Many currencies one cash pool

Managing the working capital and liquidity of the business has always been important, but knowing where your cash is and when it is due to be received have become crucial issues in the current financial conditions. And not only does a corporate need to know where its cash is, it also has to manage it to meet its ongoing obligations, ensuring it can be accessed for the benefit of the business in the right place, at the right time and in the right currency.

For any business with operations overseas, it is imperative that local cash positions, both surplus and deficit, are managed by treasury for the benefit of the group. To do this efficiently and effectively, corporates need a banking partner that understands the working capital flows of the business and can provide liquidity management solutions to meet the ongoing needs of the company, including short-term working capital facilities.

IMPORTANCE OF TREASURY In recent years, treasury has become much more of a partner to the whole business. Most day-to-day treasury tasks, such as reconciliation and payments, have been automated, freeing up time for treasury to add real business value.

The vast majority of corporates have an established treasury policy that sets out how cash is to be managed and how the company interacts with its bankers and other financial providers, at the parent and the subsidiary level, both in its home market and overseas. And with cash management's profile rising, right up to board level, within the business, treasury is gaining corporate clout and having ever greater influence on day-to-day business operations.

FOR ANY BUSINESS WITH OPERATIONS OVERSEAS, IT IS IMPERATIVE THAT LOCAL CASH POSITIONS, BOTH SURPLUS AND DEFICIT, ARE MANAGED BY TREASURY FOR THE BENEFIT OF THE GROUP.

Executive summary

- Some banks offer automated services that allow companies to concentrate cash at the centre and include it in a cross-currency pool without the need for a physical swap to be made between one currency and another.

Where treasury can add real value is by advising any part of the business which has an effect on the cash position of the company, including the sales team and procurement. For example, if the sales team are giving additional discounts or lengthening the terms of trade to achieve sales, this could adversely affect the amount of cash the business has to meet its obligations.

EFFECTIVE LIQUIDITY MANAGEMENT There have been few changes to the core elements of liquidity management over the years. It is still about making and reconciling payments and receipts in a timely manner, and managing cash surpluses and shortfalls effectively while minimising interest costs and maximising interest received.

Transaction management processes are now well established, with companies having moved to, or moving towards, making and receiving payments electronically, with links between accounts payable and accounts receivable systems for automatic reconciliation. Indeed, according to figures from APACS, the number of paper-based transactions in the UK has halved over the past 10 years and is expected to reduce by a further 50% by 2017.

Managing day-to-day cash positions on all the company's bank accounts is paramount. Where numerous accounts are held in one currency, cash pooling solutions can be offered by a bank to aggregate the overall position in a single currency.

Cash pooling is available in many countries and many corporates

CORPORATES ARE CHANGING THE WAY THEY MANAGE THEIR FINANCIAL FLOWS TO ENSURE THEY HAVE ENOUGH WORKING CAPITAL TO MEET THE ONGOING REQUIREMENTS OF THE BUSINESS. **VIVEK RAMACHANDRAN** EXPLAINS THE BENEFITS OF CROSS-CURRENCY CASH POOLING.

will pool accounts in one country or currency zone. But this can result in a surplus balance in one currency and a deficit in another.

For accounts based overseas, companies can get end-of-day balances and transaction reports via a bank's internet banking portal or SWIFT. What is becoming more important is the ability to obtain intraday information and use it to manage liquidity positions across the group during the same day.

CASH POOLING SOLUTIONS Many corporates use cash pooling solutions to maximise internal liquidity before tapping external sources of liquidity. Before establishing any structure, they will have needed to consider a myriad of internal issues to ensure legal, tax and regulatory compliance with such things as transfer pricing regulations and intercompany loan positions.

The location of a cash pool is of paramount importance. For example, does the local tax and regulatory regime allow effective cash pooling, either single-currency or multi-currency? And are sufficiently knowledgeable staff available locally to manage the cash pool on the group's behalf? Withholding tax is another important consideration: is interest charged or allowed on a gross basis on both external or internal group interest, or does tax have to be deducted at source?

With all of these considerations, the ability of a bank to tailor solutions is vital to create the right pooling structure to meet the needs of the business. Cash pooling has two principal forms:

- cash concentration, where funds are centralised in the name of the treasury or finance function account; and
- notional pooling, where surplus and deficit positions are set off against each other for interest purposes (either full interest set-off or, in locations where full set-off is not available due to the regulatory regime in the country or the bank, interest margin enhancement structures).

WITH LIQUIDITY MANAGEMENT SET TO MAINTAIN ITS HIGH PROFILE, THE TIME IS NOW RIGHT FOR CORPORATES TO REVIEW THEIR CURRENT PROCEDURES AND DISCUSS THE SOLUTIONS AVAILABLE WITH THEIR BANK.

Some banks have recognised that management of cross-currency cash positions is the obvious step forward and have developed automated services that enable cash to be concentrated at the centre and included in a cross-currency pool without the need for a physical swap of one currency for another. Such services provide treasury with greater effectiveness in managing balances across the globe, although they are still subject to central bank or exchange control regulations in the particular country of operation.

The global marketplace creates its own problems. Is the business operating in the same time zone? What are the local value dating practices? How accurate is the local cashflow forecasting? And how does the local bank process the day's transactions? For these reasons it is difficult, if not impossible, to manage accounts based outside the home market with a zero balance.

However, with a thorough understanding of historic and forecast cash positions on primary bank accounts, it is possible to establish parameters by which the overseas accounts are managed. For example, an overseas subsidiary's bank account can be managed through a target or threshold balance to ensure sufficient liquidity to meet local obligations. An added benefit is that local short-term working capital facilities could be reduced as the overall position is being managed by treasury, thus providing further cost savings. Banks with automated notional pooling services that can operate within the parameters set by the company can provide effective and timely management of cash positions across the business.

UNPRECEDENTED CONDITIONS Terms of trade across all businesses are under pressure, with buyers paying as late as possible within the agreed terms, which has a knock-on effect on the overall cash position. It has therefore become more important to have visibility of cash positions across the business and the ability to manage them effectively. Visibility is relatively easy to achieve, based on standard SWIFT messages: it is what the company is able to do with the positions across all its accounts that is more important.

The ability for the bank to be able to transfer surplus liquidity on an intraday basis automatically across the business to where it is needed will be beneficial in meeting treasury business objectives. Further, to be able to centralise liquidity automatically and establish a cross-currency pooling arrangement without the need to swap from one currency to another is a significant development.

With liquidity management set to maintain its high profile, the time is now right for corporates to review their current procedures and discuss the solutions available with their bank.

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