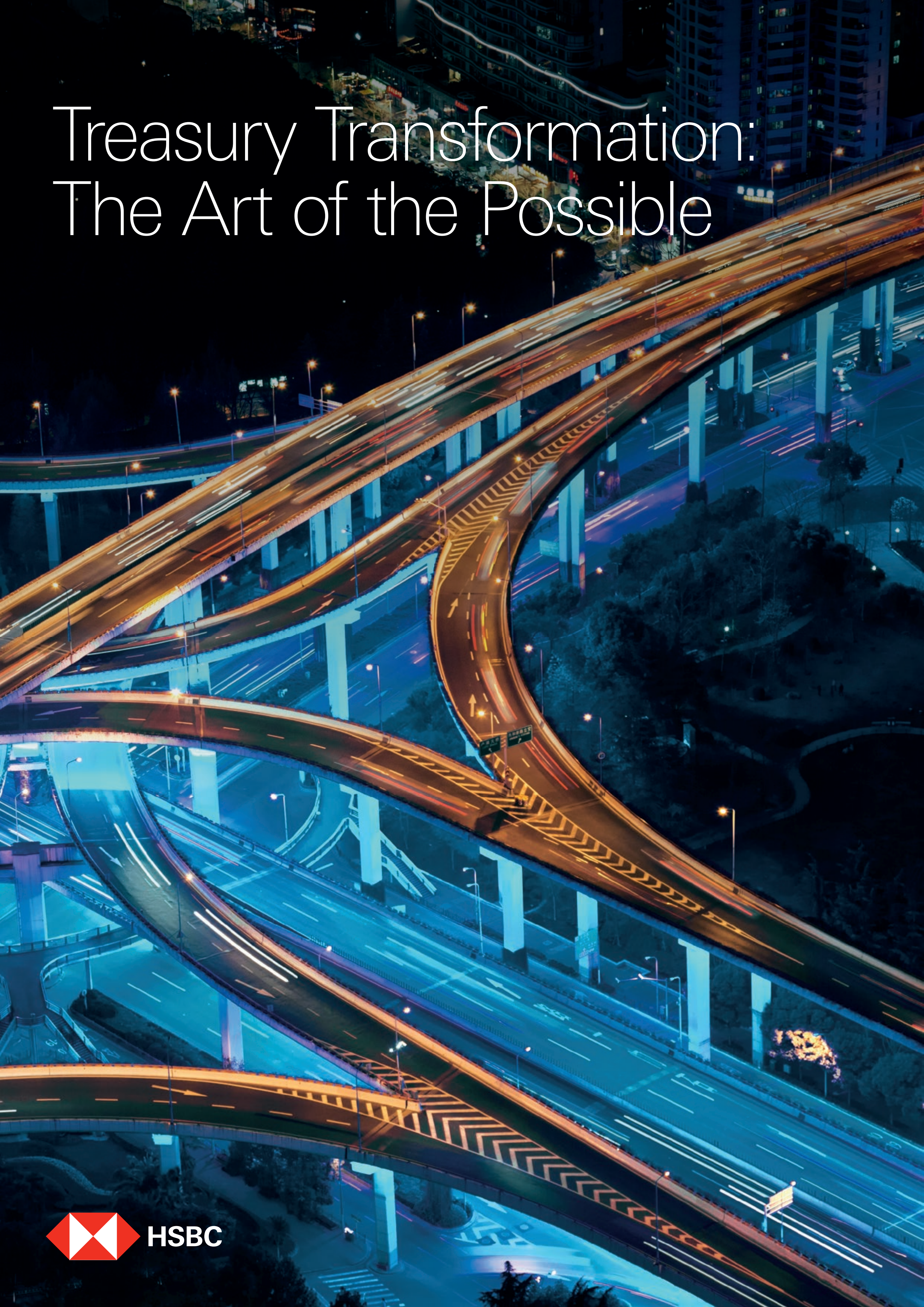
Treasury Transformation: The Art of the Possible



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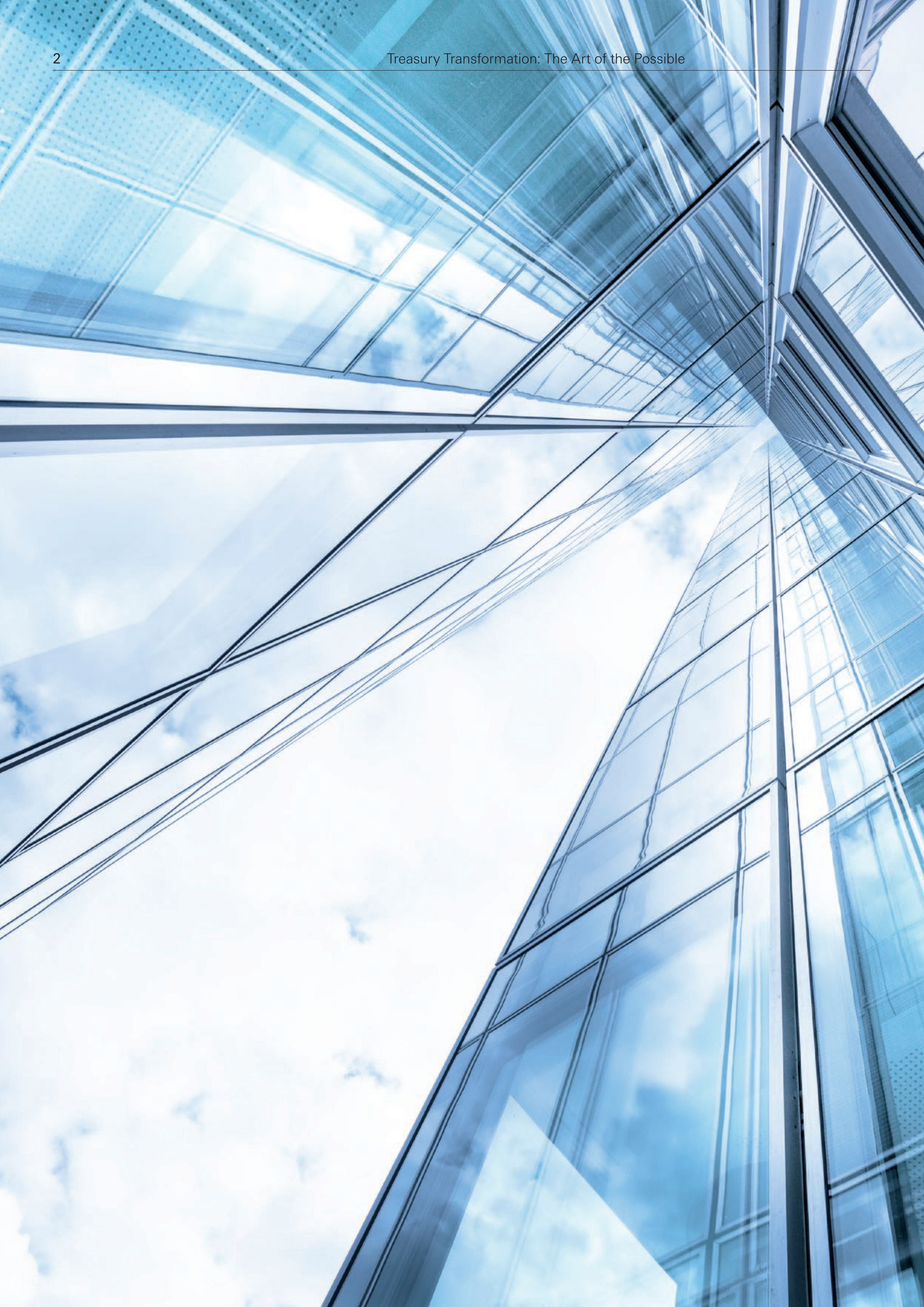


Treasury Transformation: The Art of the Possible

Joanne Towers,
Head of Payments, Product, Europe

Treasury transformation continues to feature as one of treasurers' primary objectives as they focus on efficiencies in their processes and the combatting of fraud and cyber-crime, whilst establishing account structures that will reduce cost and bank fees. In an increasingly globalised world, there is also an increased desire to manage cash regionally and globally as opposed to maintaining accounts locally. The digital economy and open banking are offering new opportunities and real time treasury is starting to emerge as the next natural step in optimising treasury organisations.

Global industry initiatives such as ISO 20022 standards in payments and the International Payments Framework Association, as well as a number of other country-specific and regional schemes, are also encouraging movement toward more consistent and efficient electronic processes. Transnational payment schemes such as SEPA alongside the development of new innovative solutions that allow companies to do more from fewer funding accounts are further driving these changes.

In this article, we will take a closer look at what companies could achieve by centralising their treasury processes, as well as the tools and solutions that companies have at their disposal.

Centralised Treasury Structures

The right treasury structure begins with efficient payments processing and will depend on the individual business' unique size and scale, geographic footprint, organisational culture, technological sophistication and more. As a result, companies may choose from a number of specialised structures, designed to help meet specific objectives and varying degrees of efficiencies in payments processing. The table below illustrates a range of structures being used today.

Treasury Centres	An internal functional construct that handles treasury and finance activities, particularly payments related to managing the company's liquidity position. In addition to centralising payments, treasury centres are also used to manage foreign exchange, financing and investments. These structures can be fully centralised, or operate on a hybrid basis whereby policies are consistent but tasks are managed by local entities.
Shared Service Centres	An internal functional construct, separate legal entity or third party provider that undertakes various activities on behalf of the group, which can include the processing of general payments, e.g. vendor payments, employee-related payments and, in some cases, taxes and other statutory payments. Since Shared Service Centres (SSCs) generally support a number of operating business units with standardised processes and controls, their key purpose is to drive back office efficiency and cost savings through economies of scale. An SSC can move beyond payments processing to manage e-Invoicing, foreign exchange, account reconciliation, trade finance, human resources and more.
In-House Banks	A separate legal entity that provides financial services to affiliates within the organisation, including credit and investment facilities, netting services and foreign exchange, among other treasury and finance activities.
Payment Factories	An internal functional construct, separate legal entity, or a third party provider that processes and executes payments and acts as the single gateway from the organisation to its banks and payment service providers. Many large global companies today are opting to establish in-house banks and payment factories. In this case, all payments flowing through the payment factory are grouped together before being sent to the company's financial institution to lower overall administrative and banking costs. In addition, the need for physical cash transfers is reduced with the availability of inter-company netting and working capital is improved since company funds are consolidated to make liquidity and foreign exchange management more efficient. Under this structure, Payments-On-Behalf-Of (POBO) or Payments-In-The-Name-Of (PINO) are arranged with the participating operating units.

On Behalf Of ("OBO") and In The Name Of ("INO") Transactions

As companies can do more from fewer accounts, this can include making and receiving payments on a given funding account on behalf of other group entities. If the company has adopted a "Payments-On-Behalf-Of" (POBO) model, the payment factory uses its own accounts to effect payment and subsequently sends a debit entry to the respective operating unit's internal account with the in-house bank. The payment factory is considered an authorised agent of the participating business units and, as such, may charge a management fee for services provided. The arrangement between a payment factory and its participating entities is typically documented through a formal contract or agreement

In the case of "INO" transactions, a treasury may be authorised to instruct payments from the accounts of other group entities. This option may be chosen where OBO transactions are not possible, potentially for regulatory reasons in certain jurisdictions.

Regional Variations

Treasury transformation is a topic relevant across all regions. There are however particularities to each region. For instance, in Europe, the standardisation of payments and collections seen under SEPA could enable companies based or doing business in Europe to capitalise on the investments made in technology and systems to standardise message formats, processes and connectivity. With the basic infrastructure in place, these corporates may take the next step toward a fully centralised global treasury to increase efficiency and lower costs further.

In Asia a treasurer should consider the distinction between open, transitional and closed economies and the implications of these as to where a regional or global treasury may be located.

In North America, companies have introduced various levels of centralisation through tools like centralisation of liquidity (such as cash concentration and zero balancing) and setting up shared service centres. As companies grow, there is a need to become more efficient.

It is important to understand where the company is along the payment centralisation journey so that effective and appropriate solutions can be introduced.

Emergence of New Tools

We find ourselves in a time of high innovation in the payments space which we believe companies can leverage to centralise their treasury operations more effectively. These tools can afford treasuries a more real time and dynamic model.

Virtual Accounts – the next step to treasury transformation on treasurers' agendas

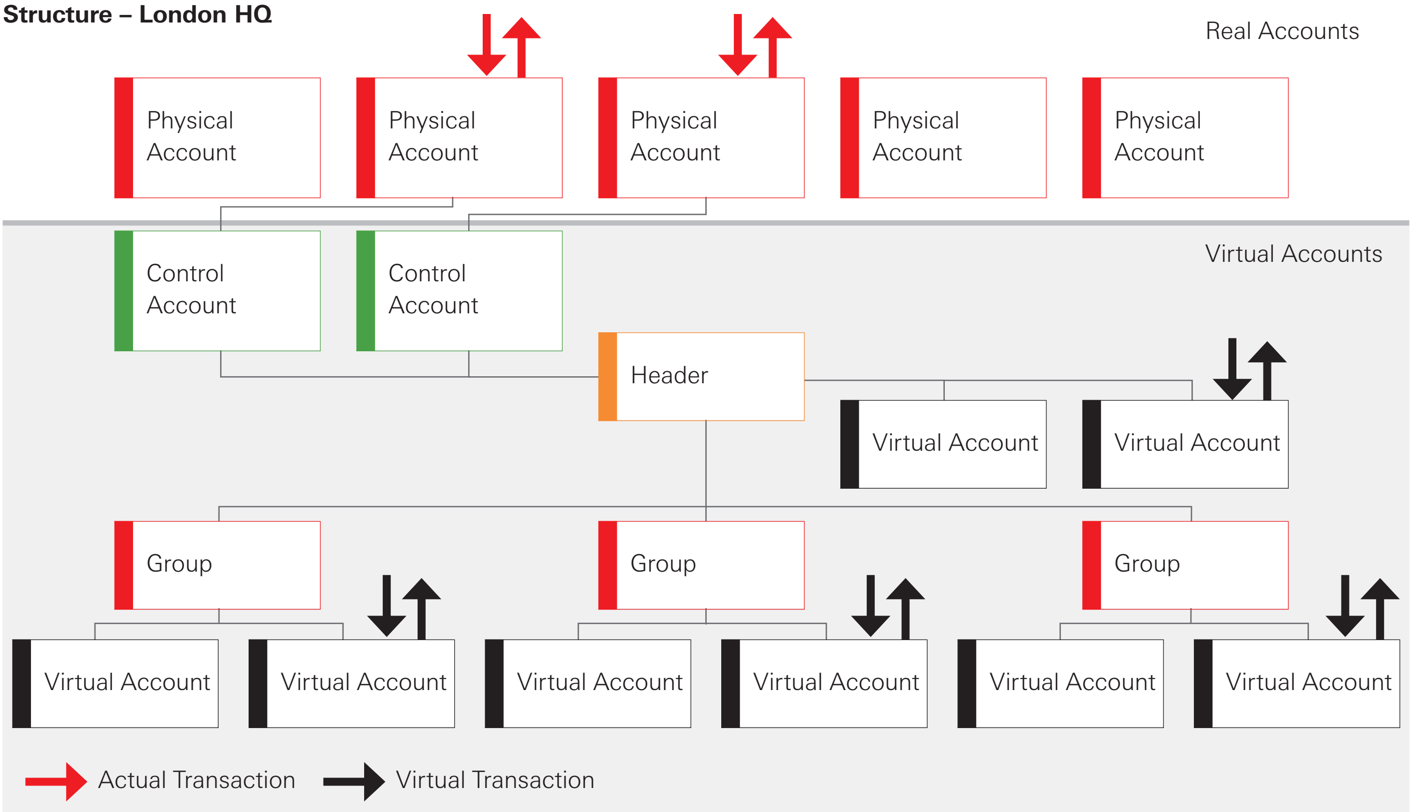
Virtual accounts are not new and historically have been used by corporates to identify payers to facilitate reconciliation of receivables. Over the past two years, however, the use of these has emerged as a natural next step in treasury transformation for both payments and receivables.

Many believe virtual account structures will be a convenient solution to address some of the pressures currently in the market by serving, for instance, as an alternative solution to notional pooling, as well as facilitating a variety of POBO and ROBO (Receivables On Behalf Of) structures.

HSBC is working on enhancing its virtual account proposition, beginning with the UK with additional countries due to be rolled out over the course of 2019. This Next Generation Virtual Account (ngVA) solution will cover a much wider scope, providing organisations with a cost effective means of centralising accounts payable and accounts receivable. The ngVA structure will become increasingly important as a way to view and mobilise liquidity, building on the traditional advantages of virtual accounts with an additional self-service element. Under the virtual account structure, liquidity is automatically concentrated in real time into the physical account that acts as the header for the virtual structure. This replaces the traditional notional pooling structure and adds greater flexibility with improved transparency, visibility and forecast accuracy.

For further information on HSBC's virtual account solution please contact your Relationship Manager.

Example of a Virtual Account Structure – London HQ



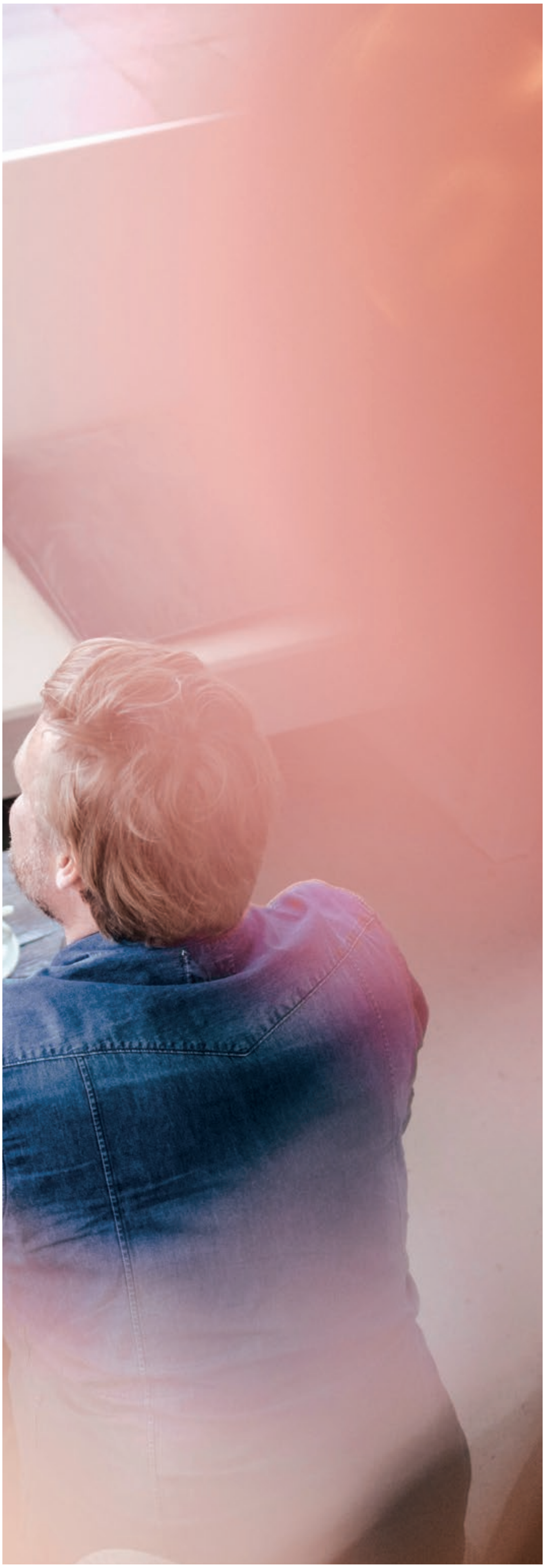
Global Disbursements – efficiently managing FX exposure on cross-border flows
Efficient management of FX risk can be a concern for treasurers. Some transactional flows fall below the radar like micro payments that can be disbursed from their different corporate entities with a variety of margins and FX fees.

HSBC has defined a solution, Global Disbursements, which allows for cross-border payments to be made from a single account in a single file. Payments can also be made from multiple accounts in different currencies or countries, in various payment types and to a range of destinations. Alongside payments to beneficiaries' bank accounts, Global Disbursement customers can also pay funds directly to beneficiaries' PayPal wallets globally.

This flexibility can help companies to rationalise their account structure by enabling them to do more with fewer accounts. This solution simplifies FX flows and management by reducing processing and preparation time for international payments. It provides accessibility to more than 60 payment schemes, optimises FX rates and margins and automates reconciliation with detailed reports.

Real Time Payments – boosting liquidity management
Technology is allowing us to complete everyday activities ever more quickly and payments are no exception. In today's fast-paced digital environment, real time payments infrastructures allowing for 24/7 settlement will change liquidity dynamics profoundly.

As cash conversion cycles accelerate, delay in payment execution is reduced, as is the level of contingency cash buffer required to be held on bank accounts. Pressure on cash flow planning and forecasting may also be reduced as working capital management becomes more efficient with liquidity working harder for the business.



Considerations before embarking on a centralisation journey

Still today many companies remain at the very beginning of their treasury centralisation journeys, maintaining decentralised models. Treasury centralisation is not an all-or-nothing process, but rather can be implemented progressively over time. A tailored and structured approach is needed to achieve a fit-for-purpose account and liquidity structure. Which responsibilities are centralised and to what extent can range from a pure function (for instance, accounts or receivables management) to an end-to-end supplier/client relationship. What is appropriate for any given corporate will depend on many factors including the type of clients and suppliers as well as geographic spread of activities.

When setting up a centralised treasury structure, there are many factors to take into consideration, such as, but not limited to, the following:

- Where the structure will reside geographically from a tax, regulatory, compliance, legal and time zone perspective,
- Who is needed to manage the centre and what pool of skilled resources in the chosen market is available,
- How easily business contingency and disaster recovery plans can be developed and implemented,
- What infrastructure (technology and processes) and organisational costs are related to making the move, and the associated return-on-investment

Throughout this journey, resources, budget and careful planning are pre-requisites within the corporate organisation.

A transverse project team with executive sponsorship is essential to the success of any treasury transformation project. HSBC can share its market and cash management experience and provide solutions to support you in this journey.