

EMERGING OUT OF LATIN AMERICA



IN RECENT YEARS, BRAZIL AND MEXICO'S BANKING SYSTEMS HAVE CHANGED DRAMATICALLY. **NICK JONES** (PICTURED) AND **FERNANDO VICARIO** OF FLEETBOSTON (BANKBOSTON IN LATIN AMERICA) DISCOVER WHAT IT MEANS FOR CASH MANAGERS.

This article provides a summary of some of the key characteristics and changes in the cash management systems of two of the leading emerging markets in Latin and Central America, namely Brazil and Mexico, together with the regional trends that are making corporate treasurers reappraise the entire region's cash management arrangements.

CASH MANAGEMENT IN BRAZIL

Since the launch of the Real Plan in late 1993, the Brazilian financial system has been undergoing substantial structural change. With the decline in inflation, the opportunity for the generation of automatic profits has disappeared. As a result, banks and other financial institutions have been forced to trim costs and step up product innovation, with a particular focus on cash management services.

At the same time, the government has broadened the scope of its privatisation programme to include the state banking sector – an unusual, if not unique, feature of the Brazilian financial system. With the restructuring of this system entering its second decade, the moment seems opportune to take stock of these developments and assess their longer-term implications.

- The Banco Central do Brazil (BACEN) regulates all financial institutions in the country.
- Significant central bank reporting requirements govern cross-border transactions and the regulatory environment continues to be complicated and dynamic.
- Brazil has an impressive and efficient highly automated financial system driven, at least in part, by the need for rapid payment clearing and settlement in a high inflation environment before the Real Plan in 1993.
- The principal payment instruments used in Brazil are cash, *cobranças* and *documentos de creditor* (credit order documents (DOCs) – which are similar to automated clearing house items. Barcode remittance documents are used as instruments for payments and collection. They are handled much like European GIRO payments.

There are three main instruments that relate to cash and treasury management:

- DOCs are used mainly for making interbank payments and intracompany and third-party payments within the same financial institution. They are processed electronically, in batches, and settled through the clearing house on the next business day.

- Cheques are still the most widely used non-cash payment instrument in Brazil. They also settle through BACEN, the national clearing house. Cheques presented to the same *praças* (regional clearing house) are cleared in 48 hours if the value of the cheque is equal to or lower than R\$299 and in 24 hours if the value of the check is over R\$299.
- *Bloquetos de cobrança* consist of a *bloquete*, a two-part document that serves as the buyer's payment receipt, and an interbank clearing document.

The *bloquete* is issued by the seller to the buyer or consumer and contains invoice information, payment amount and due date. Users may take it to any bank in Brazil and pay the face value of the *bloquete* along with any fees assessed to the bank. The interbank settlement portion of the *bloquete*, which uses bar code technology, is automatically scanned at the bank of first deposit.

All licenced banks maintain a single reserve account with the central bank that will have the control of a system called the Information System from Central Bank (SISBACEN).

Brazil's foreign exchange (FX) system is still highly regulated and restricted by the central bank. It operates using a dual exchange rate structure with official (commercial) and tourist (floating) rates. FX must take place through an authorised financial institution. In late 1999, Brazil reported that its FX plans include both the free convertibility of its currency and elimination of controls on capital outflows as the next steps to fine-tuning the free-float currency adopted at the beginning of the year.

Many common treasury management techniques used in Europe and the US are not permitted in Brazil, including leading/lagging and re-invoicing. Multilateral netting and participation in cash pooling are also prohibited. Brazil imposes a transaction tax on debits to current accounts known as *contribuição provisória sobre movimentação financeira* (CPMF). This is 0.38% of the value of the debit where the credit is to an account with a different tax identification number.

Zero balance account (ZBA) structures (where funds physically move from sub-accounts to a parent account) are permitted in Brazil, as are overnight investments, although high bank reserve requirements may make short-term investments more cost-effective than overnight.

Resident or non-residents may hold accounts in Brazil only held in Brazilian Reals. Liquid mutual funds, which pay daily or monthly interest, are an option for earning interest on surplus funds. Effective forecasting of receivables and payables can also permit a structure

of improvements and some banks are prepared to provide such a structure.

In April 2002, a new payment system was launched in Brazil, involving more than 180 financial institutions across the country, and with the capability to clear and settle financial payments in real time. This new Brazilian payment system has some positive aspects, including the following:

- automatic processes that imply reduced processing time;
- online real-time payments, reducing credit risk; and
- reduction of systemic risk.

Despite these positive aspects, some changes are necessary in the Brazilian payment system, especially in regard to security matters. As things stand, the central bank assumes the counterparty risk of other market members, creating an expectation that there were no settlement exposures.

CASH MANAGEMENT IN MEXICO

Mexico's institutional and regulatory payment system and monetary frameworks have significantly evolved over the last decade. The banking system has gone from a privatisation, to a rescue package, to a re-privatisation. The most visible effects of this transition are a highly concentrated banking marketplace and the prevalence of foreign-owned institutions.

During this period, Banco de México, the central bank (known as Banxico) became constitutionally autonomous from the executive branch of power with the essential purpose of controlling the inflation rate.

In fact, interest rates and FX exchange rates, along with almost every other relevant price in the economy, are set by the market. Not only have deregulation and diminished government intervention been the predominating tendencies, but significant changes to Mexico's system of payments have taken and are still taking place.

For many years now, companies have had the freedom to move funds to and from different cheque accounts, from one company to another, and from the Mexican peso to the US dollar, without any adverse fiscal or administrative consequences (unlike some other countries in the region). The absence of government-imposed distortions to the payments system has fostered the overall system's efficiency and therefore national and multinational corporations' treasuries' ability to streamline their collection and payment processes, locally and globally.

In 1995, Banxico implemented *Sistema de Pagos Electrónicos de Uso Ampliado* (SPEUA) as part of the payment systems reform. Through SPEUA, all banks within the Mexican banking system execute their client payment instructions in real-time, for same day value and for amounts of at least 50,000 peso to beneficiaries' accounts in other banks. SPEUAs are typically sent to the banks for execution through their respective electronic banking platforms. Since Banxico acts as the clearing agent for these types of payments by directly and automatically affecting each of the system's banks' single account with Banxico, companies benefit from a high degree of efficiency, both in execution and cost terms.

This system has greatly contributed, among other factors, to the increasing levels of stability in the Mexican financial system. One of the relative weaknesses of this system, though, is that, although the transactions flow seamlessly and rapidly into and out from Banxico's SPEUA system, those receiving banks – which process



'ACCOUNTS IN DOLLARS HAVE ABSOLUTELY NO RESTRICTION AND/OR TAX, REGARDING THE MOVEMENT OF FUNDS IN AND OUT OF MEXICO'

most of the payments within the country – may take more time to process the deposits into the beneficiaries' accounts internally.

Another electronic means to transfer funds is the electronic funds transfer, or *transferencia electrónica de fondos* (TEF), which are processed by banks through a system that runs in the Mexican cheque-clearing house Centro de Cómputo Bancario (CECOBAN). One advantage of this method of payment is that there is no minimum amount to be transferred, as with the SPEUA. However, it has the disadvantage that the paying party has to send the funds via the paying bank to CECOBAN on t-1, but the ensuing floating is earned by neither the paying client nor the paying or receiving banks. TEFs payments are typically cheaper than SPEUAs, but, again, banks may charge for it differently.

Several banks have the capability to process SPEUAs and TEF payments automatically online, and a few of these actually do so online and in real-time, without any delay. The fees to carry out SPEUAs and TEF payments vary widely among banks, depending on each bank's market strategy or specific circumstances with each client. The amount of information flowing to the ordering client regarding its payments instructions will depend on each bank's systems capabilities, as both SPEUA and CECOBAN provide electronic confirmation data on the status of the payments.

'CLABE' STANDARDISED BANKING CODE. In April 2003, a new improvement was implemented to standardise the checking account numbers among all the banks in the system. All accounts now have 18 digits, which permits the receiving banks of a funds transfer (whether through SPEUA or TEF) to run an algorithm to verify that the number is right. In this manner, errors are further reduced and payments flow more effectively. This new account code is called *Clave Bancaria Estandarizada* (CLABE) standardised banking code. It is expected that, before the end of 2003, it will be mandatory that all account numbers be eliminated and any payment instruction will have to be made using the new CLABE. With the CLABE, deposits to any account in any bank in the country can be made by just by entering the CLABE of the beneficiary. Moreover, periodic payment instructions – such as telephone or utilities bills – can be domiciled at any one bank, so that the charging party has authority to collect payment using the beneficiary's CLABE of the client.

Regarding collections, these can be received at any branch of any bank throughout the country and credited to the beneficiary's account the same day (for cash or same bank cheque deposits) or the next day (if the cheque requires clearing). There are no special prerequisites for banks to participate, as all banks are linked to the same centralised payment and clearing systems across the country. Again, fees vary from bank to bank, and from client to client.

Most liquidity management tools are available in Mexico, with the exception of netting (bilateral or multilateral) and notional (virtual) sweeping. In any event, some banks may put together synthetic structures that may achieve many of the objectives of netting. For concentration purposes or interest-bearing cheque accounts, bank accounts for businesses (not for individuals) may be established in either pesos or US dollars (only in pesos for individuals). Accounts in dollars have absolutely no restriction and/or tax, regarding the movement of funds in and out of the country.

The latest enhancement to Mexican system of payments consists in upgrading the current SPEUA system to comply with BIS standards and best practices abroad. This will entail migrating to a new, much more flexible and secure system, called *sistema de pagos electrónico interbancario* (SPEI) interbank electronic payments system. For an initial period this will run parallel with SPEUA.

SPEI will run in Banxico too, and will allow companies to make and receive electronic payments of any amount (not restricted to those above 50,000 peso, as in SPEUA) for same-day value throughout Mexico in a much more efficient and less expensive manner. The market could gradually tend to abandon TEF, with some exceptions – probably payroll – and use SPEI. This system will benefit from all the recent improvements such as CLABE. This SPEI phase is expected to be implemented by 2004.

Considering all the structural changes the payments system has undergone in recent years, companies operating in Mexico will not only find an investment grade country to do business, but, importantly, a world-class environment to process their monetary transactions. Many banks are well positioned to take advantage of these improvements and translate them into concrete cash and information processing benefits for multinational companies in Mexico.

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Regional Cash Management Trends

It is not just on a country-by-country basis that European Multinationals are taking advantage of recent changes in the countries' clearing systems to improve the efficiency of their 'local' cash management arrangements. Increasingly, treasurers are being asked to participate in a wider corporate remit, alongside other corporate functions such as HR, Procurement and IT to view the countries in Latin America as 'one region' and identify cost savings and risk reduction opportunities in treasury processes.

During the 1990s, Latin America was seen by many European treasurers as something to tackle on a regionalised basis only after cash management had been centralised in their more familiar regional 'backyard' of Europe and the more homogenous regions such as the United States. Even then, the region was afforded less importance.

Sales in Latin America typically accounted for 10% of a multinationals global turnover and were characterised by differing regulations, taxes, customs, restrictive time zone differences and limited innovation in regional technology. These obstacles created de-centralised treasury organisations, further inhibiting a re-evaluation of treasury across this region.

This picture has changed considerably in the past couple of years. Group corporate projects to determine cost savings have

driven change. Recent advances in technology including the emergence of enterprise resource planning and treasury management systems coupled with more regionally-customised, browser-based banking platforms are now more able to quantify and thus create the business case for change.

A systematic approach is usually adopted by the European treasury function to work hand in hand with key treasury personnel in the region or the US to improve country cash management practices whilst accommodating regional technology platforms that can work in harmony and 'link' each countries treasury processes. Countries with clearing systems as diverse as even Mexico and Brazil, as featured in this article, are now being regionalised for the benefit of everyone at the multinational concern.