SGD5m to non-resident financial institutions where they have reason to believe that the proceeds may be used for speculation against SGD.
- For a SGD loan to a non-resident financial institution exceeding SGD5m or for a SGD equity or bond issue arranged by a bank in Singapore for a non-resident financial institution where the proceeds will be used to fund overseas activity, the SGD proceeds must be swapped or converted into foreign currency before remitting outside Singapore.

- These SGD lending restrictions do not apply to non-resident financial institutions and there is currently a large offshore market in SGD abroad.
- The prevailing corporate tax rate in Singapore is 17% (from 2010 onwards) and there is no capital gains tax. Certain payments made to non-residents are subject to Singapore withholding tax.
- For more information, please refer to the Inland Revenue Authority of Singapore website (www.iras.gov.sg).
- Whether there are any tax considerations arising from cash concentration/pooling schemes will depend on the circumstances of each case and companies are well advised to seek independent tax advice in this respect.
- The Direct Tax Code (DTC) Singapore-India Tax Treaty:
  - Income of foreign institutional investors from transfer of investment assets is to be classified as capital gain.
  - Distinction between long-term capital gains and short-term capital gains has been eliminated.
  - Withholding tax rate on other types of income has been arrived at.
  - Test of residence: In line with the international practice, it is now proposed that a company incorporated outside India will be treated as resident in India if its "place of effective management" is situated at any time in the year in India.
  - The DTC is expected to replace the Income-tax Act, 1961, from 1 April 2012.
  - Taxation of the income earned from securities has been fixed at 20%.

Market Watch

- Singapore Budget 2011:
  - As part of the Singapore Budget 2011, the Government of Singapore will commit SGD850m as part of the Enterprise Development Fund over the next five years, to be administered by SPRING Singapore and IE Singapore. This is a substantial increase of about 45% from the previous five-year tranche. One of the priorities of the Fund is to help high-growth enterprises in their overseas expansion.
  - To ensure continued support beyond the first five years for the long-term effort to restructure industries, the Government of Singapore will top up the National Productivity Fund with another SGD1bn in 2011. This will bring the total fund size to its target of SGD2bn. This fund was set up in 2010 for initiatives customised to specific industries, clusters and enterprises, with a focus on sectors with the potential for large gains in productivity.
  - To support businesses that are globalising and earning a larger share of their income overseas, foreign tax credit pooling is being introduced to facilitate remittance of foreign income to businesses' Singapore bases. Such pooling will give businesses greater flexibility in the use of their foreign tax credits, reduce tax payable, as well as simplify tax compliance.
  - To enable the Economic Development Board (EDB) to continue its efforts to strengthen Singapore's value proposition as an Asian base for corporate headquarters and other high-value activities, SGD2.5bn will be set aside under the Economic Assistance Scheme.

- Recommendations by the Economic Strategies Committee (ESC):

The Government of Singapore established the ESC in May 2009 to develop strategies for Singapore to maximise the opportunities in a new world environment with the aim of achieving sustained and inclusive growth. The key recommendations of the ESC are as follows:

- Singapore needs to boost skills in every sector by developing an outstanding nationwide system of continuing education and training to give everyone the opportunity to acquire greater proficiency, knowledge and expertise.
- Singapore will have to deepen capabilities among Singapore companies to seize opportunities in Asia. While the MNC strategy remains key, there is considerable opportunity in the next five to 10 years to attract global mid-sized companies and to facilitate local companies to grow into industry leaders in Asia. The ESC recommends measures to develop the market for cross-border financing to help companies expand abroad with specific focus on reaping the commercial potential of Singapore's science and technology base.
- Singapore must become a distinctive global city. The ESC is of the view that Singapore's future rests on growing a deep pool of highly capable and entrepreneurial people and it must continue to attract top quality people from around the world, while investing further to provide the best opportunities for Singaporean talents to grow and develop to the highest levels of expertise in a range of fields. The ESC also recommends support for the growing creative and arts clusters, which will add to the character of the city, and nurture new talents.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
New Year's Day	1 January
Chinese New Year	23-24 January
Good Friday	6 April
Labour Day	1 May
Vesak Day	5 May
National Day	9 August
Hari Raya Puasa	19 August*
Hari Raya Haji	26 October
Deepavali	13 November**
Christmas Day	25 December

Source: Ministry Of Manpower, Singapore, 16 June 2011

** The following Monday will be a public holiday.*

*** The date, 13 November 2012, for Deepavali needs to be checked against the Indian almanac when it is available. Should there be a change in date, the Ministry of Manpower will issue a media release to announce the change.*

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Market Analysis: Sri Lanka

Overview	
Population	20.4 million (2010)
Total area	65,610 sq km
Capital	Colombo
Major language(s)	Sinhala, Tamil, and English
Time zone	GMT + 5.5 hours
Currency	Sri Lankan rupee (LKR)
Central bank	The Central Bank of Sri Lanka
Gross domestic product (GDP)	105.5bn (2010); 0.1% real growth rate (2010 est.); 5,169 per capita (2010)
Inflation rate (consumer prices)	5.9% (2010)

Trade			
Total exports	USD8.4bn f.o.b. (2010)	Total imports	USD15.5bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 30.1% Fuels and mining – 1.0% Manufactured – 65.0% (2010)	Major imports (% by product group)	Agricultural – 15.3% Fuels and mining – 24.0% Manufactured – 58.6% (2010)
Major markets (% of total)	European Union – 35.0%, US – 21.3%, India – 5.6%, UAE – 3.0%, Russian Federation – 2.9% (2010)	Major suppliers (% of total)	India – 20.6%, Singapore – 13.1%, European Union – 12.4%, China – 10.1%, Iran – 5.3% (2010)
Total trade	USD23.9bn (2010)	Total trade with Asia	USD12.1bn (2010)

Banking System and Bank Accounts

- The Central Bank of Sri Lanka (CBSL) is the primary authority for the regulation of all banks and financial institutions in Sri Lanka. As the central bank, CBSL is responsible for formulating monetary policy, maintaining the stability of the country's financial system and currency management.
- The Sri Lankan banking sector accounts for 56.7% of the local financial sector in terms of assets. There are 22 commercial banks, 11 of which are foreign and 11 local.
- Under CBSL regulations, banks are authorised to operate offshore foreign currency banking units

(FCBU), which are free from exchange control regulations. The FCBU allows for foreign currency dealings by non-residents and companies approved by the Board of Investment (BOI) – see the Legal, Company and Regulatory section.

- Documentation required for opening corporate bank accounts include identification documents such as business registration, memorandum and articles of association, etc. to satisfy "know your customer" (KYC) requirements and a board resolution/secretary certificate.
- The following types of bank accounts are currently available:[1]

Account type	Local current	Local savings	Foreign current	Foreign savings
Local registered	Yes	Yes/Interest bearing (IB)	Yes (domestic banking unit – DBU)	No
Local registered with BOI approval	Yes	Yes/IB	Yes (FCBU)[2]	Yes (FCBU)/IB
Local registered with Export Development Board	Yes	Yes/IB	Yes (DBU)	Yes (DBU)/IB
Local registered – professional service providers (FCAPS)	Yes	Yes/IB	Yes (DBU)	Yes (DBU)/IB
Local registered – hoteliers	Yes	Yes/IB	No (but if opened under FCAPS, yes)	Yes (DBU)/IB
Local registered – suppliers of material input	Yes	Yes	Yes (DBU)	Yes (DBU)
Local registered – shippers/airlines on behalf of parent company	Yes	No	Yes (DBU)	No
Overseas registered	Yes – non-resident SLR account; share investment external SLR account; treasury bond investment external SLR accounts	Yes under special foreign direct investment account	Yes (FCBU)	Yes (FCBU or DBU under SFDIA)/IB

1. Please note that these are basic account types that are guided by exchange control circulars.

2. FCBU accounts can be opened by companies incorporated outside Sri Lanka or by companies with BOI approval. In the FCBU, accounts are not subjected to exchange control restrictions but must be maintained in approved foreign currencies, which are Australian dollar, Canadian dollar, Danish krone, euro, Hong Kong dollar, Norwegian krone, Singapore dollar, sterling, Swedish krona, Swiss franc, US dollar and yen. FCBU savings accounts would be in the form of call deposits or time deposits only.

Clearing Systems and Payment Instruments

- The Sri Lanka Automated Cheque Clearing House (SLACH) was established in 1988 and is responsible for providing automated cheque clearing facilities. It has considerably reduced the time required to clear local cheques and is at T+1, increasing the efficiency of the banking system. The central bank manages and sets the rules for the country's clearing system. Since February 2002, SLACH has been operated by the private company LankaClear (Pvt) Ltd.
- Interbank payments, such as money market, foreign exchange (FX) settlements and other bank transfers, are handled electronically through the real-time gross settlement (RTGS) system. High-volume, low-value payments are routed through the Sri Lanka Interbank Payment System (SLIPS) and is T+0 for vendor payments and at most T+1 for other payments such as payroll.
- The Cheque Imaging and Truncation System (CITS) is the interbank cheque clearing system that has been used by all commercial banks in Sri Lanka since April 2006. Inward clearance cheque images and details are received from LankaClear (Pvt) Ltd (the company's major shareholders are the CBSL and two state banks) and loaded onto the CITS. The images and details are verified, and respective customer accounts are debited. Outward clearance cheque images and details are loaded onto the CITS and burnt onto a CD, which is sent to LankaClear at the end of the day. LankaClear then performs the reconciliation based on the clearing rules set by the central bank.

Clearing system	Comments
Sri Lanka Automated Cheque Clearing House (SLACH)	The Sri Lanka automated cheque clearing house is responsible for providing automated cheque-clearing facilities, which include cheque imaging and truncation. It is managed by LankaClear. There is also a system to clear locally issued US dollar cheques.
Sri Lanka Interbank Payment System (SLIPS)	SLIPS is used for high-volume, low-value payments, although the system can also handle larger-value interbank transfers as well. The present threshold is LKR5m.
Real-time gross settlement (RTGS) system	The RTGS system is used for large value payments such as money market, FX settlements and other bank transfers.

Legal, Company and Regulatory

- Apart from the CBSL, another significant regulator is the BOI. Any foreign incorporated company investing in Sri Lanka (or a Sri Lankan company making a large capital investment) can apply to the BOI for Board of Investment status. This essentially grants these companies a host of tax incentives. Additionally, certain BOI-approved companies can maintain and operate their banking accounts in the FCBU, which is exempt from most exchange control regulations.

Liquidity, Currency and Tax

- In terms of liquidity management, automatic sweeping of funds between accounts is permitted, while cross-currency and cross-border cash concentration is not feasible due to regulatory constraints on FX conversion, and tax and accounting considerations.
- Cash pooling is offered in the FCBU and DBU as well.
- Cash concentration facilities are available in Sri Lanka.

- There are exchange control restrictions and the conversion of LKR to foreign currency for remittances is permitted under specifically stated conditions and with supporting documents. Companies registered with the BOI or foreign companies opening accounts in Sri Lanka are not subject to these conditions when debiting foreign currency accounts in the FCBU. However, under the new budget directives exchange controls have been relaxed in a number of areas, such as the ability of foreign investors to invest in rupee-denominated debentures issued by local companies, Sri Lankan companies to borrow from foreign sources, foreign tourists and businesses to open foreign currency accounts, Sri Lankan residents to invest in equities of foreign companies, etc.
- Non-financial companies will pay corporation tax at 28% from 1 April 2011 (formerly it was at 35%). This excludes alcohol and tobacco companies, which will pay 40% corporation tax from 1 April 2011.
- Withholding tax is levied at 10% on all interest earned on deposits held in LKR in a DBU account for corporates. Charities and partnerships are levied an 8% withholding tax. However, if interest is being paid on USD balances, then withholding tax does not apply.

Market Watch

- With the ending of the civil war the government has undertaken a series of initiatives to double the per capita income in Sri Lanka to USD4,000 by 2016 and develop the country into a regional hub for ports and aviation, knowledge and education, business processing outsourcing (BPO), etc. Successive budgets by the incumbent government have set the stage for an accelerated development plan that includes setting the right environment to encourage foreign direct investment.
- Sri Lanka has already relaxed some of its existing capital restrictions; for example, foreign investors can now invest in LKR accounts with the ability to repatriate the funds. The authorities are currently considering further relaxation of the remaining capital restrictions. There are restrictions in the remittance of funds overseas that are permitted under pre-defined categories with specific documentary requirements.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Duruthu Full Moon Poya Day	8 January
Tamil Thai Pongal Day	15 January
Special bank holiday in lieu of Tamil Thai Pongal, which falls on a Sunday	16 January
Additional half holiday in lieu of the National Day, which falls on a Saturday	3 February
National Day	4 February
Milad un Nabi (Holy Prophet’s Birthday)	5 February
Nawam Full Moon Poya Day	7 February
Special bank holiday in lieu of the Holy Prophet's Birthday, which falls on a Sunday	10 February

(table continues)

Mahasivarathri Day	20 February
Medin Full Moon Poya Day	7 March
Bak Full Moon Poya Day	6 April
Good Friday	6 April
Day Prior to Sinhala and Tamil New Year Day	12 April
Sinhala and Tamil New Year Day	13 April
May Day	1 May
Wesak Full Moon Poya Day	5 May
Day following Wesak Full Moon Poya Day	6 May
Special bank holiday in lieu of the Day following Wesak Full Moon Poya Day, which falls on a Sunday	7 May
Poson Full Moon Poya Day	4 June
Esala Full Moon Poya Day	3 July
Nikini Full Moon Poya Day	1 August
Id-Ul-Fitr (Ramazan Festival Day)	19 August
Adhi Binara Full Moon Poya Day	31 August
Binara Full Moon Poya Day	29 September
Id-Ul-Alha (Hadji Festival Day)	26 October
Vap Full Moon Poya Day	29 October
Deepavali Festival Day	13 November
Il Full Moon Poya Day	27 November
Christmas Day	25 December
Unduvap Full Moon Poya Day	27 December

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Market Analysis: Taiwan

Overview	
Population	23.2 million (2010)
Total area	35,961 sq km
Capital	Taipei
Major language(s)	Putonghua (Mandarin), Taiwanese (a Fujianese-based dialect), and English
Time zone	GMT + 8 hours
Currency	New Taiwan dollar (TWD)
Central bank	The Central Bank of Taiwan
Gross domestic product (GDP)	824.7bn (2010); 1.1% real growth rate (2010 est.); 35,604 per capita (2010)
Inflation rate (consumer prices)	1.0%

Trade			
Total exports	USD274.6bn f.o.b. (2010)	Total imports	USD251.2bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 2.0% Fuels and mining – 7.1% Manufactured – 85.4% (2010)	Major imports (% by product group)	Agricultural – 5.3% Fuels and mining – 28.0% Manufactured – 65.2% (2010)
Major markets (% of total)	China – 26.7%, Hong Kong – 14.5%, US – 11.6%, European Union – 10.5%, Japan – 7.1% (2010)	Major suppliers (% of total)	Japan – 20.8%, China – 14.0%, US – 10.5%, European Union – 9.0%, Korea – 6.0% (2010)
Total trade	USD525.8bn (2010)	Total trade with Asia	USD328.4bn (2010)

Banking System and Bank Accounts

- The Central Bank of the Republic of China (CBC) is responsible for monetary policy and foreign exchange (FX) regulations, ensuring the sound operation of banks and exchange rate stability.
- Documentation required for opening bank accounts in Taiwan is not particularly onerous and includes standard items such as the company's business licence and certificate of registration.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes	No	Yes
Non-resident	No	Yes	No	Yes[1]
Credit interest	No	Yes	No	Yes[1]

1. Restrictions on non-residents opening foreign currency savings accounts in domestic banking units apply.

2. Foreign currency current accounts are not allowed by regulation.

Clearing Systems/Mechanisms and Payment Instruments

There are three major local currency clearing systems in Taiwan: the cheque clearing infrastructure for paper-based payments (TCH), Financial Information Service Co. Ltd (FISC) and the automated clearing house (ACH) for electronic payments:

Clearing system	Comments
TCH (Taiwan Clearing House) cheque clearing system	• Local currency paper-based cheque clearing system, which is operated by the Taiwan Clearing House (TCH) with three major cheque clearing centres and 12 clearing branches throughout Taiwan. • For cheque clearing, the TCH uses magnetic ink character recognition (MICR) technology in the clearing process. The process is automated in Taipei, Taichung and Kaohsiung. Local cheques are usually printed in Chinese. • It normally takes two working days to clear a cheque drawn in the same city, and five to seven working days to clear a cheque drawn in another city. • Post-dated cheques (PDCs) are commonly used for payments as well as credit instruments, since most local banks provide PDC discounting services.
FISC (Financial Information Service Co.) electronic funds transfer systems	• A multi-purpose interbank electronic fund transfer system developed and operated by FISC to allow banks to share common resources, exchange financial information and implement the overall automation of financial services. • The system is Chinese character-based and provides TWD same-day value interbank transfers. Included in the FISC system are several other sub-systems, such as the shared cash dispenser/automated teller machine (ATM) system, Interbank Remittance System, and the Financial Electronic Data Interchange System. • The most widely used system is the Interbank Remittance System, with a total of 107 financial institution participants.
	• FISC allows real-time transfer of funds between client accounts maintained with banks. • It is used to settle all kinds of wire transfers, both low and high value. • In January 2011, FISC, working jointly with Mega Bank, a local bank, launched the domestic USD clearing system limited for the domestic

(table continues)

	transfers of USD among member banks. Membership of the USD domestic clearing system is different from the TWD clearing system.
ACH (TCH – Automated Clearing House) automatic clearing system	• An automated clearing house operated by the TCH that is used to settle low-value/high-volume electronic payments in batches. • ACH allows for the direct electronic debiting and crediting of individual and/or corporations' banking accounts. Because of this feature, ACH is normally used for payment/collection of utility bills, payment of salaries, insurance premiums and cash dividends. • Bank customers send a list of account entry transactions to the originating bank for processing. The originating bank then transfers the transaction data to the TCH, which clears the debits and credits by the receiving bank, then transmits the balancing statements to the central bank for settlement. • The clearing time is two days for debit transfers and one day for credit transfers, with funds available on the next banking day.

Legal, Company and Regulatory

- Apart from the CBC, the other major regulatory authority is the Financial Supervisory Commission (FSC), established in 2004 with a view to consolidating the supervisory responsibilities of banking, securities and insurance sectors in Taiwan. The four bureaus under the FSC are the Banking Bureau, the Securities and Futures Bureau, the Insurance Bureau and the Examination Bureau.
- The main laws governing financial institutions include the Banking Act, the Securities and Exchange Act, the Futures Trading Act and the Insurance Act.

Liquidity, Currency and Tax

Liquidity Management

- The following table summarises the products and services available under current regulations:

Products category	Notional pooling	Sweeping
Account type	Savings account Current account	Savings account only
Currency	TWD only	Both TWD and foreign currencies (can only sweep among accounts in the same currency)
Physical movement of funds	No	Yes
Geography	Onshore	Onshore
Right of offset/Cross-guarantee	Yes	No

Investments

- TWD and foreign currency fixed-term deposits are the most popular investment instruments for surplus liquidity. The tenor of these can range from one month to up to three years, or even longer for TWD. For foreign currencies, tenors range from overnight up to usually a maximum of one year. Simple interest is paid at maturity. A 10% tax is withheld from interest paid to residents while 20% is withheld from non-residents.
- Overnight deposits in TWD are not available (although they are available in other currencies) and the alternative of bond funds is not popular due to credit risk considerations. Commercial paper under a repurchase agreement (repos) is a popular instrument due to the flexibility in tenor.

Foreign Exchange

- Under the CBC current FX regulations, settlement of foreign currencies against the TWD and vice versa fall under three categories:
  - FX receipts from the export of goods or provision of services.
  - FX disbursements for import of goods or services provided by non-residents.
  - FX receipts/disbursements from other sources, such as investments, capital repatriation and dividends.
- Trade-related FX (categories 1 and 2 above):
  - There is no limit to the amount of FX settlement against trade-related transactions, as long as the supporting documents are provided to the FX bank at the point of settlement. Eligible supporting documents include letters of credit, documents against acceptance/payment invoices and sales/purchase contracts.
- Non-trade-related FX settlements (category 3 above):
  - The limits for settlement of non-trade related FX are as follows:

Entity	Settlement of FX receivables	Settlement of FX payables
Taiwan registered business	USD50m	USD50m
Taiwan individual residents	USD5m	USD5m

- Foreign nationals without an alien resident certificate and overseas entities not registered as businesses in Taiwan are allowed to convert between TWD and foreign currencies but are subject to a limit of USD100,000 or equivalent per transaction.
- All conversions of foreign currencies into TWD or vice versa are subject to CBC reporting and declaration requirements. FX conversions of TWD500,000 or more must be reported to the CBC by completion of a standard CBC declaration form. In the case of companies, the declaration form must be completed with the company's official seal(s). For corporates, supporting documents such as invoices or the agreement or approval letter issued by the government are required when the deal amount is in excess of USD1m.
- The following is a summary of the rules governing corporates/institutions:

Amount	FX declaration form	Supporting documents
Less than TWD500,000	Not required	Not required
Less than USD1m	Required	Not required
Equal to or larger than USD1m	Required	Required

- The detailed implementation of the basic FX/conversion-related regulations outlined above may still be subject to CBC's interpretations.

Corporate Tax Rate

- In June 2010, the Income Tax Act was amended to reduce the corporate income tax rate from 25% to 17%, applied retroactively to take effect from 1 January 2010 onwards. Following this cut, Taiwan's corporate tax rate is one of the lowest in Asia. There is a withholding tax on dividend payments of 20%. Interest paid on foreign currency deposit accounts opened by non-residents with an offshore banking unit (OBU) (see www.banking.gov.tw/public/Attachment/4121316115771.doc) is not subject to income tax. However, TWD accounts are not available in OBUs.

Market Watch

No recent or anticipated change of significance.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Lunar New Year Holidays	23-27 January
Peace Memorial Day	27-28 February
Children's Day, Tomb Sweeping Day	4 April
Labour Day	1 May
National Day	10 October
New Year's Day	31 December

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Market Analysis: Thailand

Overview	
Population	63.9 million (2010)
Total area	513,120 sq km
Capital	Bangkok
Major language(s)	Thai
Time zone	GMT + 7 hours
Currency	Baht (THB)
Central bank	The Bank of Thailand (BOT)
Gross domestic product (GDP)	589.0bn (2010); 0.8% real growth rate (2010 est.); 9,221 per capita (2010)
Inflation rate (consumer prices)	3.3%

Trade			
Total exports	USD195.4bn f.o.b. (2010)	Total imports	USD184.6bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 18.0% Fuels and mining – 6.2% Manufactured – 72.5% (2010)	Major imports (% by product group)	Agricultural – 6.6% Fuels and mining – 22.0% Manufactured – 67.0% (2010)
Major markets (% of total)	European Union – 11.2%, China – 11.0%, Japan – 10.5%, US – 10.4%, Hong Kong – 6.7% (2010)	Major suppliers (% of total)	Japan – 20.8%, China – 13.3%, European Union – 7.6%, US – 5.9%, Malaysia – 5.9% (2010)
Total trade	USD380.0bn (2010)	Total trade with Asia	USD233.2bn (2010)

Banking System and Bank Accounts

- The Bank of Thailand (BOT) plays the role of the central bank in Thailand and is the key policymaker governing the banking industry.
- The regulated nature of Thailand's banking industry allows the largest five local commercial banks to dominate the banking businesses. There are a total of 57 banks operating in the country, comprising:
  - 14 Thai commercial banks;
  - one retail bank;

- one subsidiary bank;
- 15 foreign bank branches; and
- 26 foreign bank representatives.

- In 2009, BOT introduced the Financial Sector Master Plan Phase II, aiming to reduce system-wide operating costs and promote competition and financial access including permitting existing foreign banks to request opening of up to two additional branches.
- For companies registered outside Thailand, the documents required for opening a bank account include the following (please note other similar/different documents will be required for different types of business incorporation):
  - board of directors' resolution or letter of intention to open corporate account;
  - certified true copy of the company's certificate of incorporation;
  - certified true copy of the official document detailing particulars of directors and secretary;
  - certified true copy of the company's licence/permission to conduct specific business;
  - certified true copy of the company's memorandum and articles of association;
  - certified true copy of the list of shareholders or similar document e.g. declaration letter showing principal shareholder(s) who is/are entitled to control or exercise the control, whether directly or indirectly, of 10% or more of the voting rights of a company; and, if any, bearer shares indicating who, directly or indirectly, holds 5% or more of the total shares of the company;
  - bearer share declaration form, if applicable, showing who, directly or indirectly, holds 5% or more of the total shares of the company;
  - certified true copy of passports of principal shareholders, directors and all authorised signatories; and
  - certified true copy of proof of residential address (and permanent address if different from the residential address).
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident[4]	Yes[1]	Yes[1]	Yes[2]	Yes[2]
Non-resident[4]	Yes[3]	Yes[3]	Yes[3]	Yes[3]
Credit interest	No	Yes	No	Yes

1. No restrictions are applied to residents opening THB accounts; Thai residents are discouraged from holding overseas accounts. Approval from BOT is accordingly required, especially if deposits into those overseas accounts are made with funds of domestic origin. It is rare for BOT to permit this unless it is proved necessary and allowed under the governing act of the applicant.

2. For resident foreign currency accounts where the foreign currency originates from abroad, there is no deposit limit and no need for documentation showing future foreign currency obligations. If the source of foreign currency originates from within Thailand, deposit of such foreign currency can be classified into two types, with and without an obligation:

— For foreign currency deposits with an obligation, the deposit limit is USD100m. If residents deposit more than USD100m, the obligation within a 12-month period must be presented. The deposit should not exceed the obligated amount.

— For foreign currency deposits without an obligation, the deposit limit is USD500,000.

Any transfer and withdrawal should be accompanied by supporting documents and reported.

For foreign currency deposits in a current account, a cheque book is not available.

3. No restrictions are applied to non-residents opening foreign currency accounts; however, non-resident THB accounts are prohibited from having outstanding balances at the end of each day exceeding THB300m, inclusive of all THB accounts of the same non-resident opened with onshore banks. Cheque facilities are not available for non-resident THB accounts held in Thailand because of the difficulty of BOT reporting requirements.

4. Funds deposited from resident to non-resident accounts must be accompanied by payment obligation documents (evidence of obligation for service).

Clearing Systems and Payment Instruments

- BOT operates six clearing systems in Thailand:

Clearing system	Comments
Electronic cheque clearing (ECS) system	The ECS is used for processing and clearing cheques from commercial banks in Bangkok and the metropolitan area. It has been in operation since July 1996.
BOT automated high-value transfer network (BAHTNET, RTGS)	BAHTNET is an electronic network linking users to BOT's current account system. BAHTNET participants are commercial banks, specialised banks, non-bank financial institutions, and certain departments of BOT. Settlement via BAHTNET is done on a real-time gross settlement (RTGS) basis.
Bulk Payment System (formerly known as SMART/ Media Clearing)	Bulk Payment System is a retail funds transfer (credits and debits) system for transactions occurring on a recurring basis. BOT is the centre for executing funds transfers to any branch of all banks throughout Thailand. The system provides interbank clearing for small-value transfers, including payroll and dividend transfers on the credit side and payments of household utility bills on the debit side. In late 2006, BOT changed its policy by having its role as the operator (central switching centre) assumed by a private company called National Interbank-Transaction Management and Exchange (NITMX). NITMX will become the central switching centre for SMART systems in Thailand, in order to allow BOT to concentrate on its role overseeing the system as the regulator. In October 2007, the Bulk Payment operator migration was completed for credits. In July 2008, Bulk Payment credit same day went live allowing customers to instruct same-day automated clearing house (ACH) transactions. For Bulk Payment debit, only next day debit is available. The live date for same day debit is yet to be confirmed.
Provincial cheque clearing	For provinces outside Bangkok, cheque clearing within the same province takes one day at local clearing houses (managed by commercial banks or BOT representatives) located in provincial centres and some large districts. Provincial clearing house regulations are based on agreement among members but do not differ from the standard format. Clearing house operations have changed gradually from a manual to a computerised system to increase efficiency. Clearing of cheques deposited in the same province but paid in different districts takes three to five business days, depending on transportation and distance.
Cross Zone Upcountry Cheque Clearing (BC-3D)	Cheques are sent to the head office of the drawee bank, and the head office of the issuing bank processes cheque clearing with its branch within three business days upon exchanging the physical cheque with the collecting bank.
Imaged Cheque Clearing and Archive System (ICAS)	New cheque clearing system using digital images instead of physical cheques in the clearing process to enhance efficiency by shortening the

(table continues)

	cheque clearing cycle to only one day nationwide and to eliminate cheque transportation costs. The new system is scheduled to launch in Bangkok and metropolitan areas on 3 February 2012 and the roll-out nationwide is to be advised.

- In addition to BOT, another significant regulatory body is the Anti-Money Laundering Office (AMLO), which serves as the financial intelligence unit (FIU) for law enforcement agencies in Thailand.
- Note: For regulations related to anti-money laundering and countering the financing of terrorism (AML/CFT), HSBC Thailand is required to comply with both the Hong Kong Monetary Authority's Guideline/Supplement to the Guideline on Prevention of Money Laundering and Thailand's Anti-Money Laundering Act.

Legal, Company and Regulatory

- In order to establish a limited company in Thailand, the following steps are required:
  - corporate name reservation;
  - three natural persons or more to act as promoters;
  - filing of a memorandum of association;
  - convening a statutory meeting;
  - registration of company; and
  - tax registration.
- There are no minimum capitalisation requirements for companies incorporated in Thailand, but capitalisation should be adequate for the intended business operation and in practice, at least THB50,000 in registered capital would be appropriate.

Liquidity, Currency and Tax

- Non-residents can open and maintain foreign currency accounts with authorised banks in Thailand without any restrictions.
- Notional pooling (both domestic and cross-border) is permitted, but only domestic cash concentration is allowed. Cross-border cash concentration is allowed only if the company concerned has obtained a treasury centre licence from BOT.
- For cash concentration, inter-company interest earnings will be subjected to special business tax (SBT) of 3.3%, if lender and borrower have cross-holdings of less than 25%, such stakes must be held for at least six months before lending activities. All inter-company interest earnings are subjected to withholding tax (WHT) of 1%.
- Popular local investment instruments for surplus liquidity include:
  - time deposits;
  - bills of exchange;
  - structured bills of exchange;
  - treasury bills; and
  - government bonds (e.g. bonds issued by BOT).
- Foreign exchange (FX) regulations apply in case onshore banks undertake FX transactions involving THB with non-residents. For further information please consult the FX regulations on BOT's website.
- Corporate income tax is levied at 30% of net profit and is due twice each fiscal year. A mid-year profit forecast is used as the basis for advance payment of corporate taxes.
- A value-added tax (VAT) of 7% is levied on the value added at each stage of the production process, and is applicable to most firms. It must be paid on a monthly basis.

- A specific business tax, based on gross receipts, is levied on firms engaged in certain categories of business not subject to VAT at a variable rate ranging from 0.1% to 3.0%.

Market Watch

- In August 2008, BOT released guidelines governing banks' use of electronic banking services. All banks offering these services in Thailand must now comply with the guidelines, which cover electronic funds transfer, security/internal controls and prevention of fraud.
- BOT has issued the schedule for the release of the Image Cheque Clearing and Archive System (ICAS). The roll-out will start in the Bangkok area in November 2011, with plans for the system to be used nationwide by 2012.
- Under the Deposit Protection Agency Act, which provides protection to THB deposits of Thai residents, on 11 August 2011, the amount of protection was reduced from 100% to THB50m per bank per legal entity. On 11 August 2012, the amount of protection will be further reduced to THB1m per bank per legal entity. This is considered an important change in the market, especially for the corporate segment where the average balance is substantially beyond the amount protected by the Deposit Protection Agency. Hence, a bank's credit rating becomes a key consideration for customers.

Clearing Systems Holidays 2012

Days on which the clearing systems are not in operation in 2012:

Holiday	Date
Substitution for New Year's Eve and New Year's Day	2 January
Additional holiday	3 January
Makha Bucha Day	7 March
Chakri Day	6 April
Songkran Festival	13 April
Substitution for Songkran Festival	16 April
National Labour Day	1 May
Substitution for Coronation Day	7 May
Wisakha Bucha Day	4 June
Asarnha Bucha Day	2 August
Substitution for H.M. the Queen's Birthday	13 August
Chulalongkorn Day	23 October
H.M. the King's Birthday	5 December
Constitution Day	10 December
New Year's Eve	31 December

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Market Analysis: Vietnam

Overview	
Population	88.3 million (2010 est.)
Total area	331,212 sq km
Capital	Hanoi
Major language(s)	Vietnamese, with English, French, Chinese spoken widely in the business community
Time zone	GMT + 7 hours
Currency	Dong (VND)
Central bank	The State Bank of Vietnam (SBV)
Gross domestic product (GDP)	277.4bn (2010); 0.4% real growth rate (2010 est.); 3,143 per capita (2010 est.)
Inflation rate (consumer prices)	9.2% (2010)

Trade			
Total exports	USD69.8bn f.o.b. (2010)	Total imports	USD83.4bn c.i.f. (2010)
Major exports (% by product group)	Agricultural – 18.9% Fuels and mining – 11.6% Manufactured – 68.9% (2010)	Major imports (% by product group)	Agricultural – 9.8% Fuels and mining – 12.7% Manufactured – 72.0% (2010)
Major markets (% of total)	US – 20.0%, European Union – 16.5%, Japan – 11.1%, China – 9.5%, Switzerland – 4.4% (2010)	Major suppliers (% of total)	China – 22.2%, Singapore – 10.0%, Japan – 9.8%, Korea – 9.6%, Taiwan – 8.7% (2010)
Total trade	USD153.2bn (2010)	Total trade with Asia	USD93.7bn (2010)

Banking System and Bank Accounts

- State Bank of Vietnam (SBV) is the top regulatory and supervisory entity of the banking sector. SBV operates throughout the country in 64 branches located in each city and province of Vietnam. Besides the SBV, other regulators such as the Ministry of Planning and Development and the Ministry of Finance also impact the banking industry.

- There are six state-owned commercial banks, 37 joint-stock commercial banks, five joint-venture banks, 48 branches of foreign banks, four foreign banks, and a social policy credit system. Foreign banks can enter Vietnam's banking sector by setting up a representative office, foreign bank branch, establishing a joint-venture bank with a domestic commercial bank, establishing a 100% foreign-owned bank or taking ownership of up to 20% of shareholding in a domestic bank.
- Documentation required for opening corporate bank accounts includes identification documents such as business registration, memorandum and articles of association, etc. to satisfy "know your customer" (KYC) requirements and a board resolution/secretary certificate.
- The following types of bank accounts are currently available:

Account type	Local current	Local savings	Foreign current	Foreign savings
Resident	Yes	Yes[4]	Yes[1]	Yes[1,4]
Non-resident	Yes[2]	Yes[4]	Yes[5]	Yes[4]
Credit interest	Yes[3]	Yes[4]	Yes[3]	Yes[4]

These accounts are corporate accounts. Saving accounts are payment accounts that earn interest.

1. Foreign currency payments require supporting documents.

2. Non-resident organisations can open VND accounts but transactions are restricted and supporting documents required.

3. Subject to approval of local managers.

4. Subject to the deposit cap rate regulated by SBV from time to time.

5. Foreign currency transactions between two non-residents do not require supporting documents but foreign currency transactions between non-residents and residents require supporting documents for specific purposes as stipulated in Decree 160/2006.

Clearing Systems and Payment Instruments

- CITAD, the interbank payment clearing system, is the central payment clearing system and is run by the SBV. Since 5 April 2008, CITAD has been operating with two value categories. Low-value clearing is classified as any transaction with a value below VND500m, with anything at or above that threshold being classified as high value. The cut-off time for low-value payments is 3:00pm and high-value payments at 3:45pm.
- Low-value clearing charges are levied on a fixed-fee basis, while high-value charges are levied according to the actual value.
- Both value categories operate on a same-day value.
- Cheques are not generally used in Vietnam, so the country has effectively moved directly from using physical cash to same-day transfers for local currency clearing. As a result, the clearing environment is particularly efficient from a cash management perspective, with fast collections/payments, less paperwork and fewer manual processes.
- Payments are required to be made through banks in order to receive value added tax (VAT) refunds, except for transactions below VND20m, according to 2.3 Article 12 – Law on Value Added Tax13/2008/QH12.

■ Cash management solutions at a glance:

Investment product[1]	**Transaction management** — **Payments**	**Transaction management** — **Collections**	**Liquidity management**[1]
• Local currency/ foreign currency statement savings • Time deposits • Treasury products: — Swap — Forward	• Local outward transfer • Overseas outward transfer • Bulk payments • Principal protection • Payroll service • Standing instruction • Payments advising • Monthly billing • XCS (Xpress Collection Services) (payment documents) • Cash withdrawal over HSBC's counters • Cash withdrawal over the counters of local alliance banks	• Local inward remittance • Overseas inward remittance • Direct debit • Virtual account • Bills payment facility • Cash deposit over HSBC's counters • Cash collection (deposit over the counter and on-site cash pick-up) via local alliance banks • Point-of-sale (POS) collection provided by local alliance banks • Cash collection via Vietnam Post • Cheque collection (overseas cheque collection offered on a case-by-case basis)	• Notional pooling and cash concentration offered on a selective basis • Working capital financing/ credit lines

1. Cash management services are delivered via HSBCnet, HSBC's electronic banking systems.

■ Payment capabilities and cut-off times:

Electronic payments			
RTGS	GIRO/ACH	Payroll	International funds transfer
Yes	Yes	Yes	Yes
2:00pm	2:00pm	2:00pm	2:00pm

Paper payments					
Local currency payments	Foreign currency payments	Bank demand draft/Cheque	Cheque outsourcing (via HSBCnet)	Petty cash	Payment advising
Yes	Yes	Yes	No	Yes	Yes
1:00pm	1:00pm	Available during branch hours	N/A	Available during branch hours	N/A

Legal, Company and Regulatory

- In addition to SBV and the Ministry of Finance, the Ministry of Planning and Investment plays an important regulatory role in matters such as the issuing of investment licences, etc.
- Capitalisation rules apply; wholly owned subsidiaries of foreign companies can only borrow up to the investment capital approved in their investment licence (issued by the Ministry of Planning and Investment) with a medium- to long-term tenor overseas loan.
- Foreign direct investment (FDI) enterprises are required to register all medium- and long-term overseas loans (loan tenors above 12 months) with SBV prior to funds disbursement.
- Different company licences will allow different scopes of business activities. A representative office licence has the highest restrictions vis-à-vis wholly owned subsidiaries of foreign companies, which have more latitude.
- In some cases, foreign companies may be required to establish a company bank account in Vietnam first as the details of the bank account are required to be submitted as part of the information in the business registration process.
- In general, the regulatory environment in Vietnam can be complex and is constantly evolving, so taking professional advice in advance of any action is advisable.
- Foreign currency transactions are subject to foreign exchange control of SBV under Decree 160.

Liquidity, Currency and Tax

- Overdrafts are permitted in Vietnam, so there is some leeway for notional pooling and /or cash concentration services. However, this is only permitted in VND.
- All US dollar (USD) activities are monitored by the regulators and transfers require supporting documentation.
- Term deposits are commonly used as instruments for investment of surplus liquidity. Tiered credit interest rates on current accounts are also popular.

Market Watch

- The Vietnamese government has become far more particular about supporting documentation for foreign currency outward remittances. In the past, it was relatively easy for corporations to buy USD to pay dividends or to make payments to suppliers offshore. Supporting documentation showing the underlying commercial transaction must be provided to the remitting bank prior to remittance.
- For a client buying foreign currency to settle an invoice, banks can only sell the client the foreign currency mentioned in the invoice, unless there is a clause in the client's commercial contract stating that both buyer and seller agree that payment can be made in a different currency.
- The requirement for supporting documents is currently creating bottlenecks for banks as it takes more administrative time than anticipated.

Clearing Systems Holidays 2012

Below is a list of public holidays in Vietnam in 2012. Please note that holidays falling on a Saturday or Sunday will be observed on the following working day.

Holiday	Date
New Year's Day	1 January
Lunar New Year's Eve	22 January
Lunar New Year's First Day	23 January
Lunar New Year's Second Day	24 January
Lunar New Year's Third Day	25 January
Hung Kings' Anniversary	31 March (10 March Lunar Year)
Liberation Day	30 April
Labour Day	1 May
National Day	2 September

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Glossary of Terms

acceptance The act of giving a written undertaking on the face of a usance bill of exchange to pay a stated sum on the maturity date indicated by the drawee of the bill, (usually in exchange for documents of title to goods shipped on documents-against-acceptance terms).

acceptance credit A letter of credit which requires the beneficiary to draw a usance bill for subsequent acceptance by the issuing bank or the advising bank or any other bank as the credit stipulates.

accepting bank The bank that accepts a bill of exchange drawn on it under a letter of credit.

account analysis A statement, usually monthly, produced by a company's bank that summarises the transaction activity, cash balance and charges on each account held.

accounts payable (A/P) Ledger of balances owed by a company for purchases.

accounts receivable (A/R) Ledger of balances owed to a company for sales.

accreditation Formal process of certifying a particular process or function usually linked to service quality (e.g. ISO 9001 accreditation).

ACFTA ASEAN-China Free Trade Area.

ACH Automated clearing house – capable of handling automated electronic domestic payments, usually used for low-value clearing systems (e.g. BACS in the UK and ECG/autopay in Hong Kong).

advising bank The bank that advises the letter of credit at the request of the issuing bank. It is usually a bank in the beneficiary's country.

AFTA ASEAN Free Trade Area.

agency A role in which a bank or trust institution manages assets in which the title remains with the owner.

amendment An alteration to the terms and conditions of the letter of credit. Following the applicant's request, the amendment originates from the issuing bank and is advised to the beneficiary by the advising bank. Irrevocable credits (almost all credits are irrevocable) cannot be amended unless the beneficiary agrees.

APEC Asia Pacific Economic Cooperation.

applicant The party, usually the importer, on whose request the letter of credit is issued. Sometimes referred to as the opener or accountee.

ASEAN Association of South East Asian Nations.

ASP Application service provider – an ASP provides customers with application hosting and related services over the Internet that would otherwise have to be located and supported in-house.

authentication A software security device that creates a check sum using a confidential algorithm attached to the message. It is tested to ensure no changes have been made to any message components in transit. Used where a message is not secret and does not require encryption.

auto-invest A method of cash concentration where balances in operating accounts are swept to an interest-bearing account for overnight investment purposes.

available funds Funds that are available for withdrawal and so have good value.

avalise The act by a bank in guaranteeing payment of a bill of exchange or promissory note by endorsing the reverse with the words "good per aval" and signed by the bank, or by the issuance of a separate guarantee.

B2B Business-to-business – e-commerce conducted between two or more businesses.

B2C Business-to-consumer – e-commerce conducted between a business and consumers.

back value The adjustment to the posted value date of a transaction debited or credited to an account, with the effect of providing a debit or credit item with an earlier value date.

back-to-back credit A credit issued against the security back of another credit (master credit) on the understanding that reimbursement will stem from documents eventually presented under the first credit (master credit) issued. It follows therefore that each side of a back-to-back transaction covers the shipment of the same goods.

BACS Bankers' Automated Clearing Services – BACS Limited is a company established to operate the UK's automated clearing house (see ACH above), handling lower-value bulk clearing for both GBP credits and direct debits on behalf of the 17 major banks and building societies. Banks sponsor corporate customers into BACS.

BADT Bank accounts debit tax – imposed on debit transactions made to accounts with a cheque book facility (other than exempt accounts held with banks) in all states and territories in Australia.

bankers' acceptances A time or sight draft drawn on a commercial bank by a borrower, usually in connection with a commercial transaction. The borrower is liable for payment, as is the bank, which is the primary obligor, to pay the draft at its face amount on the maturity date. Used primarily to finance the export, import, shipment or storage of goods.

Basel II The new accord proposed by the Basel Committee for Banking Supervision calls for minimum capital requirements, supervisory review and market discipline in the industry to replace the current accord set in 1998.

Basel III The third Basel accord was developed in response to deficiencies in financial regulation revealed by the financial crisis. Basel III strengthens bank capital requirements and introduces new regulatory requirements on bank liquidity and bank leverage.

basis point The unit that represents the minimum interest rate change of 0.01%.

beneficiary The party in whose favour a letter of credit is issued and who will receive payment under it if the terms are met.

bilateral netting A system in which purchases between two subsidiaries in the same group are netted against each other, periodically (typically monthly) and only the net difference is transferred.

bill for collection Document(s) or cheque submitted through a bank for collection of payment from the drawee.

bill of exchange An unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time, a certain sum in money to or to the order of a specified person, or to the bearer. It is usually referred to in a letter of credit as a draft.

BIS The Bank for International Settlements, located in Basel, Switzerland, has evolved into an important international monetary institution, and provides a forum in which central bankers meet and consult on a monthly basis. As an independent financial organisation, the BIS performs a variety of banking, trustee and agent functions, primarily with central banks.

B/L Bill of lading – a document created for a given shipment that indicates the contents and destination, and forms a contractual basis for claims or resolution with the carrier if required.

bond Security issued by a borrower to a lender, covering short- or long-term debt at variable or fixed interest rate.

cap A contract between a borrower and a lender whereby the borrower is assured that he or she will not have to pay more than a specified maximum interest rate, or cap, on borrowed funds.

capital market A market in which long-term capital is raised.

carrier Person or company undertaking, for hire, the conveyance of goods, e.g. a shipping company.

cash concentration A facility by which balances of several accounts are physically aggregated through a funds transfer mechanism. Funds actually move between accounts. Cash concentration types include: zero balance accounts (ZBA); target balance accounts; and auto-invest accounts.

cash flow forecasting Identifying and/or forecasting known future cash receipts and obligations, and calculating cash balances for each future date in order to cover shortfalls and invest surpluses.

cash management The effective forecasting, monitoring and management of liquid resources:

- Maximising access to liquidity and minimising deficit positions at optimal cost.
- Controlling cash flow on a cross-border basis.
- Optimising funding/investments of cash/debt.
- Controlling/minimising risk.

cash pooling The notional offsetting of multiple balances for the purposes of calculating interest on the net balance. In contrast to cash concentration (see cash concentration above), there is no actual movement of funds. Interest is debited/credited to a designated master or header account, although some corporations/banks will reallocate interest rates. Single currency cash pooling is most common although cross-currency and cross-border pooling is offered by some banks.

central bank reporting A requirement in many countries to report cross-border and currency transactions to the local monetary authority. This can be done by transaction or summary, and is often done by banks on behalf of their customers.

centralised (treasury) A structure in which a group treasury has responsibility for all treasury activities. Operating companies maintain limited treasury responsibility locally, usually for commercial reasons.

CEPA Closer Economic Partnership Arrangement – a free trade agreement between mainland China and Hong Kong SAR, signed on 29 June 2003.

certificate of deposit (CD) A form of time deposit at a bank or savings institution; a time deposit cannot be withdrawn before a specified maturity date without being subject to an interest penalty for early withdrawal. Small-denomination CDs are often purchased by individuals. Large CDs are often in negotiable form, meaning they can be sold or transferred among holders before maturity.

CHAPS Clearing House Automated Payments System – the London-based credit transfer/settlement system designed to handle high-value electronic interbank payment traffic on an online real-time gross settlement basis. Payments are secure (through authentication and encryption) and settlement, with same-day value, is unconditionally guaranteed. CHAPS is SWIFT-compatible and transactions are irrevocable at the time they enter the system.

CHATS Clearing House Automated Transfer System – the Hong Kong SAR-based settlement system under the control of the Hong Kong Association of Banks. CHATS operates on an RTGS basis.

CHIPS Clearing House Interbank Payments System – a New York-based settlement system.

CIF Cost, insurance and freight – An international trade term of sale in which, for the quoted price, the seller/exporter/manufacturer clears the goods for export and is responsible for delivering the goods past the ship's rail at the port of shipment (not destination).

clean Used to describe a draft or cheque with no shipping documents (collections transactions), or to describe a bill of lading without clauses that expressly declare a defective condition of the goods or the packing.

cleared balance The funds in a customer's account that are available for withdrawal by the customer.

clearing cycle The time taken for transfer instructions to pass between bank branches and clearing centres to enable payment.

clearing house An institution where mutual claims are settled between accounts of member depository institutions. Clearing houses among banks have traditionally been organised for cheque-clearing purposes, but more recently have cleared other types of settlements, including electronic funds transfers.

CLS Continuous Linked Settlement – CLS is an industry initiative that aims to significantly reduce foreign exchange settlement risk through simultaneous exchange of net currency values.

collar A floating rate debt contract that establishes a maximum and minimum interest rate to be paid by the borrower.

commercial paper A relatively low-risk short-term unsecured form of borrowing.

confirmation The confirmation and matching of transactions (normally treasury) usually matching (system) through an external, independent system, but it may also be done by an internal independent system or an internal treasury management system (TMS). Standing data such as the bank's contact, name and address will be matched with the transaction details. The system will then automatically match the corporation's transaction details with the bank's record. The system will require a pre-defined level of authorisation to produce the confirmation, which will not require manual signature. In trade, confirmation refers to a definite undertaking of the confirming bank, in addition to that of the issuing bank, to honour or negotiate a complying presentation.

consumables Supply items such as liquids and specialised types of tooling that are consumed in the production process.

controlled disbursement (account) A technique used in the US to enable a widely dispersed group to fund its disbursement banks to match cheque clearing on a same-day basis.

convertible security A bond or preferred stock that the holder can convert into new stock instead of obtaining repayment.

Core Principles for Systemically Important Payment System (CPSIPS) Chaired by the Bank for International Settlements (BIS), The Committee on Payment and Settlement Systems (CPSS) established a Task Force on Payment System Principles and Practices in May 1998 to consider what principles should govern the design and operation of payment systems in all countries. These principles were set out as CPSIPS.

correspondent bank   A bank that acts as an agent for another bank, generally in a region in which it does not have a suitable presence itself.

cover   The term used to describe funds in the currency of a payment transferred between banks to support (cover) a payment order.

CRM   Customer relationship management. CRM encompasses methodologies, software and usually Internet capabilities that help an enterprise manage customer relationships in an organised way.

cut-off time   Latest time of day at which a transaction can occur to ensure standard settlement is achieved (e.g. value today).

daylight overdraft   An intra-business-day customer overdraft creating a temporary exposure to the bank providing the facility.

debenture   An unsecured long-term loan taken by a company, usually with a maturity of 15 years or more. Debentures are marketable securities.

debit card   A card that resembles a credit card but which debits a transaction account (cheque account) with the transfers occurring contemporaneously with the customers' purchases. A debit card may be machine-readable, allowing for the activation of an automated teller machine or other automated payment equipment.

decentralised (treasury)   A structure where day-to-day treasury activities are managed at the operating company level, rather than at the group level. In practice, there is usually a split of responsibilities between group treasury and the operating units.

deferred payment credit   A letter of credit that allows the nomination of a bank, or the issuing bank to effect payment against stipulated documents at a maturity date as specified or determinable from the wording of the credit.

delivery versus payment (DVP)   The standard method of settling securities transactions whereby delivery of the security is made on the same day as the payment.

demand deposit   A deposit payable on demand.

deposit reconciliation   A service that enables deposits from multiple locations, being credited to a single corporate account, to be identified and reported. Also known as branch consolidation services.

derivatives   Instruments that are valued according to the expected price movements of underlying assets, which may be commodities, currencies or securities.

DES-based security   Data encryption standard – used to secure data transmitted electronically.

digital signature   A digital signature can be used to authenticate the identity of the sender of an electronic message. The signature will be different for each message or document being signed.

direct debit   A means of authorising recurring payments (e.g. mortgage or insurance payments) to be drawn on an account.

documents against acceptance   Instruction for commercial documents to be released to the drawee on acceptance of the bill of exchange.

documents against payment   Instruction for documents to be released to the drawee only on payment.

documents of title   Documents that give their owner the right to the goods, i.e. the bill of lading.

double taxation agreement   A treaty between two countries to ensure that residents are not doubly taxed on the same source of income in more than one country.

DPO   Days payable outstanding – the number of days on average a company takes to pay its accounts payable.

draft   An instrument drawn on a bank that cannot be dishonoured due to lack of funds (e.g. it is guaranteed). Drafts can be negotiable or non-negotiable. In trade, a draft is a bill of exchange issued by an exporter and submitted to the bank for collection, or under a letter of credit – usually submitted with attached shipping documents.

DSO   Days sales outstanding – the number of days on average a company takes to collect its accounts receivable.

e-banking   Electronic banking – an application supplied by a bank to support the transmission of information, payments, advice, etc. by electronic means to or from a customer.

e-cheque   An electronic version of a paper cheque that uses the same legal and business protocols associated with traditional paper cheques and can be used in similar transactions.

e-commerce   Electronic commerce – the exchange of business information from one organisation to another in an electronic format in some mutually agreed standard.

e-procurement   This is the automated buying and selling of goods and services between qualified corporate users over the Internet.

EAI   Enterprise application integration – technologies designed to help integrate the different data and business processes among networked applications in an organisation.

eBAM   Electronic bank account management

EBPP   Electronic bill presentment and payment – the invoicing and payment process for consumers in B2C applications.

EDI   Electronic data interchange – any system used to exchange business data electronically that avoids manual re-keying and eliminates paperwork.

EDIFACT EDI for administration, commerce and transport. It is the standard adopted by the United Nations for business messages, and is managed by SWIFT.

EFT Electronic funds transfer – a payment in which the payer sends a payment instruction to a bank by electronic means. The payment is then made automatically by the bank using SWIFT or a similar domestic system. Fixed format counterparty lists are often used to speed up regular payments.

EFTPOS Electronic funds transfer at point of sale.

EIPP Electronic invoice presentment and payment – the invoicing and payment process between businesses in B2B applications.

EMU European Monetary Union.

encryption A process that "scrambles" a message so that it cannot be read by someone who may intercept it.

enterprise-wide systems Systems that span an entire organisation, providing end-to-end functionality.

entrusted loans Loans for which funds have been provided by a third party, who bears the repayment risk, and the lender acts only as an administering party and receives a handling fee. Also known as entrust loans.

ERP Enterprise Resource Planning systems are accounting-oriented information systems for identifying and planning the business-wide resources needed to handle all aspects of customer orders. ERPs are designed to automate the business processes of medium-sized and large businesses.

escrow This is a mode of settlement for a trade that requires the keeping of monies in trust by a third-party intermediary (a bank).

escrow accounts Accounts in which conditions apply restricting access to the funds. For example, funds will be left to accumulate to pay taxes or insurance on mortgaged property.

exchange control Regulation requiring a level of prior approval for cross-border transactions. Such approval may be delegated to major banks to simplify the process.

factoring A finance technique in which a business sells invoiced receivables at a discount to a bank or finance house (the factor) or to an internal finance company. The factor may or may not accept the incumbent credit risk.

Federal Open Market Committee (FOMC) In the US, a 12-member committee consisting of the seven members of the Federal Reserve Board and five of the 12 Federal Reserve Bank presidents. The committee sets objectives for the growth of money and credit that are implemented through purchases and sales of US government securities in the open market. The FOMC also establishes policy relating to system operations in the foreign exchange markets.

Federal Reserve System The Fed is the focal point for domestic US funds movement. For cheque (Fed) clearing, the Fed receives cheque deposits from depository institutions and then clears the cheque back to the drawer bank. The Fed operates FEDWIRE and is the main operator of the ACH system that clears electronic payments.

FEDI Financial EDI – the standard EDIFACT formats for communicating financial information are:

- payext – payment instruction (incl. remittance advice);
- creadv – credit advice;
- payord – payment instruction;
- paymul – multiple payment instructions;
- bansta – bank statement information;
- remadv – remittance advice; and
- dirdeb – direct debit instruction.

The electronic transmission of payments and payment-related information in standard formats between company trading partners and/or their banks. FEDI includes electronic format for invoices, initiation of payments, lockbox deposit reports and remittance information sent either directly to a trading partner or processed through a financial or communications intermediary.

FEDWIRE A nationwide US electronic payments system operated by the Fed for high-value low-volume same-day USD wire transfers. FEDWIRE payments are irrevocable.

financial instruments (FIs) Formal financial documents such as options, futures and other financial contracts, usually used for speculative and hedging purposes and derived from other basic assets or rates such as stocks and currency rates.

financial leverage The ratio of long-term funds with a fixed interest charge, such as debentures, that comprise a company's capital to its ordinary share capital.

float The elapsed time from the date an asset or liability is incurred until its final settlement (e.g. the money represented by cheques in transit between deposit and payment). Float can be broken down as follows:

- billing float;
- mail float;
- internal processing float;
- collection float (availability and presentation float); and
- advice float.

FOB Free on board – the seller delivers when the goods pass the ship's rail at the named port of shipment. The buyer has to bear all costs and risks of loss of or damage to the goods from that point. The FOB term requires the seller to clear the goods for export. This term can be used only for sea or inland waterway transport. If the parties do not intend to deliver the goods across the ship's rail, the free carrier (FCA) term should be used.

foreign currency (FCY) account An account held in a currency that is not the local currency in the country in which the account is held.

foreign exchange Purchase or sale of the currency of one nation with that of another. Foreign transactions exchange rates refer to the number of units of one currency needed to purchase one unit of another, or the value of one currency in terms of another.

forfaiting Forfaiting means selling a bill of exchange, at a discount, to a third party, the forfaiter, who collects the payment from, essentially, an overseas customer, through a collateral bank(s), and, thus, assuming the underlying responsibility of exporters and simultaneously providing trade finance for importers by converting a short-term loan to a medium term one.

forward exchange A type of foreign exchange transaction whereby a contract is made to exchange one currency for another at a fixed date in the future at a specified exchange rate. By buying or selling forward exchange, businesses protect themselves against a decrease in the value of a currency they plan to sell at a future date.

freight Goods or the cost of transporting goods.

future An agreement to buy or sell a particular commodity, currency or security for delivery at a fixed date in the future at a fixed price.

gateway A bank that is a full member of a clearing system and which acts as the point of access for non-member banks to submit and receive payments.

giro systems Centralised payments systems, common in Europe, generally operated by using direct debits and credits. In many cases a term analogous to ACH. Giro systems can be classified into paper-based giro (i.e. paper-based credit transfers) and electronic giro (i.e. direct debits, standing orders and direct deposits) depending on the types of payments and the processing system. Interbank giros allows the transfer or payment of funds from one financial institution to an account maintained with another financial institution.

good value This is the availability of funds for use (e.g. a deposited cheque only provides good value once it has cleared and the funds may be withdrawn).

group treasury The finance function with overall responsibility for treasury activities within a group of companies, including any regional or in-country treasury operations. Responsibilities will vary depending on whether the treasury function is centralised or decentralised.

hedging The use of techniques or instruments to reduce existing exposure to price, interest rate and/or foreign currency movements. The effectiveness of a hedge is measured in terms of the residual gain or loss that results from a rate, price or currency movement after taking account of any hedging.

Herstatt risk The risk of loss in the capital value of a currency transaction, where one side of the bargain is completed, but completion on the other side is delayed.

HSBC Autopay A bulk payments service available through HSBC's Internet banking channel – HSBCnet. Autopay allows for the automation of low-value instructions such as vendor or salary payments.

HSBC Connect HSBC Connect provides secure host-to-host integration between a company's systems infrastructure and HSBC. It is specifically designed for corporate and institutional clients to manage the transmission of large volumes of information and transaction data to and from HSBC.

ICC The International Chamber of Commerce is the international body that promotes and facilitates world trade, and which codifies world trade practices in various publications.

IMF International Monetary Fund.

in-house bank An internal treasury function that acts as a main counterparty for other group companies (e.g. FX and funding).

Incoterms ICC Publication No. 560 entitled "Incoterms 2000" defines and describes the official rules for the interpretation of the most commonly used international trade terms (FOB, CIF, etc.)

interbank market The part of a money market in which banks lend to each other and to large financial institutions, usually for very short periods and often overnight.

interest rate swap The exchange between counterparties of a fixed interest rate and floating interest rate in a single currency.

interface, host-to-host The method of establishing a connection between two or more computing environments. Host-to-host interface popularly refers to a process wherein mainframe computers exchange data ("talk") to each other. Such environments are typically used for global and high-volume applications, and often require customisation to be able to interface with other systems.

intranet A closed network based on Internet protocols belonging to an organisation, usually a corporation, accessible only by the organisation's members, employees or others with authorisation. Like the Internet itself, intranets are used to share information and intranet web sites look and act just like those on the Internet.

invitation to tender (ITT) Cash management industry standard terminology for the document prepared by a company and issued to one or more banks detailing their cash management requirements. (See also RFI and RFP).

ISDN Integrated speech and data network – operated by telecommunications companies for rapid transmission of data.

kitting The process of collecting and grouping materials that serve as components of an assembled presentation, product or package.

LAN Local area network (linking computers).

LC Letter of credit – a conditional undertaking by a bank to make payment, often abbreviated to credit. More precisely, it is a written undertaking by a bank (issuing bank) given to the seller (beneficiary) at the request of the buyer (applicant) to pay a sum of money against presentation of documents complying with the terms of the credit within a set time limit.

leading and lagging A tax-efficient technique enabling cash-rich companies in a group to "lead" intercompany settlements to those companies in a deficit position to avoid using short-term borrowing facilities. Conversely, cash-poor companies may "lag" payments to companies in the group that have a positive cash flow position.

letter of hypothecation A promise to hold goods as security taken from customers who are granted loans against goods imported on a collection basis.

LIBOR London interbank offered rate (also HIBOR, Hong Kong interbank offered rate; JIBOR, Jakarta interbank offered rate, etc.). The interest rate quoted by banks for lending to other prime banks. It varies constantly and is the recognised basis for calculating a floating interest rate, usually agreed as LIBOR plus a spread. LIBOR rates are quoted for a number of currencies. LIBID is the rate at which the banks will take deposits.

lifting charges Transaction costs associated with the movement of funds calculated as a percentage of the transaction value (particularly prevalent in Germany).

liquidity risk The risk that an entity may not have the funds available to meet its cash flow needs and will be unable to meet its debt obligations.

lockbox A collection service in which a post office box is maintained in the name of a customer but operated by a bank. Cheques and, increasingly, trade documents or payment instructions, are deposited in the "lockbox" collected by the bank, and processed by staff at the bank. Customers receive details of the items deposited in electronic or hard copy format. Services include retail and wholesale, domestic and international lockbox.

logistics The management of business operations, such as the acquisition, storage, transportation and delivery of goods along the supply chain. Logistics is that part of the supply chain process that plans, implements, and controls the efficient, effective flow and storage of goods, services, and related information from the point of origin to the point of consumption in order to meet customers' requirements.

logistics network The linked set of resources used in moving and storing material at the required location and time, which can be classified as external (vendors, customers, distribution centres and transportation providers) and internal (production, material movement and storage).

m-commerce Mobile commerce – electronic commerce conducted between mobile applications.

master credit In back-to-back operations, the original export credit against which the second credit is issued.

MACCUG Member-Administered Closed User Group –a service administered by SWIFT whereby a corporate client can join the SWIFT network and send and receive SWIFT compliant files and messages. Companies can join SWIFT by registering in a closed user group set-up and managed by their financial institution (i.e. the financial institution elects which customers can participate). Within a MACUG, a corporate can communicate only with its bank, which decides which kinds of messages and files (payments, treasury, reporting, and securities) can be exchanged. If a corporate wishes to communicate with several banks it can register in multiple MACUGs.

MICR Magnetic ink character recognition – used in the machine reading of a special print in magnetic ink using a magnetic head. MICR is commonly used to read the bank information printed on the bottom of cheques.

milk run The combination of shipments from multiple vendors in close geographic proximity into one shipment received by the customer, normally done for a defined route on a recurring basis.

MIS Management information system. A system used to provide banking information to clients, enabling them to monitor their cash position.

MNC Multinational corporation.

mobile payments/m-payments Mobile payment is when payment for goods or services is processed using a mobile device such as a mobile phone or personal digital assistant (PDA).

money market The short-term (less than one year) liquid market for high-quality instruments. In free jurisdictions, instruments are available in domestic and euro-market form, so characteristics may be different.

multibank reporting/payments Electronic banking facility in which the proprietary electronic banking system of one bank is available for delivering or receiving messages to/from third-party banks.

multicurrency account An account that allows for the transfer of payments (including cheques drawn) in any readily convertible currency to and from designated account.

multilateral netting A system in which trade obligations among participating subsidiaries of a group are netted so that each participant pays or receives only the net amount of its inter-company sales and purchase.

multimodal shipment Shipment using more than one transportation mode (rail, truck, air, etc.) where the original shipment is containerised or otherwise kept together in its original condition.

negotiation The purchase by the nominated bank of drafts (drawn on a bank other than the nominated bank) and/or documents under a complying presentation, by advancing or agreeing to advance funds to the beneficiary on or before the banking day on which reimbursement is due to the nominated bank.

net present value (NPV) The value of a project's cash flows discounted at the weighted average cost of capital or an appropriate discount rate.

net worth The book value of a company's common stock, surplus and retained surplus.

netting A system that reduces the number of cross-border payments/foreign exchange transactions among units of a company either through the elimination or consolidation of individual funds flow. There are two types of netting: bilateral and multilateral.

nostro account A bank account conducted with a bank in another country in the currency of that country.

OECD Organisation for Economic Cooperation and Development.

OEM Original equipment manufacturer – where one company purchases a manufactured product from another company and resells the product as its own, usually as a part of a larger product it sells.

off balance sheet Financing that is not shown as a liability in a company's balance sheet.

offshore financial An environment permitting the establishment of financial operations services centre (e.g. treasuries, finance companies) where regulations are usually freer than normal and taxes on income are lower (e.g. IFSC, Ireland; BCC, Belgium; OBC Labuan, Malaysia).

open account trade credit When one business sells goods or services to another with payment to come later. The demand for payment is on an invoice that contains the details of the transaction, what is to be paid and when. The supplier runs an account of invoices issued and payments subsequently received on an open or rolling basis for their customer. All these accounts are collectively described as "receivables" or "trade debtors".

option An option provides the holder with the right, but not the obligation, to buy or sell an underlying bond, equity, currency, or commodity, or to receive a payment based on the movement of such underlying interest. The holder of the option pays a premium for this right.

overdraft A negative balance on a current account. Certain countries do not allow overdrafts (e.g. US). Others distinguish between casual overdrafts (penal pricing) and arranged/advised overdrafts (planned pricing).

overlay An additional layer of bank accounts between operating company local accounts and group treasury established with a global cash management bank to facilitate central cash management for a group of companies. There are a number of different ways to structure overlay accounts.

packing credit A loan given to the beneficiary by the bank to enable them to purchase raw materials. The beneficiary is usually requested to deposit the letter of credit with the bank as security.

payables financing A bank financing of the buyer's payables to its suppliers. Buyer normally introduces its select suppliers to the bank with the cost of financing, based on the buyer's credit rating.

per mille charge Transaction charge by banks to their most credit-worthy customers. A benchmark rate for lending.

PKI Public key infrastructure – PKI enables the users of public networks such as the Internet to communicate with each other in a secure manner.

PO Purchase order – written authorisation for a supplier to ship products at a specified price, which becomes a legally binding contract once the supplier accepts it.

pooling An international service offered by a bank to enable the notional offsetting of multiple balances for the purposes of calculating interest on the net balance.

portals In a B2B context, portals may be commonly described as electronic meeting places, or exchanges, for companies to transact business, access information, and interact with the various participants in the community. Portals may be generalist in nature, or they may exist to fulfil a particular set of needs. Horizontal portals typically serve the functional needs of a broader community, whereas vertical portals cater to the specialised needs of a particular industry.

promissory note A signed statement containing a written promise to pay a stated sum to specified person at a specified date or on demand.

PVP Payment versus payment. A standard method of simultaneous settlement in foreign exchange markets.

real time There is an increasing demand for real-time applications that reflect changes in an environment back to the user almost as they occur. This is especially important in treasury and cash management where users need to immediately know about changes, so that a financial position may be hedged or advanced.

reconciliation, automated Corporates are increasingly concerned about automating the reconciliation process, such that all outstanding transactions are reconciled in a straight-through processing (STP) manner and on an intra-day basis. As a result, discrepancies may be identified as early as possible for the sales force to follow up with clients, eventually leading to a faster application of cash. As a number of cash and treasury professionals are being measured by metrics such as Days Sales Outstanding, they are particularly keen to hasten cash application wherever possible.

red clause credit A letter of credit with a clause that authorises the advising bank to make an advance payment to the beneficiary.

reinvoicing centre A centre established as a focal point for inter-group and third-party currency sales. It acts as a principal by being invoiced in the seller's currency, and reinvoicing the buyer in its home currency, thus centralising foreign exchange management/exposure.

repo Repurchase agreement – an agreement whereby a borrower will sell a security to an investor with an agreement to buy the security back at an agreed date and price to provide the investor with a return. Reverse repo is the same transaction from the opposite viewpoint.

request for information (RFI) A document prepared by a company, addressed to one or more banks, to solicit details of cash management service capabilities. Often used as a means of pre-qualifying or pre-selecting banks to whom the formal RFP or ITT will be sent.

request for proposal (RFP) A document prepared by a company, usually detailed, addressed to one or more banks, to solicit a formal response for cash management services.

reserve requirement An obligation on a bank or other financial intermediary to maintain a specified proportion of total assets in liquid form. These can be designed to ensure solvency of banks or they can be used as a device for helping limit the creation of credit.

resident/non-resident In cash management terms, there is an important distinction in the status of the account holder, therefore the account. Governments often apply different rules to each.

revolving credit A letter of credit automatically reinstated after each drawing or upon receipt of authorisation from the issuing bank, with limits as to the duration of the facility and as to the (cumulative or non-cumulative) amount involved for each drawing.

RTGS Real-time gross settlement – a method of payment settlement that eliminates the threat of settlement risk (often known as Herstatt risk) between two parties and its knock-on effect to other banks by the provision of immediate good value on payments in and out (separately).

same-day value A value date equal to the date on which a transaction is initiated.

SCORE (The Standardised Corporate Environment) A model or service administered by SWIFT, whereby corporate clients can interact with financial institutions using standard SWIFT messages. The service is based on a closed user group.

secondary market A market in which existing securities are traded, as opposed to a primary market, in which securities are sold for the first time.

securities settlement system (SSS) A system which permits the holding and transfer of securities or other financial assets, either free of payment or against payment (delivery versus payment).

senior debt Debt that must be paid off before others in the case of bankruptcy.

SEPA Single Euro payments area

settlement assurance In an e-commerce environment, deals may be struck at a faster pace with increasing anonymity among buyers. This makes the certainty of payment an even more important issue. Banks that find ways to guarantee a larger portion of the payment and, at the same time, reduce the "payment up front" obligation of buyers will do well.

settlement date The date on which a security transaction is completed by actual exchange of securities for cash.

shipping guarantee Guarantees of this nature are required to enable customers to obtain goods before the arrival of the documents of title, and are issued to the shipping companies by the bank against an undertaking to forward the bills of lading when they are received.

smart card A microcomputer embedded within a conventional bank card used as a security device on controlling payments via electronic banking and clearing systems.

spot The exchange of one currency for another, at the agreed current rate of exchange of one currency, normally for payment and receipt of the funds in two working days.

spread The extra interest charge above the standard or risk-free rate to compensate for extra risk.

SSC Shared service centre – a single unit providing common services to a number of subsidiaries. This may be a domestic arrangement or an international/regional one. The SSC performs a broad range of finance activities, including domestic and cross-border payables and receivables. Treasury may also be incorporated into such a structure. (See in-house bank.)

standing order A written payment instruction passed to the bank by the payer. These instructions are for repetitive payments of the same value. Payments will only cease upon instruction from the payer to the bank.

STP Straight-through processing – a process (usually payments) that is completed electronically without any manual intervention.

subordinated debt Debt over which senior debt takes priority; in bankruptcy, subordinated debt-holders receive payment only after senior debt is paid off in full.

supply chain The network of retailers, distributors, transporters, storage facilities and suppliers that participate in the sale, delivery and production of a particular product.

supply chain management Coordinated set of techniques to plan and execute all steps in the global network used to acquire raw materials from vendors, transform them into finished goods and deliver both goods and services to customers.

supply chain optimisation Coordination of linked resources across all or part of a supply chain to eliminate or reduce manufacturing and logistics bottlenecks and to create optimised schedules based on shared inventory and order information.

swap An agreement between two businesses to exchange commodities, payments or other financial products to reduce the risk of volatile market conditions.

sweeping See cash concentration.

SWIFT Society for Worldwide Interbank Financial Telecommunication. A cooperative organisation created and owned by member banks to facilitate the transfer of information and payments/advice instructions between each other via a global data network. Standard formats are:

- MT103 – payment instruction (customer);
- MT202 – payment instruction (bank);
- MT210 – advice of funds/pre-advice (customer);
- MT940 – detailed bank statement information; and
- MT950 – summary bank statement information.

syndicated loan A loan made available by a group of banks in pre-defined proportions under the same credit facility in order to share the risk in a large transaction.

systemic risk The risk that a specific large counterparty (such as a country), a certain market or a settlement system should experience a crisis, and that there will be widespread spillover into the financial markets as a whole.

TARGET Trans European automated RTGS Express Transfer System – a payment system comprising a number of national real-time gross settlement (RTGS) systems and the European Central Bank payment mechanism (EPM). The national RTGS systems and the EPM are interconnected by common procedures to provide a mechanism for the processing of euro payments throughout the euro area and some non-euro area EU member states.

target balance A method of cash concentration where collection and disbursement sub-accounts are swept to/from a master (concentration) account leaving a target (residual) balance at the sub-account level and an aggregated balance at the master account – also known as compensating or cap accounts.

tenor The period of time that must pass before a bill of exchange or promissory note becomes due for payment. The date must be determinable from the face of the bill or note.

terms Stipulates the conditions of the letter of credit, the method for the dispatch of the goods, the basis on which the payment amount is fixed (e.g. FOB, CIF), and the documents required under the credit.

Trade Services Utility (TSU) The SWIFT Trade Services Utility is a collaborative, centralised data matching and work flow engine providing for a commercial proposition for the corporate trade supply chain.

transaction exposure The income statement exposure to a change in foreign exchange rates between the time a transaction is booked and the time it is settled.

transferable credit Permits the beneficiary to transfer all or some of the rights and obligations under the credit to a second beneficiary or beneficiaries.

transferee A party (second beneficiary) to whom a transferable credit is transferred in whole or in part.

transferor A party (first beneficiary) at whose request a transferable credit is transferred to a second beneficiary in whole or in part.

treasury management system (TMS) A configuration of hardware and software linked to internal and external information sources that allows an organisation's treasury function to collect all the necessary financial information regarding the organisation in a uniform format. A TMS allows the automation of a variety of treasury tasks and greatly facilitates analysis, forecasting of treasury results, and risk management.

UCP – Uniform Customs and Practice rules The Uniform Customs and Practice for Documentary Credits is a set of rules on the issuance and use of letters of credit. The UCP is utilised by bankers and commercial parties in more than 175 countries and has been standardised by the International Chamber of Commerce (ICC) by publishing the UCP in 1933 and subsequently updating it throughout the years. The current version is UCP 600.

usance In contrast to a sight credit, a usance credit is one where the bill/draft is intended to be payable at a date later than that of the presentation of documents (see "tenor").

value date The value date on which the payer is debited and the payee is credited (although these may differ if there is a float). A compensation characteristic of international cash management.

VaR Value at Risk – an estimate of the maximum that a company can lose in a defined period under normal market conditions. It is generally based on correlation of currency rate, security price and commodity price movements.

VOIP Voice Over Internet Protocol. The use of the Internet for making telephone calls.

WAP Wireless application protocol – a technology that allows portable wireless devices to access the Internet and communicate with each other.

warrant Option to purchase or sell (normally the former) an underlying instrument at a given price and time.

withholding tax (WHT) Tax on payments that is deducted by the payer at source and paid directly to the relevant revenue authority. Typically on interest, dividend and royalty flows, tax is for the account of beneficiary. WHT rates vary country by country.

working capital A company's investment in short-term assets such as cash, inventories, marketable securities and accounts receivable.

WTO World Trade Organization.

zero-balance accounts (ZBA) A method of cash concentration whereby collection and disbursement sub-ZBA accounts are swept to or from a "header" or master account to leave a zero balance at the sub-account level and an aggregated balance on the master account.