Bats at the Ready!

Navigating Treasury Curve Balls in 2022

Expecting the unexpected is *de rigueur* these days. So, we asked Peter Cunningham, Managing Director, Head of Corporate and Public Sector Sales, EMEA, Citi, to stand in left field, gaze into his crystal ball, and give us his predictions for the challenges and opportunities that treasurers might encounter in 2022.

By **Eleanor Hill**,
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The past two years have arguably been the ultimate test of treasurers' ability to cope with curve balls.

Indeed, treasury professionals have had to pivot from one extreme to the other. As Cunningham explains: "This time last year, many corporates were still struggling liquidity-wise as a result of the Covid crisis. They were busy shoring up their positions, both through external capital-raising exercises and releasing cash internally by pulling levers in the cash conversion cycle."

Now, 12 months on, the tables have turned. "Given government incentive schemes and quantitative easing, there is now an excess of liquidity in the market. This presents a different type of headache for treasury teams: many are struggling to find an effective home for their short-term liquidity, and this is exacerbated by the challenging rate environment."

As a result, short-term investment policies will require treasurers' attention over the year ahead. "Regular reviews of counterparties, asset classes and tenors will be needed in 2022 – perhaps more than ever before. And treasury teams may need to look to 'step out' from traditional instruments in order to optimise their portfolio and returns, assuming that the risk profile is a good fit. ESG-driven short-term investments will no doubt also be more firmly in the picture in 2022 as well, with sustainability KPIs becoming more commonplace in all aspects of corporate treasury."

Supply chain vulnerabilities

Another area that has been significantly impacted by the pandemic over the past 24 months is the supply chain – from both a physical and financial perspective. "Despite some ongoing challenges, such as semiconductor shortages, we are starting to see a good dose of recalibration in supply chains. Early on, Covid exposed some huge vulnerabilities in physical supply chains, especially those that were geographically widespread, concentrated in terms of critical suppliers, or those which operated on a just-in-time model," says Cunningham.

In response to these challenges, companies started to build in greater resilience, through tactics such as nearshoring or onshoring of supply as well as multisourcing, in order to reduce counterparty risk. "In 2022, we expect to see that work continuing as it's not a quick 'plug-and-play' conversion – supply chain changes take time and effort. And from the treasurer's perspective, there will inevitably be impacts on the financial supply chain." These potential knock-on effects include changes to the cash conversion cycle; shifts in counterparty and country risks; and alterations in the basket of currencies the treasurer is dealing with.

Over the next 12 months, Cunningham therefore expects to see topics such as 'transactional FX' high on the treasury team's agenda. Supply chain finance (SCF) and dynamic discounting can also be added to this list, as companies look to continue to support, and build good relationships with, their strategic suppliers – while maintaining control of working capital.

Global tax and regulatory hurdles

As supply chain geographies shift, tax legislation is also likely to become more of a factor for organisations in 2022. One clear change here is the forthcoming global minimum tax (GMT). Cunningham outlines the changes here: "Recently, the OECD [Organisation for Economic Co-operation and Development] and G20 have published a Two-Pillar Framework for global tax reform, which is being described in the industry as BEPS [Base Erosion Profit Shifting] with teeth. The first pillar aims to ensure the companies with a permanent establishment in a country are actually taxed there. This has become a particular issue in the age of e-commerce. The second pillar revolves around the GMT, which will introduce a minimum corporation tax rate of 15% in all jurisdictions."

But what will all of this mean for corporate treasurers? With implementation of these rules due in 2023, Cunningham believes that there will, unfortunately, be some additional workload and complexity. He expects that treasury teams will be involved in demonstrating where the company's taxable base is, which inevitably means having local accounts, paying in local currencies and paying local taxes. This could potentially lead to "liquidity puddles" in markets where it is not necessarily straightforward to repatriate cash, he says. There may also be related conversations around where SSCs are located, especially those dealing with treasury matters.

Given the level of due diligence and technical work to do here, Cunningham expects to see treasurers working more closely with their tax and banking partners throughout 2022 to "figure out what this global tax reform actually means for them and how to comply without undoing the efficiencies that have been carefully built up over the years".

Another change on the regulatory horizon is the introduction of additional reporting requirements and disclosures around ESG. Work here is ongoing, but as world leaders met in Glasgow for COP26 in November 2021, the International Financial Reporting Standards (IFRS) Foundation Trustees announced

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the formation of a new International Sustainability Standards Board (ISSB) to develop a comprehensive global baseline of high-quality sustainability disclosure standards to meet investors' information needs. And, as Cunningham points out, "this is a very clear indication of the direction of travel in terms of ESG reporting – and finance and treasury teams will be at the heart of the action".

Treasurers have much more to offer in the ESG space than merely being conduits for information, though. Indeed, close involvement in ESG is becoming a treasury imperative, believes Cunningham. "What was remarkable about COP26 was the strong presence and involvement of private sector organisations, not just governments. In fact, one corporate treasurer was a spokesperson at the 2021 event – which is hugely significant in terms of ESG's growing prominence in our profession."

And off the back of COP26, corporations are making pledges to be 'net zero' by 2050 at the latest, meaning that treasurers are increasingly expected to proactively contribute to their organisation's ESG activity. "ESG is no longer something to simply talk about. Action is happening. In addition to investment in green assets, as I mentioned earlier, treasurers are exploring options such as green and sustainable bonds and loans, as well as sustainable SCF programmes to incentivise suppliers to act with greater integrity."

With this further integration of ESG into the treasury function, Cunningham is also seeing more focus on all aspects of sustainability, rather than the traditional focus on the 'E' aspects. "The social and governance components have become equally important in 2021 and that will continue into 2022 as corporates look to cover all three ESG pillars, including the interplay between the three – not just in consumer-facing industries but in B2B sectors too."

E-commerce continues to soar

Like ESG, the realm of e-commerce is also evolving from being the sole preserve of consumer firms. While B2B digital sales are still nascent, they look set to increase significantly in the years ahead, as digital transformation does away with old-fashioned, clunky, and costly behaviours, says Cunningham. "E-commerce is no longer a hobby," he quips. "For both consumer-facing organisations and B2B corporates, building a frictionless digital experience for their customers is a no-brainer."

Of course, the consumer space remains well ahead of its business counterpart, not least because payment innovations typically start there before migrating into the corporate world. This makes the consumer realm a great learning ground for treasurers wondering how to prepare for B2B e-commerce and its financial ramifications, or those looking to improve their existing e-commerce offering.

Here, Cunningham says that education is key to getting e-commerce right – and treasury has an important advisory role to play when decisions are being made. "Treasury needs to be in front of management-level conversations around e-commerce because channel decisions inevitably impact payment and collection methods in terms of cost, settlement period, counterparty risk and so on."

While treasurers might traditionally have been on the receiving end of such decisions, Cunningham is starting to see them be much more involved in e-commerce discussions. But for those treasurers who aren't yet in that position, he says it is important to build the business case for the treasurer's involvement early on. "It's not an easy conversation to have, but bringing the CFO onside is often a good place to start. And the benefits will start to become very clear once the implications of payment methodologies are explained in terms of clear financial costs."

API DEVELOPMENTS GAIN TRACTION

Underpinning the rise of real-time data and integrated forecasting systems is the growth in APIs. While APIs themselves are not new, treasurers are now starting to embrace them with gusto. Cunningham notes: "We've seen a real uptick in the number of corporates wanting to connect to the bank via API, for both bank reporting and sending of payments."

While some corporates are choosing APIs as an alternative to traditional host-to-host connectivity or SWIFT, others are using them in addition to existing channels. "With APIs, corporates no longer have to rely on information pushed from the bank. They can ping across an API call and pull the information they need, on demand. It's a different mindset and one that I believe will become more prevalent in 2022 – especially among corporates planning to upgrade their TMS or ERP system as that's an obvious catalyst for reviewing connectivity options."

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Real-time treasury ramps up

Against the backdrop of growing e-commerce, instant payments are also gaining traction – as is the wider theme of real-time treasury. Cunningham believes this will only accelerate in 2022. "We're edging closer to a tipping point around real-time payments. More and more markets are embracing instant payments and settlement and it's only a matter of time before corporates use them, whether directly through a proactive choice, or indirectly through consumer or B2B customer behaviours."

Treasurers are also starting to more seriously examine value-added services around instant payments, such as request to pay and other alternative payment and collection methods, like direct APIs, as a means to reduce transaction costs and increase efficiency. With these real-time digital payment methodologies comes a wealth of instant data, which can help corporates to work towards the goal of building a real-time treasury.

This data goldmine is not without its challenges, though. "With so much data now flooding into treasury, it can be hard to see the wood for the trees," admits Cunningham. "Data is only useful if you can make it actionable. With this in mind, we expect to see a few shifts in treasury toolkits and skill sets in 2022," he says.

"Data science is becoming a desirable skill for treasury recruits. Some large treasury teams even have their own data scientist allocated by head office. But if up-and-coming treasury practitioners can offer data science knowledge, they will undoubtedly have a head start over others. Existing team members can also look to upskill and we've already seen several seasoned professionals taking course of RPA, APIs, data analytics, and so on – this will likely gather momentum in 2022."

With the right skills in place, the level of smart technology in the department will likely increase too. "There are evergreen challenges such as cash forecasting that can benefit enormously from the application of technologies such as AI. We are starting to see treasurers work directly with fintechs to embed AI-driven forecasting into their existing set-up – with tangible results. And there's certainly more to come there."

In fact, Cunningham goes so far as to describe intelligent forecasting as "one of the biggest areas of opportunity and promise around data in treasury. This is especially true when it is viewed against the backdrop of instant payments and real-time treasury. Daily, weekly and monthly forecasts are arguably becoming old hat, and real-time cash positions are much more critical – although forecasts still have a strategic purpose, of course."

Further bumps in the road

Despite all of the opportunities ahead, the spectre of inflation and interest rate risk cannot be ignored. "Covid is still here and we must therefore expect further central bank action in terms of quantitative easing. Inflation is a definite concern and the signals in the market point to interest rate rises in 2022, although there is some divergence across jurisdictions," explains Cunningham.

For treasurers, this economic picture will require a re-evaluation of the underlying operating model, together with a close look at the organisation's currency mix, he says. "It will also be critical to assess where the company is long [or short] in cash, as well as where natural hedges exist and how those can be optimised in the shifting interest rate environment, through pooling structures, sophisticated hedging solutions or swapping out currencies, for example."

With all of these different forces to contend with, treasurers might rightly be entering into 2022 with a sense of trepidation. But Cunningham remains optimistic. "On reflection, 2021 has been a year of growth and progress – with many successful M&A deals in the corporate sector, GDP growth, and excellent levels of innovation from banks, fintechs, and corporates alike. We're extremely proud of how our clients have coped with unexpected twists and turns and we're helping them to make the most of the momentum behind digital transformation and business model evolution.

"For 2022, I expect to see this positive drive continue. Thanks to their hard work over the last 12 months, treasurers are now more ready than ever to cope with curve balls. When [not if] one comes, I am confident that they will either bat it away, or they will weigh the benefits of following a different path – and adapt accordingly."