

CURRENT TRENDS AND THE EVOLVING ROLE OF CORPORATE TREASURY MANAGEMENT

BEATA ŠARKANOVÁ

Ing. Beata Šarkanová, Katedra financií a účtovníctva, Ekonomická fakulta Univerzity Mateja Bela, 048/446 6320,
beata.sarkanova@umb.sk

Abstract

Corporate treasury management as a specialized part of financial management in enterprises transformed significantly under the influence of financial crises, globalization, technological development, and the increasing complexity of economic environment during the past 50 years. The paper is focused on the evolving role of corporate treasury management over the last few decades, and on current trends influencing the incoming modern corporate treasury function.

Key words: *treasury management, history of corporate treasury, trends in treasury, role of corporate treasury*

Introduction

Treasury management could be defined as a specialized subsystem of corporate financial management responsible for corporate liquidity management, financial and investment decisions of companies, risk management, relationship with banks and other external subjects, moreover with an important advisory and supporting function.

The term *treasury management* and its understanding could be most probably derived from different meanings of the term *treasury* such as: (1) "a collection of valuable things" (<http://www.macmillandictionary.com>, 10.10.2015), (2) "the funds or revenue of a state, institution, or society", or (3) "a place or building where treasure is stored" (<http://www.oxforddictionaries.com>, 10.10.2015). According to Rajendra (2013), in business history the term treasury has been used for centuries derived from the term *tresorie* meaning "room for treasure". Since then, the treasure has been replaced by money and assets owned and used by companies to generate value for its stakeholders.

Generally, the rise of the corporate treasurer as a professional specialization has been influenced by various factors including (Billings, 2007) changes in organization of companies, changes in financing of companies, change and innovation in financial markets, wider professionalization of management, or internalization of business.

1. The evolution of corporate treasury management

While the origins of corporate treasury management (as mentioned by Billings, 2007) can be found in US companies already in the nineteenth and early twentieth-century, e.g. General Electric Company (1899), U.S. Steel Corporation (1904) or Union Typewriter Company (1906) where terms treasury or treasurer have already been used, in Europe the main stimuli leading to the development of corporate treasury in companies were the economic and financial uncertainties in 1970s. For instance, the evidence tends to support the view that treasury management in British companies developed in late 1960s and 1970s. Furthermore, the establishment of the Association of Corporate Treasurers in 1979 significantly supported the creation of the concept of treasurer's knowledge with seven pillars of treasury. Subsequently, the initial seven pillars have been reduced to the following five pillars: (1) corporate financial management, (2) capital markets and funding, (3) money (or cash) management, (4) risk management and (5) management of the treasury function (operations).

The development of corporate treasury during the past few decades can be divided into three phases or generations of treasury management (see figure 1). The fourth phase represents the future of corporate treasury.

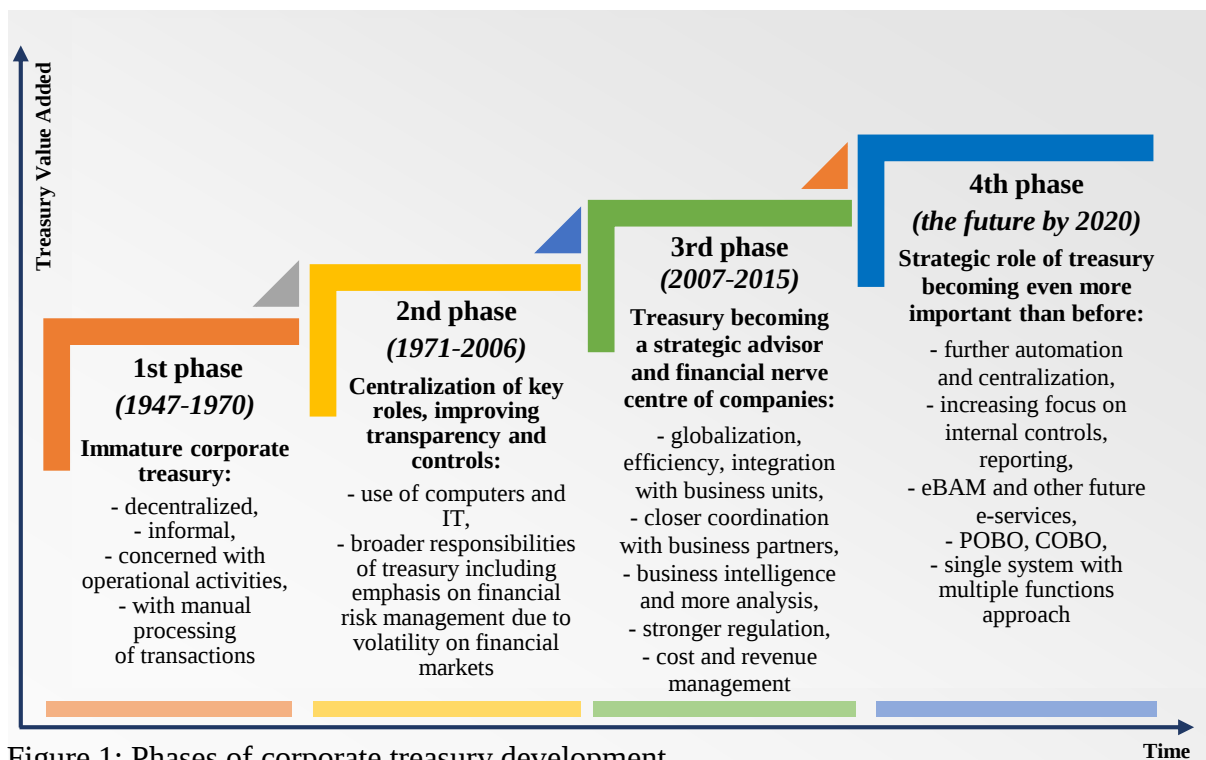


Figure 1: Phases of corporate treasury development

Source: Author.

The first generation of treasury management represents the period of corporate treasury development before 1970. San José et al. (2008) describe treasury-related tasks in the 1960s as purely routine work and as an ancillary function. According to Polak et al. (2011), prior to the 1970s treasury functions were immature, fragmented or informal, processes were manual without the use of computer, corporate treasury was largely decentralized and concerned with operational activities. Furthermore, Shah and Yung (2012) add that companies engaged in cross-border business typically established local treasury teams in those countries where they operated, processes such as settlements were performed manually and the communication of treasury with headquarters was often inadequate or delayed. Additionally, McCullie (2012) specifies that prior to 1970 exchange rates were fixed, liquidity was plentiful, the commercial paper market was still developing. Banking was about relationships, companies borrowed mainly from banks and kept ample compensating balances.

The first significant changes began in the early 1970s after the collapse of Bretton Woods system and the end of the gold standard (McCullie, 2012). The 1970s represent the beginning of *the second phase of corporate treasury development*. The economic environment was hit by recession, exchange rates and the global financial markets became more volatile. The recession favoured the emergence of short-term monetary policy instruments. However, corporate treasury was still restricted to obtaining of funding, management of payments and collections and maintenance of bank balance positions. Corporate treasury became integrated into general corporate management in the 1980s and began to be based essentially on a liquidity management (or cash management) perspective (San José et al., 2008). According to Polak et al. (2011) volatile financial markets increased the focus of the treasurer on financial risk analyses and management. Technological development, and subsequently, the availability of

financial data and information increased the transparency and effectiveness of transactions. The scope of corporate treasury broadened to include financial risk management and required improved dialogue with internal and external stakeholders. Furthermore, as companies expanded their businesses, treasury centralization became a convenient possibility (Shah and Yung, 2012).

Regarding the development of cash management as a function of corporate treasury, Bellin (2014) points out its local or regional character despite globalization as a result of key differences between Europe and North America. While US companies have had one main currency leading to lower FX, and enabled a uniform payment infrastructure and greater centralization of cash management, European companies have had to deal with many currencies, therefore higher currency risk and more difficult way towards standardisation of payments. European treasury management has been most often executed either per location or financial hubs – especially in London, Zurich or Frankfurt. Obviously, the introduction of SEPA significantly pushed the standardization of payments in Europe. Another differences include the extensive use of electronic payments in Europe with one hundred per cent dates accuracy (focus on medium-and long-term cash planning) in contrast to the use of cheques in the United States (focus on short-term cash management), or the separation of accounting from treasury in Europe in contrast to the United States, where treasuries are still tied in to accounting.

Nowadays, corporate treasury function is in its *third generation*. According to Shah and Yung (2012), the Global Financial Crisis of 2007-2009 supported the transformation of treasury from a support function into an important advisor of company. Further centralization of treasury can lead to gathering of timely and accurate information on the flow of funds and financial data across the company, improved analyses, and also forward-looking strategic approach. The crisis emphasized the role of liquidity and risk management, the need to focus not only on earnings, but also on cost savings, strengthening of internal controls, and relying on internal sources and liquidity instead of dependence on external financing. Polak et al. (2011) mention that corporate treasury must act in far closer coordination with its business partners. In third generation, treasury has become a strategic advisor, more closely integrated with business units, supporting globalization and efficiency. According to McCullie (2012), in this era treasury transforms into the financial nerve centre of companies. McCullie points out that intelligence is now required as the strategic application of information in order to generate and monitor liquidity and mitigate risks as well.

2. Corporate treasury in the future – strategic and centralized

As already mentioned above, the role of corporate treasury management transformed during the last (approx.) 50 years from an informal and decentralized function with manually processed transactions into an automated, centralized, trusted strategic advisor of companies with a number of different responsibilities.

According to the results of the “2014 AFP Strategic Role of Treasury Survey” by Oliver Wyman and the Association for Financial professionals (AFP, 2014) and earlier surveys conducted in 2006 and 2011 (AFP, 2006; 2011), there are several key reasons contributing to the expansion of treasury’s strategic role within companies (see figure 2). The results show that since 2006 the number of reasons has increased. Recently, major factors contributing to the rise of the role of corporate treasury include:

- the importance and emphasis placed on cash management and corporate liquidity in the current economic environment,
- closer attention being paid to liquidity and risk exposure by senior management and board,

- innovative effort of companies in leveraging the skills that reside in treasury,
- and also a more cross-functional approach of companies to their activities.

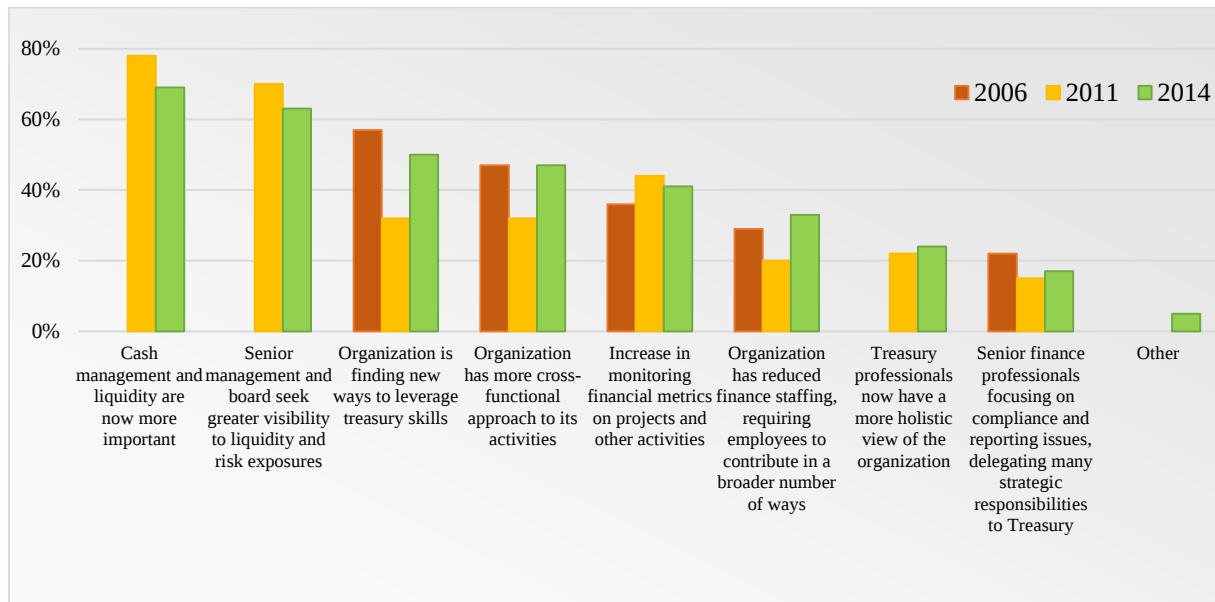


Figure 2 Key reasons for greater strategic role of corporate treasury

Source: Author based on AFP Strategic Role of Treasury surveys (2006, 2011, 2014).

The rise of treasury's strategic importance will continue in the future. According to Masquelier (2014), the 2020 corporate treasurer function (*fourth phase of corporate treasury development*, see figure 1) will become even more strategic with increased value-added, while operational matters will become relatively less important with lower value-added. The results of "The future of the corporate treasury" survey (a survey of large corporate treasuries and their objectives until 2017) conducted by Nordea (2014) support this opinion and show similar expectations (see figure 3). The future of corporate treasury is described as strategic and centralized.

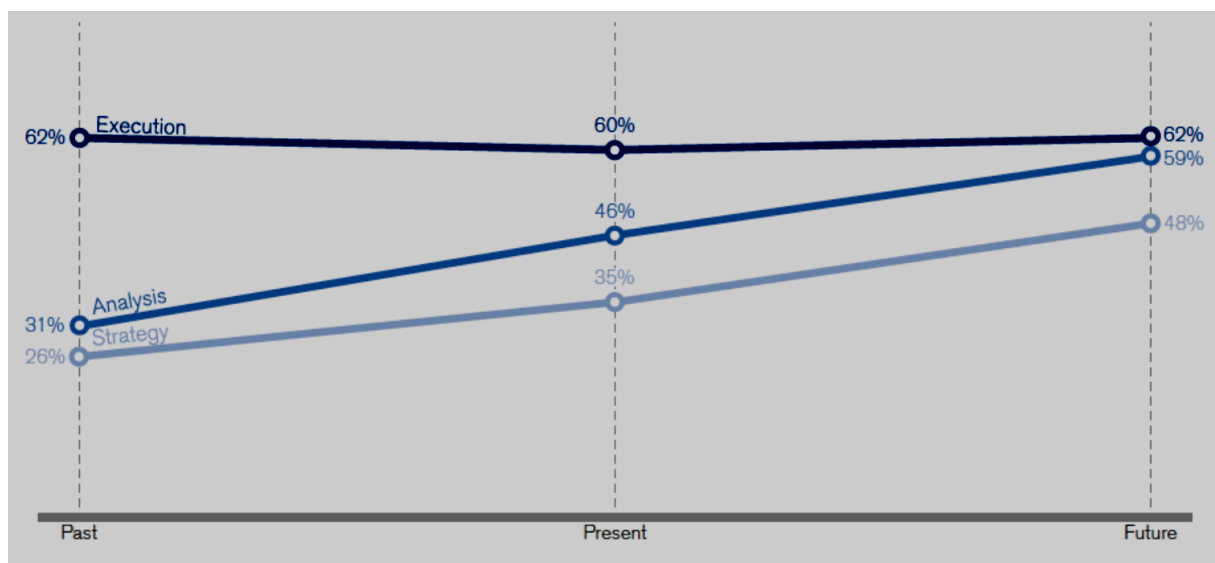


Figure 3: How the treasury views its role (percentage of respondents giving "high importance rating")

Source: Nordea, 2015, p. 6.

Masquelier (2014) describes the future of corporate treasury by 2020 with the following watchwords: productivity, mobility, portability, adaptability, analysis and compliance.

The focus on internal controls will be increasing and will act as a driver towards automation and to full Straight Through Processing (STP). The multi-system approach will be replaced by a single system with multiple functions. This level of automation will include the automation of all flows, automated and secured (encrypted) financial transactions since protection against fraud becomes one of the major issues of the oncoming years.

In case of cash and liquidity management, Masquelier points out the importance of the move to “Payment On Behalf of” (POBO), “Collection On Behalf of” (COBO). According to Arnold (2014) channeling payments / collections through a single legal entity, by making payments on behalf of / collections on behalf of multiple group entities enables and helps treasurers to rationalize their accounts, increase efficiency, and simplify cash management. Effective management of cash could be achieved also by the use of eBAM (mentioned by Masquelier, 2014) – electronic Bank Account Management – an automated, integrated and dematerialised approach to bank account management allowing companies to send messages to their banks using SWIFT XML messages, or by the use of other e-services (Kelly, 2015).

Masquelier (2014) argues that by 2020 the approach to risk management should become global and integrated, with tools to support decision-making and business intelligence reports meeting the needs of top managers and board. This post-2015 trend could also be described by the term risk-intelligence culture also mentioned by Vergues and Tliba (2014).

Conclusion

Since its beginnings in the second half of the twentieth century corporate treasury management changed substantially. In its first generation, operating in quite stable economic environment, corporate treasury started as an immature, largely decentralized, fragmented or informal function of corporate financial management, focused especially on operational issues. Economic uncertainties in the 1970s, volatility on financial markets hand in hand with technological progress affected the development of corporate treasury and shifted it towards its current form. Consequently, in its second generation corporate treasury expanded and broadened the scope of its responsibilities. The continuous change in treasury since the 1970s can be described by a few words: centralization, automation, standardization. These challenges and trends also supported the change of corporate treasury from an operational unit into a strategic advisor and will continue to influence the treasury function in the future.

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