THE ART OF CONVERSATION IN LIQUIDITY MANAGEMENT

Adopting a more holistic view when crafting liquidity strategies

By Sridhar Kanthadai

Designing a well-structured liquidity solution for multinationals and top domestic corporates is not just about putting it all to paper, or cobbling a few cash concentration techniques. On the contrary, it is a dynamic process where the liquidity solution provider engages the client in a conversation. The fact is that there is simply no right or wrong solution until the specific situation facing the client has been discussed.

Liquidity management involves having the right amount of cash – at the right place, at the right time, in the right currency. It is, therefore, not just about implementing netting or pooling techniques that are, after all, just techniques or tools utilized to achieve several liquidity management goals. More than anything, it is about knowing what is appropriate for a company, and making sure that the model pursued is in line with its strategy and culture.

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Management buy-in

Of critical importance is how integration is achieved between different legal entities. The first key issue a treasurer must consider when instituting liquidity solutions across an organization is the need to obtain management buy-in from all levels within. This is an absolute must. The support of the most affected entities or departments will simply ensure smoother implementation and a better rate of success.

The consultation must then start quite early within the organization itself. In treasury, for example, there are people involved only in hedging risks, while some are focused solely on payments, collections and other types of transactional activities. Each has their own view on how visibility of accounts and process testing can be improved. It is also important to bring the CFO into the conversation. His or her view is essential given the broad and strategic role this position often plays in managing liquidity.

Only when the treasurer has participated in these various aspects of the conversation can a better perspective be gained of the workings of the organization.

Holistic view

As it is, the treasurer looks at various options when it comes to ensuring sufficient working capital. He or she can choose to borrow from the organization's bank, or tap the capital markets. If the company is enjoying excess liquidity, the treasurer has to identify opportunities where that cash can be made to work for the advantage of the shareholders.

But first the treasurer needs to have a clear understanding of what the company already has, what it needs and the timeframe required to satisfy that need. Essentially, it is about taking a holistic view, which is exactly how Citigroup approaches each situation – beginning with strategic conversations with treasurers to craft the most appropriate liquidity management solution.

It is also the reason why, as the premier cash management institution, Citigroup values its in-house consulting service, which is made up of professionals who can structure solutions. What Citigroup has specifically is a model that brings in knowledgeable product experts. The company's relationship managers are well trained and can identify opportunities in the capital market, in investment and in the working capital space.

What's more, Citigroup shapes its conversation with a corporate client based on the key concerns that preoccupy the latter. With the impact of the Sarbanes Oxley Act, for example, the focus has been on compliance and corporate

Many countries have regulatory restrictions on the type of structures in which companies can participate. Factors to consider when structuring liquidity management solutions include:

- Resident and non-resident accounts
- Inter-company lending regulations
- Commingling of funds
- Debit and credit interest
- Overdraft policies
- Special regulatory reporting
- Economic benefits

governance practices. The regulation has prompted treasury organizations to work harder in ensuring a high level of compliance and greater visibility in accounts.

Only when compliance issues have been addressed and tools such as ERP systems are in place can the treasurer then focus on external developments that directly impact liquidity.

Given the rising interest rates and volatile foreign exchange, the treasurer needs to look at all things in the balance and arrive at a holistic strategy on how to address their impact on the company's cash flow, looking at the same time at the opportunity costs. While the goal of minimizing the level of idle cash in accounts is important, it is also critical to look into how this is achieved and to determine whether it is being done in a cost-efficient and truly automated way. Be aware, however, FX and swap costs can either enhance or wipe out gains of cash concentration.

Compliance concerns

In Asia, considerable challenges remain when it comes to structuring a comprehensive regional liquidity solution. In some jurisdictions, the size of inter-company loans and how they are priced are still heavily regulated. The commingling of funds from non-residents' resident accounts is not allowed in some cases, and there are regulations about overdrafts and currency convertibility. Ultimately, liquidity management is bound by varying compliance and regulatory issues and the challenge becomes understanding those issues fully to avoid unnecessary risk.

At the same time, restrictions imposed on how cash is moved continue to come down. For instance, Malaysia and China have both recently made a number of changes. In addition, two markets that come up often in conversations with clients are Korea and India. These are two of the more highly regulated markets, but where regulators are starting to move in line with some of the less regulated markets in the region. In Korea, the government has strict controls on FX documentation. While inter-company movement of funds is allowed, there are tax regulations that could make such transfers unattractive. The tax issues have certainly made it difficult for Korea to participate in cash concentration initiatives.

Treasury organizations are better off implementing liquidity solution in stages, starting first with the less regulated jurisdictions and then moving toward the more regulated ones.

Corporates can pursue various cash optimization strategies in-country – either at the most basic single entity, single currency level or through the more complex single/multi-entity, multi-currency type of arrangement. There are different models that can be aligned on top of one another to provide an infrastructure that is efficient.

Summary

The key to implementing these different solutions is the quality of infrastructure of the key liquidity solution provider. In terms of Citigroup, the bank has a consistent infrastructure that offers the ability to integrate regional treasuries from around the world, and this serves as a key driver for implementing a solution.

At the moment, many corporates are trying to move their liquidity structures into a regional treasury structure, complementing the existing structures of shared service centers. Citigroup's ability to achieve a regional interface and provide a regional solution is what drives customers to the company's solutions.

For more information, please contact your relationship manager.

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