BANK OF AMERICA

Putting evolving treasury capabilities to work

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Jonathon (00:00): You're listening to the Treasury Insights podcast. This is a part of our broader objective to foster a treasury relationship that prepares clients for the future, supports more strategic decision making, creates efficiencies and helps manage risk. Put another way we want to give you the power to see what's next. I'm Jonathon Traer- Clark, Head of GTS Advisory, and joining with me is Michael Bosacco, Treasury Advisory Executive of Bank of America. Our host will share his insights on how treasury has evolved in the past and where we might see treasury evolving in the future. Hi, Mike. (Hi, Jonathon.) Let's start by I guess considering a retrospective point of view. We talk about wanting to see the power of what's next, but I think it's also to reflect on what's happened in the past. So in your career, how have you seen treasury evolve from where it started to where it is to date?

Michael (01:01): We saw a transformational efforts from spreadsheets into what was originally called a treasury workstation, and is more familiar these days called a treasury management system. Banks traditionally provided, just that, banking services bank accounts, the ability to hold deposits, lending facilities, and then banks has treasury evolved into not only a bank providing core banking services but also banks that were providing more of a technology service. The ability now of the bank to reach further into its clients' pockets to demonstrate a strength around not only can we serve as your bank, but we can also provide some technology solutions. That is slowly evolved into a situation where now banks offer transactional services and products that are specific to certain channels within the treasury landscape. When I go and visit my clients, there's always a question around whether it's robotics or artificial intelligence, how digital assistance can have an impact on treasury or the ability of an artificial machine deployed in the background to uncover insights and a massive amount of data that can be used further as a layer to generate additional information from the data information that we didn't have before. So it's an incredible change.

Jonathon (02:29): The world is a very different place to how it was two or three months ago. Let's start with cash. Cash is the blood. If you like, the organization is the lubricant in the engine room of treasury. What would you suggest or what would you be focusing on right now?

Michael (02:45): Forecasting should be a discipline that every treasury pursues, and it's one of those that is a never ending pursuit. Understanding the trade flows, the intercompany flows, the treasury flows, the tax flows, the payroll flows, the ad hoc flows is critically important at all times. Whether you're flush with cash or you're able to raise funds in a blink of an eye in the CP market because your ratings are so high and everyone wants to buy your paper. I don't think either of those two things mitigate the need for forecasting and doing it well and holding teams accountable for the accuracy of the information that's provided.

Jonathon (03:25): If I paraphrase a little, essentially the age old adage, cash is King, it's still very true. But what you're also sort of highlighting is the fact that it's also important to know where that cash is coming from at any given time as well.

Michael (03:40): It's tough to say cash is King and not understand its source when you're going to have it or when you're going to have to let go of it absolutely.

Jonathon (03:48): Beautifully put. You touched on commercial paper and I guess market activities obviously. How do you see banking partners helping with that, how should we say, the life cycle of cash across the organization?

Michael (04:00): Banks have a critical role to play, whether it's technology offering or it is very much we can manage your liquidity on your behalf and provide reporting. You just tell us how you want funds to move that can be managed. The strength of the banking partner community from an operational standpoint is key, and I don't want to step into risk necessarily, but did mention briefly what risk looks like. That should be a consideration as you think about managing cash and how your banking partners can facilitate certain operational efficiencies. Also, I have to be considerate of the risk that's being invoked as a result of having that partner too deeply involved in liquidity management, for example.

Jonathon (04:45): It makes a lot of sense. It's impossible not to consider risk. I think it's one of those things that certainly is evolved in response to market based triggers. When we consider market stress events for example, then obviously risk becomes a clear part of that. If I was sitting in my seat today, I would certainly be thinking very hard about investments as always. The tradeoff across the treasury triangle of protection of principle, duration and yield and whereabouts, I wanted to create a balance there. I'd be thinking a little bit about liquidity, how quickly I wanted to fund or my time to funding if you like. I also would think about my supply chain and supply chain financing. I think the other aspect of that of course is you need to know them very well from a stability perspective. Do you see the focus in that area changing? Do you see the applicability of the techniques changing in that or do you think it's a continuation of where you already are?

Michael (05:40): I believe it changes. The risk portfolio, if I may refer to it as such, I hope changes. I start to think about my categories of risks, those that you just mentioned for example and assign given market conditions, different quantitative and qualitative attributes against those risks and then monitor and measure again on a regular basis that positions me incredibly well to be, not reactive, but proactive to support my customer base, to support my supply base, to mitigate my exposure to certain customers. The ability to marry data in a way that sends signals into my risk management portfolio that would suggest I should reevaluate the credit exposure to a certain customer given that customer's market actions or changes in payment behaviors alongside perhaps an analyst report. On the opposite side of that, you have your supply base.

Michael (06:42): It should be a payment policy, which is very financially driven and part of that should be the type of criteria used to measure the viability of a supplier, its segmentation of that supplier. It's critical means to the overall organization and when that and how that supplier is paid or banks counterparty risk. This one always comes up. It's a financial measure against how much exposure a corporate treasury has to a bank. It's kind of a traditional measure, but counterparty risk today is not just at the bank level, its suppliers, it's customers as well among many others. This comes again back to that risk portfolio. It's not just a financial measure. One of those changes is around cyber risk. Cyber risk is driven by a counterparty, one that you never want to know necessarily, but they want to get to know you. When you think about who you're dealing with, your counterparties as a corporation, as a corporate treasury, that should become a measure within your risk portfolio to ensure that you're not exposed to additional cyber risk because you have too many banking partners or your vendor selection criteria is absent a cyber-assessment on that particular supplier.

Jonathon (08:00): That's interesting because at the beginning we were reflecting on technical evolution and of course the counter side to that, no pun intended, is of course that digital connectivity creates risks in its own right from a cyber perspective even just from a connected ecosystem perspective. There is a lot of volatility as always in the capital markets and obviously the volatility scale changes day by day, but treasuries have always done an element of FX hedging and interest rate hedging and so on. Would you see those disciplines changing or would you change perhaps the frequency by which you are hedging? What would you do right now?

Michael (08:39): The idea around hedging centers on predictability, not speculation. Treasury is trying to ensure the predictability of an outcome. As a result, using a derivative of some kind to take a position again to minimize changes of an event that may happen. Cash flow side or has already happened. Balance sheet side. This is another one, Jonathon, I sound like a broken record a bit, but hedging should be assessed on a regular basis and that shouldn't be just the outcome of what you did and determine that, okay, well my hedge was within my tolerance. That's good enough. The distribution of that risk is changing and these triggers, these events increase the magnitude of change. Incorporating the ability to have a flexible hedging program, whether it's interest rate, whether it's currency, commodity, it doesn't matter, should be dynamic enough to flex against the change in risk that is brought on by the event. I'm not saying we as treasurers can predict the event, but what I am saying is that we as treasurers can understand operationally what we may need to do to flex our hedging programs to mitigate, right, to maintain the predictability. That's what we're trying to do in the hedging space.

Jonathon (10:05): The dynamic management that you're applying to these various elements of risk management in accordance to the volatility, and the rate of change of that change within your environment. If there's a need to hedge more dynamically, just simply because you're seeing a lot of change in rates in the FX markets for example, then scale up your approach to it accordingly, right? (Right.) Great. I mean obviously technology is a key enabler for that, but if we move on a little bit, actually, let's just reflect on one little thing or maybe this is a connection between the two. Did you see any kind of the change in risk parameters associated with how we're working today versus how we were say a year ago?

Michael (10:47): Yes. Ways of working today are a bit different. There's certainly a lot more digital slash remote communication than I think we're all accustomed to. As a result of the distance, not only between each other but also from the operation, we are both hearing and experiencing an impact that perhaps was not as visible absent the new sort of way of working that we've been accustomed to in the last several weeks here. The impact of that distance really is demonstrating that while there's a lot of risk in my ability to initiate payments because the operation is at a physical location requires a physical signature, for example, and the ways of working presently do not accommodate that type of environment. There's this reactionary rush to try and digitize paper-based payments, whether that's the traditional EFT or single use card or multi-use card. There's this rush, now reactionary rush to address it. That's an area that I think many treasuries didn't account for. I'm a big believer in having the availability of levers to shift how I'm paying, when I'm paying, what programs I may use and why and when levers around managing the risk or collecting my cash, being predictive in that space. Critically important at all times, not following an event or a trigger.

Jonathon (12:21): It sounds to me like having agility of continuity of business operations is a critical aspect now of building a treasury function that can mutate as needs be in response to demands, be those business demands, market based demands, customer base demands, et cetera. So that could be to switch between paper to electronic as you alluded to, it could be to change working capital parameters across the supply chain and how you manage inventory and your payables cycles. But we're really talking about optionality as being a critical design characteristic that we should all look to think about in our treasury functions. Am I right?

Michael (13:03): You're right. Having a treasury that is dynamic, one that is prepared, allows or I should say minimizes the disruption associated with business requirements/M&A triggers in the marketplace. Currency volatility as an example is a trigger. Events that drastically change the environment. A static treasury is going to be staring into a very deep, very dark tunnel. A treasury that's prepared and agile will be picking its path through the light and able as a result to manage holistically. And holistically, I mean in support of its customer base, its supply base, having an ecosystem as a whole, managing through, picking again different lights that it needs to chase to ensure the stability of its counterparties inclusive on its own cash war chest.

Jonathon (13:57): It's interesting though that change management or adaptability, there is a word I think that's used a lot. Maybe not quite to the extent it should be really has gravitas in a function that is essentially orchestrating transactional flows across the business. When you and I have debated, why should you be restrictive in the way that you think about distribution of monies to your suppliers or the way that you might want to collectively receive monies from your customers and then how you interact with other channels such as your banking partners, how you pay your staff, how you deal with expenses and everything else.

Michael (14:40): Well said. Jonathon. Completely agree.

Jonathon (14:42): We've mentioned a lot about technology being a key enabler for the effectiveness of the treasury function. We've discussed how the very aptitude and attitude of the treasurer in terms of being flexible in thinking, open-minded, dynamic, constantly seeking to self-improve, as being key attributes of if you like a an agile treasury organization and one that can respond very quickly. We've looked at areas such as cash flow, working capital, we've looked at risk, we've looked at digitalization and some areas focused in that space. I think we've even pondered the macro continuity and agility of the business and the back office functions as well. Is there anything else that you would think about today perhaps a greater focus today than you may have done in the past year or so?

Michael (15:36): I probably would ensure the integrity of my forecast and by that I mean understanding the direct forecast flow. What treasury is traditionally responsible for, that 13 week rolling forecast is what we most commonly hear and is probably most traditionally used - direct cash. It's already been booked as a sale. It's on my balance sheet. In other words, it's already been agreed to pay. Marrying that with the indirect forecast, the longer term view, which is traditionally comes out of a FP&A division within corporate finance and that's typically driven out of the business units that comprise the enterprise.

Jonathon (16:20): Do you mean like a hedging program, that sort of thing or even just a forward view of fund flow.

Michael (16:26): Forward view of fund flows as forecast by the business.

Jonathon (16:32): Brilliant! I think we'll leave it there. Thank you so much for your insights and your considered thoughts. It was amazing to hear your take on all of this. (Thank you, Jonathon!) You've been listening to treasury insights. I'm Jonathon Traer-Clark, Head of GTS Advisory. My co-host today was Michael Bosacco, Treasury Advisory Executive. As each day brings innovation and opportunity, we are dedicated to working with you to turn technology advances into intelligent treasury.