Seeking Clarity from Crisis: CFOs and Treasurers Speak Out

How risk, regulation and cash management are driving new ways to manage enterprise treasury.

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Executive summary

In the three years since the collapse of Lehman Brothers, many CFOs and treasurers have worked diligently to apply the lessons learned from the global financial crisis. The crisis revealed shortcomings in many treasury groups. Now executives are striving to fill those gaps in areas such as cash management and risk management. CFOs and treasurers are seeking solutions that combine a new category of integrated treasury technology with expert advice in order to optimize their treasury operations. The executives who are able to quickly understand and implement these solutions can establish world-class operations and protect their organization’s financial positions in today’s global economy – an economy which is so volatile, it continues to focus the minds of CFOs and treasurers on the risks they face.

On September 29, 2008, the Dow Jones Industrial Average fell more than 777 points, its largest-ever one day loss. This event was one of the key events of the global financial crisis.

Three years later, we can clearly see how the crisis exposed weaknesses in many corporate treasury groups and the inability of their processes and technology to operate under worldwide economic stress. Today, many chief financial officers and treasurers are busy applying the lessons learned from the crisis, and 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—that became problematic as credit markets seized up.

About this white paper

In the spring of 2011, Reval conducted a series of interviews with financial executives at a number of public and private companies around the world. Our goal was to collect and disseminate the views of chief financial officers and treasury executives on the future of treasury management in a post-crisis world. What are their responses to the global financial crisis? What changes are they considering to operate in a new financial environment?

To conduct this research, Reval interviewed executives and other observers—such as consultants and journalists—to assess the impacts of the financial crisis on their treasury function and find out how they are working to apply the lessons learned from the crisis. Reval spoke with senior executives and other industry participants in North America, Europe, Asia and Australia for this white paper.
But some financial executives are making more progress than others. Those who are not able to quickly optimize their treasury management functions expose their operation to financial and operational risk. In this white paper, we will examine the important goals CFOs and treasurers are trying to accomplish in their treasury groups to ensure that they do not repeat the mistakes of the past, among them:

- 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 labor 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 both the individual and aggregate risks inherent in the company’s business. This requires effective ways to handle enterprise treasury and risk management.

PART I: FACING NEW CHALLENGES

Challenge 1:
A new attitude toward risk

One of the key focus areas among the CFOs and treasurers we spoke with is adopting a new risk mindset—with the treasury function playing a vital role. Now more than ever, CFOs and their treasurers worry about many different types of risk, particularly commodity risk, foreign exchange risk, interest rate risk and counterparty risk.

They have a heightened awareness that the treasury group is one of the few areas of a large company that can see many of an organization’s risks—and, thus, can have
a hand in identifying and managing risks from a holistic point of view. There is a new awareness of risk, both in daily planning and long-term decision making, and also in how risks can be interconnected.

Today the treasury group must not only deal with such issues as liquidity and funding risk, they must also have an understanding of risks that are not readily apparent and their potential for contagion. Executives to whom we 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 hedging strategies—which is made all the more challenging because of the extensive changes in the derivatives markets brought about by the Dodd-Frank Act and converging hedge accounting regulations.

As the global economy recovers, many treasurers find themselves managing almost unprecedented amounts of cash. As of June 2011, US corporations in the S&P 500 had roughly $1.1 trillion in cash on their balance sheets, according to FactSet. In Australia, as of July 2011 companies were depositing $1.25 into banks for every $1 they were borrowing, according to a study by East & Partners. To this date in 2010, their deposit-to-loan ratio was $1.15. With so much cash on hand, growth through mergers and acquisitions is tempting for many well-positioned companies. But with memories of the financial crisis still fresh, risk aversion remains high. To this end, treasurers are becoming more involved in M&A, evaluating a potential target’s positions and potential risks.

Globalization has also become more than a buzzword for most financial executives. Doing business in far-flung locales is now a day-to-day reality. As companies continue to globalize—especially in emerging markets—treasurers are tasked with issues such as managing exposure to multiple currencies.

**Challenge 2:**
**The 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 and/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, treasurers can no longer simply request and quickly receive large lines of credit from financial institutions. Today they need to begin considering this need far in advance and also examine their counterparty risk exposure. Treasurers are dealing with raising the importance of funding diversification and relationship management. They have more focus on contingent and diversified funding sources, especially those that serve them in the short term.

Another example involves cash held in foreign subsidiaries. In the past, many treasurers just accepted that this cash was trapped overseas and attached little strategic importance to these assets. Today, most treasurers must know how much cash exists overseas and where, the institutions in which it is held and how they can repatriate it if needed.

When it comes to compliance, treasurers are challenged with an increasing array of new regulations. For example, executives in financial institutions must comply with Report of Foreign Bank and Financial Accounts (FBAR) requirements. United States corporations must annually file with the IRS a list all foreign account holders over $10,000, and report the maximum balance in that account over the past 12 months. 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. Compliance with the many other regulations following the global financial crisis is one of the main drivers expanding the role of the treasurer and CFO.

Treasurers are also playing a pivotal role in gathering comprehensive exposure data from business units and managing the task of having these units own their appropriate risks. In addition, many treasurers see the need to allocate share-of-wallet to fewer banks—after determining which ones are willing to make significant balance-sheet commitments.
Challenge 3:
The CFO-treasurer dynamic

We 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, 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. The financial executives who are quickly able to master these challenges could put themselves and their organizations at a competitive advantage. For some treasurers, these new tasks include:

- Developing a keen understanding of the organization’s current and projected liquidity position.
- Understanding and securing access to short and long term funding.
- Establishing more active risk management discipline during periods of volatility, particularly around:
  - Commodity risk
  - Foreign exchange risk
  - Interest rate risk
  - Counterparty risk
- Managing tax implications across cash movement and intercompany lending.
- Partnering with the business side: working across departments and across business units to assist with the creation and execution of financial plans.
- Managing compliance.
- Managing resources to actively train and retain valuable treasury staff.
- Managing technology to secure and utilize the most effective tools to execute on the above tasks.

Treasury functions and dysfunctions

One of the biggest challenges we unearthed in our research is the concept that treasurers can no longer sit in an office and expect all the various functions of their department to run smoothly. Markets move too quickly and risk tolerances are too low, so treasurers need to be proactive about such questions as:

- How much cash do I have at the moment and how do I look over the next three months?
- What is my counterparty risk at today?
- What compliance actions do I need to take next, and what are my deadlines?

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However, keeping in mind the funding problems encountered by many companies during the financial crisis, many CFOs want treasurers to concentrate on their traditional—and vital—responsibilities. These include allocating cash, forecasting and determining the cost of capital and ensuring ample liquidity (as opposed to understanding the organization’s current and projected liquidity position, mentioned above). For more on the how today’s treasury organizations function, see the accompanying sidebar “Treasury functions and dysfunctions.”

Some CFOs noted that the financial crisis exposed a lack of controls in some organizations. 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, such as those mentioned above in the section on the expanding roles of the CFO and treasurer (Challenge 2).

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

**PART II: THE SEARCH FOR ANSWERS**

With all these new challenges come opportunities, and the financial executives we spoke with are all eager to face this changed economic landscape. Following the financial crisis there is a common understanding that there have to be changes to the way treasury operations work. The “new normal” of a typical treasurer’s role is not temporary – it represents a permanent shift in the expectations of what a treasury operation needs to deliver. In this section of the white paper, we will focus on important aspects of the solutions executives are seeking in the post-crisis environment.
Solution 1: Gaining better visibility

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

Many financial executives bemoan the fact that they lack complete visibility into all cashflows 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 told us 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 is today, leading to a demand for horizontal, integrated treasury management software. Treasurers in particular want an enterprise-wide treasury management solution that brings together various treasury workstation and risk management applications to give them a full view of their entire organization in order to meet all the demands placed on them. The market is trending toward such a system; one that can handle cash management, hedge accounting and risk management.

However, in the current marketplace, financial executives told us they perceive a number of barriers to this target state. The three most evident ones are:

1. Many financial executives told us that their key problem is integrating core treasury and risk technology with existing software, such as back-office applications, across the enterprise. Over the past decade, technology investments have been
made piecemeal from different providers. While some solutions providers are attempting to integrate these disparate pieces, this is rarely easy or inexpensive.

2. Their current software solutions may be disconnected and relatively inefficient, but financial executives still require technology vendors to show them a path to return on investment and clear performance gains to entice them to switch vendors. While exact ROI figures will vary for each successful implementation, typical users of integrated treasury management solutions can expect efficiency gains of at least 20 percent to 25 percent. For more on determining ROI, see the accompanying sidebar, “Measuring ROI.”

3. The market is mainly comprised of a handful of large enterprise software companies that do not provide a fluid STP enterprise treasury and risk management solution, and niche vendors that provide treasury management solutions as their sole offering.

Solution 2:
Is software as a service the answer?

Our 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).

Most of the individuals we interviewed see the benefits of adopting a SaaS-based solution. In fact, some told us that their IT staffs prefer solutions that are maintained off premise. The executives who are using SaaS-based TMS are experiencing many of the promised benefits: they see cost savings; they see the advantages of outsourcing support; and they can always use the latest iteration of the software.

Another clear advantage, as mentioned above, are the efficiency gains of integrated TMS. By streamlining workflow and outsourcing support with SaaS-based TMS, treasurers can potentially save even more time. Those time savings can give treasurers more opportunity to be analytical and strategic. Previously, 80 percent of treasury time

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**Measuring ROI (continued)**

3. Decreased cost of borrowing based on better liquidity management: Borrowing costs can be reduced through improved borrowing decisions and pay-down practices.

4. Reduced internal IT costs: IT support costs can be slashed when SaaS-based TMS eliminates the need for hardware support, disaster recovery, backup, upgrades and integration.

5. Reduced internal audit costs: SaaS-based TMS delivers better audit and control features and reporting as compared to a manual, Excel-based environment. Public companies can typically save 50 percent on their annual Sarbanes-Oxley audit.*

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could be spent on processing, with the remaining 20 percent available for analysis and strategy. SaaS-based TMS can reverse this, to enable 80 percent 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.

However, many industry observers point out that the strategic benefits of SaaS need to be better spelled out to the marketplace in order to differentiate it from hosted and ASP offerings that have preceded SaaS.

The two main drivers that are pushing SaaS solutions over hosted solutions are time savings and cost savings. To utilize a hosted solution, CFOs and treasurers still need the blessing of their IT department to install one. Of course, IT must schedule and manage the installation—some have taken up to 12 months—and continue to support the technology. SaaS solutions typically need very little time for users to get up and running.

As for cost, hosted systems typically cost $500,000 to $1 million to install, whereas a SaaS system is significantly less—due to the reasons outlined above. Over time, SaaS users also have the advantage of regular software updates direct from the solutions provider. Not only do these updates give users state-of-the-art technology, they also maintain regulatory compliance because new rules can be built into the software. Hosted solutions, on the other hand, require a user to purchase software updates and work closely with the vendor to install them. Institutional inertia can often lead to update purchases being skipped, which can leave treasury operations vulnerable to non-compliance with new regulatory requirements. Even when updates are purchased, the responsibility for installing them often falls to stretched internal IT teams.

Solution 3:
Managing regulatory risk

The technical advantages for SaaS delivery are numerous, but for CFOs and treasurers the various types of software architecture seem to take a backseat to functionality and the operational benefits that a truly integrated solution for enterprise-wide treasury and risk management can offer. Treasury groups are demanding integrated offerings
to shore up gaps in operational efficiencies, particularly in a post-crisis world where mitigating regulatory risk is imperative.

From new risk-based capital requirements for banks to higher penalties for airlines that bump passengers, many companies are being deluged with new regulations. Whether it be Dodd-Frank or Basel III; the IASB or the FASB, the flow of new regulations and the numerous bodies that can generate more is enormous.

Technology married with efficient processes and well-trained staff can help mitigate the risk of compliance trouble by giving CFOs and treasurers a more holistic view of an organization’s positions and risks. Our research suggests that financial executives and thought leaders who influence buying decisions will gravitate toward those players in the marketplace who understand this new regulatory landscape.

Conclusion

The roles of the CFO and treasurer have clearly come a long way since 2008. The financial landscape has changed dramatically, and will continue to change, not least because of the ongoing response to the crisis by various regulatory bodies. Compliance with these regulations and understanding their impact, while all the time monitoring for developments that can threaten a business, is a challenge with the current patchwork of solutions available in the market. A single technology solution that provides total visibility throughout an organization is the stated preference for many CFOs and treasurers. It would be reasonable to expect that with the financial crisis so fresh in the mind of so many executives, a move to this sort of technology solution will happen sooner rather than later.