Alleviating the trapped liquidity crunch

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ASIA PACIFIC IS AWASH WITH TRAPPED LIQUIDITY, AND CORPORATES REQUIRE TAILORED SOLUTIONS TO MAXIMISE THEIR FINANCES

At both a regulatory and a corporate level, there are varying degrees of acceptance and development when it comes to liquidity management in Asia Pacific. While some of the region's more mature markets have world-class systems and regulations governing the movement of liquidity, other jurisdictions make the free transfer of liquidity a huge challenge for banks and clients looking to optimise their trapped cash.

In a nutshell, corporates and the banks they partner to optimise liquidity structures cannot rely on one generic model to unlock trapped cash. Corporates require tailored solutions to optimise liquidity, irrespective of whether they are domestic, regional or multinational organisations. Given the different regulations and requirements in Asia Pacific, one size does not fit all when optimising trapped liquidity within balances.

FACTORS INFLUENCING TRAPPED LIQUIDITY

Trapped liquidity is defined as the cash surpluses that remain in any given country by the intervention of regulatory means.

For the banks providing these solutions and the clients requiring enhanced services, there are several external factors influencing what can and cannot be done when addressing trapped liquidity.

Country-specific regulations are one factor that has restricted the movement of liquidity around Asia. Equally, the unique aspects of each corporation that operates in Asia Pacific, whether they are domestic, regional or multinational, makes finding one model for optimising trapped liquidity near impossible.

In many cases, liquidity can become trapped due to tax implications, the prohibition of inter-company lending and the lack of foreign currency convertibility and transfer. Aside from these external factors, many of the problems faced by corporates involving trapped liquidity arise from insufficient infrastructure, the absence of monitoring or on-the-ground regional treasury, and a lack of accounting and willingness to embrace solutions like co-mingled funds.

These and other factors in Asia Pacific means that trapped liquidity is a very real problem for many corporations and provides a significant opportunity for transaction banks with proven and automated solutions in optimising dormant surplus cash. And given this back-drop, it is unsurprising that the use of liquidity management tools and solutions amongst corporates in Asia Pacific is lower than in other regions.

THE REGIONAL DILEMMA

At a country level, regulations restricting the movement of trapped liquidity have been problematic for corporations, causing many of them to accept trapped liquidity as a negative component of managing a treasury in this region. For multinationals and local corporates with Pan-Asian operations, the challenge of optimising trapped liquidity has been particularly troublesome, given the complex and contrasting regulatory framework found in each country.

Prohibition of inter-company lending, domestic tax implications, local currency regulations and in-country account reporting all play a detrimental role in optimising trapped liquidity in Asia Pacific.

For example, many corporates have often struggled in optimising liquidity management structures in China. As a result of a highly regulated financial and foreign exchange regime, standard liquidity management structures available in the world's more developed financial markets have not been available in China, breeding pockets of trapped liquidity. Chinese regulation prohibits direct inter-company lending, which most multinationals find to be a common treasury technique in many developed markets. Direct funds movement from one legal entity to another is also illegal in China, unless it is a trade-related transaction, payment of service or royalty fee.

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Elsewhere around the region, certain markets add to the complexity of effectively managing liquidity and getting the most out of in-country cash balances. In countries such as Indonesia, Malaysia, Pakistan, the Philippines, Sri Lanka and Taiwan, the local currency is not internationally transferable or convertible, which creates further liquidity shortfalls on balances. Many countries in Asia also have tax reporting issues, which further constrain the effectiveness of optimising liquidity.

FLEXIBLE SOLUTIONS TO OPTIMISE LIQUIDITY

Increasingly, it is becoming obvious that banks have a greater role to play in maximising corporates' trapped liquidity which is stuck in regional markets.

To succeed in this often-frustrating endeavour, banks must be forthright in their understanding of client objectives and cash profile when structuring solutions. They must also maintain an encyclopedic knowledge of the individual market regulations that contribute to trapped liquidity in the complex and diverse Asia Pacific region.

So where does the solution to trapped liquidity lie? Globally and regionally, Citi is at the forefront of optimising trapped liquidity and is leading the evolution in Asia Pacific. With an automated platform that is live across 16 countries in Asia Pacific, Citi is the unrivaled leader in providing solutions for optimising trapped liquidity in this region. Through unique solutions, trapped liquidity can be unlocked and its true potential as a boost to regional balance sheets can be realised.

More specifically to clients in Asia Pacific, innovative optimisation products are becoming extremely popular, with the introduction of several specific solutions, which can be tailored to suit the requirements of corporates.

COMBATING TRAPPED LIQUIDITY

To counter the impact that squeezing yields can have on companies facing trapped liquidity problems across the region, banks have been forced to innovate. Clients can now have access to a new solution that leverages its overall cash balance into Citi's regional accounts. Through this liquidity management solution, clients experience both improved yields and compressed debit rates in their operating accounts.

The area where the trapped liquidity challenge faced by many countries is being addressed head-on is through extracting liquidity from balances. This process works through the use of customised instruments to enable corporates to extract surplus cash from some of the more tightly regulated countries around the region. By leveraging Citi's resources, corporates can address trapped liquidity issues by allowing holding companies to borrow surplus funds from subsidiaries.

The third point of innovation impacting the industry and how corporates are optimising trapped liquidity in Asia Pacific is through the application of liquidity swap solutions.

Finally, the trapped liquidity dilemma in Asia Pacific has prompted Citi to introduce its Interest Optimisation solution to the market.

Unlocking trapped liquidity and optimising liquidity balances both regionally and in-country was never meant to be an easy endeavor for clients. As markets continue to evolve in Asia Pacific and regulations permitting the movement of funds liberalise further, optimising trapped liquidity will become easier, which will in turn breath life into more sophisticated products offered by financial services partners.

CITI'S APPROACH

Visibility, mobilisation, optimisation: improving these core metrics are high on every treasurer's list of goals. Meeting these challenges is tough, and increasingly so as markets, competition and regulations evolve. Success consistently demands an end-to-end cash and treasury approach to address these three core challenges. With market leading and reliable global infrastructure, Citi has a proven track record of providing customised liquidity solutions to companies in Asia Pacific. Citi brings together the breadth and depth of products, geographic footprint, balance sheet and experience to service your needs – today, and as these expand and evolve in the future. ◢

GRUNDFOS

A TRAPPED LIQUIDITY CASE STUDY

Denmark-based Grundfos Group is one of the world's largest pump manufacturers with revenues in excess of US$4 billion and a regional presence in 13 countries. Like many other multinationals in Asia Pacific, Grundfos Group has experienced issues with trapped liquidity through an array of challenging and unique markets like China, India and Thailand. Despite running a regional treasury centre in Singapore, the absence of a tax-beneficial treasury entity does not enable the firm to effectively centralise and optimise liquidity.

In 2008, Grundfos Group mandated Citi with the challenging task of maximizing its liquidity management structure, consisting of in-country and individual country surplus balances. The firm also charged Citi to solve problems with intra-month mismatches of liquidity positions across different currencies, which are used by Grundfos to short positions with bank overdraft lines.

Faced with a large regional presence and numerous difficult markets for optimising trapped liquidity, Citi was forced to think outside of the box and provide a solution that met all of Grundfos Group's requirements. That solution was Citi's Interest Optimisation.

According to Petra Ho, Grundfos' regional treasury manager: "The biggest challenge that Grundfos Group treasury faced in Asia was to develop a solution that enables us to leverage our regional relationship with Citi to improve our interest income, whilst concurrently compressing our interest borrowings. Also, we needed a solution that requires minimal maintenance and documentation efforts given the limited resources within regional treasury. This solution enables us to meet our immediate needs with minimal implementation efforts."

By linking all of its operating accounts through Citi's Interest Optimisation platform, Grundfos Group can now leverage all its pockets of cash across the region to improve overall interest enhancement and overdraft rate compression.

In partnership with Citi, Grundfos Group has now implemented an automated regional interest optimisation structure in all 10 countries, with two more coming live shortly. ◢