Oracle Financial Services

The Evolving Role of Banks in Corporate Liquidity Management

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INTRODUCTION

Increasing levels of operational complexities in the corporate world and challenging market conditions have triggered a radical reshaping of the treasury landscape and the way corporates interact with banks. Of the many challenges that treasurers face, managing and controlling liquidity has emerged a top priority.

Liquidity management may hold the key to a company's survival in today's heavily regulated, globalized economy. This is especially true in a highly competitive environment where shareholders want to see healthy utilizations and balanced exposures in corporate books. Banks need to support their corporate customers to manage liquidity effectively and enable them to derive maximum benefits at minimal cost.

For companies both large and small with global operations, managing liquidity has its own challenges, for example the lack of knowledge of the cash in hand (cross border and/or cross currency), the inability to mobilize and manage cash to take corrective action. If banks are to be more relevant and benefit from digitalization, they need to invest in new and innovative capabilities that can help them provide efficient liquidity management services.

THE GROWING IMPORTANCE OF LIQUIDITY MANAGEMENT

Digital technology is rapidly expanding its influence on the corporate landscape and the way enterprises function globally. Enterprises are developing newer business strategies that involve the need for efficient utilization of their global liquidity.

Regulatory changes, such as Basel III, have significantly impacted some long standing liquidity management techniques and substantially affected the way banks handle liquidity. With an environment of low or negative interest rates in several geographies, managing liquidity across markets, currencies and business units has become complex and increasingly challenging. These new challenges have triggered a radical reshaping of the corporate treasury landscape and the way corporate interacts with banks.

While liquidity management has always been a core function of corporate treasurers, it has gained more attention in the last few years in the banking ecosystem. The analysis of the recent financial crises has revealed that despite adequate levels of capital, companies faced financial struggles due to improper liquidity management. The end of the crisis came with higher regulation, leading to higher cost of liquidity and higher volatility.

Business Priorities of Corporate Treasurers

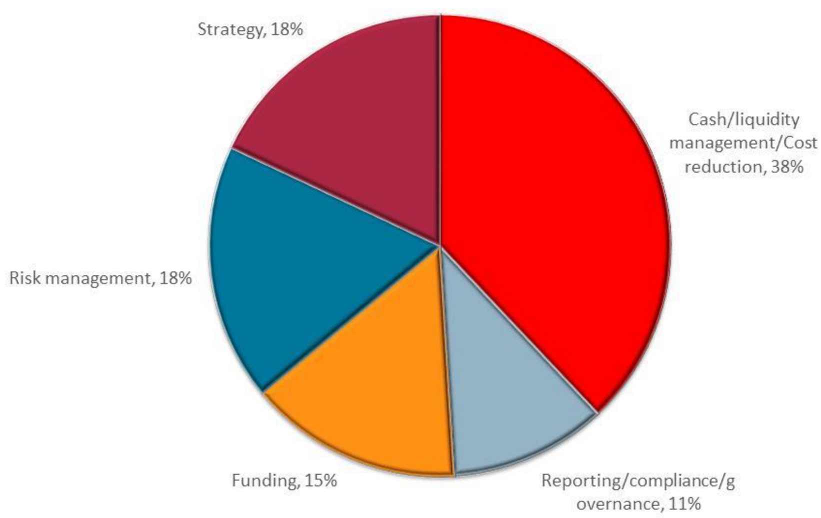

Figure 1: Corporate Treasurers' Priorities – Celent Research

Liquidity management is perhaps the key to a company's survival in today's highly regulated and globalized economy, especially since it is becoming increasingly difficult to secure external funding. Global corporations are beginning to take note of liquidity management as one of the most important areas of focus for treasuries around the world. By any litmus test, it's clear that liquidity management is top-of-mind for companies of all shapes and sizes.

BANKS NEED TO PLAY A CRITICAL ROLE IN CORPORATE LIQUIDITY MANAGEMENT

Banks need to support their corporate customers to manage liquidity effectively and enable them to derive maximum benefits at minimal cost. For companies both large and small with global operations, managing liquidity has its own challenges like the inability to know cash in hand (cross border and/or cross currency), inability to mobilize and manage cash to take corrective actions.

For banks to remain a valued partner to their corporate customers they must learn to navigate today's reshaped liquidity management landscape. Corporate customers are beginning to realize that cash and liquidity management are no longer a necessary evil but competitive arsenal. Research suggests that companies are dissatisfied with their cash visibility and cash centralization. To help corporations manage cash effectively and enable better mobility of cash it takes a depth of capability.

Role of Banks in Corporate Liquidity Management

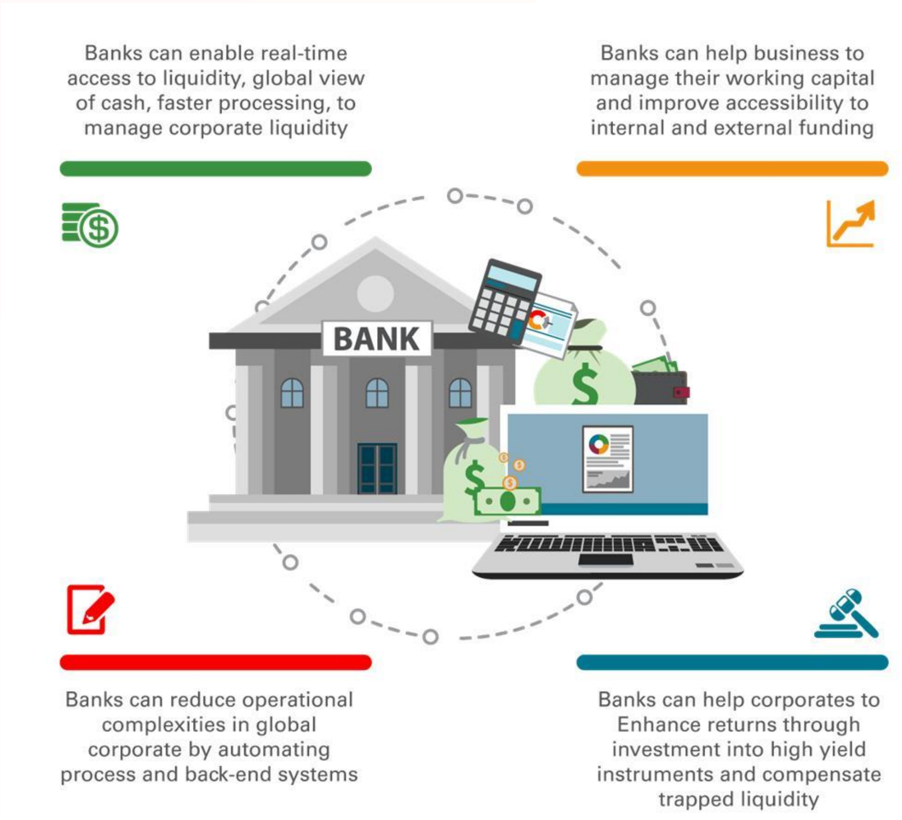

Figure 2: Role of Banks in Corporate Liquidity Management - Oracle

To be more relevant and benefit from digitalization, banks need to invest in new and innovative capabilities to support their corporate customers with efficient liquidity management services. An effective liquidity management solution should cater to, not just the present needs of the corporate treasury, but also any future needs. Systems should be able to predict what the cash positions will be at future dates. This will help eliminate the element of surprise for corporations, future-proofing them and allowing in-time course correction.

As liquidity management continues to gain prominence, banks should provide faster, integrated and more innovative offerings in order to manage the ever-increasing complexities of global corporates. Banks should also offer self-service capabilities that will enable corporates to configure, monitor and manage their liquidity structure. This will help banks to drive customer centricity and offer great experience. Banks can enhance their existing liquidity management system or replace it with more specialized and advanced solutions. Either way, the banking solution will have to play a dominant role if corporates are to make the right decisions with real-time access to relevant liquidity information.

To help businesses remain competitive and grow steadily despite all odds, Banks should offer the right solution which will enable access to liquidity, significantly reduce costs, optimize investments and improve the ability to control and manage Liquidity.

COMPONENTS OF EFFICIENT LIQUIDITY MANAGEMENT SOLUTIONS

How can banks help corporates take the appropriate next steps in effecting change geared toward globalization, automation, tighter regulatory environment and more diversified banking relationships?

It begins with the decision to opt for a global solution to manage liquidity. The solution should provide an enterprise-wide framework that is not only malleable enough to adjust to market conditions, but also stable enough to act as a central hub for all liquidity management activity. Corporates will expect banks to offer solutions that improve the efficiency of their cash management and working capital management across the global enterprise. Banks should look to offer the below mentioned key components to enable corporates to manage cash and liquidity more efficiently.

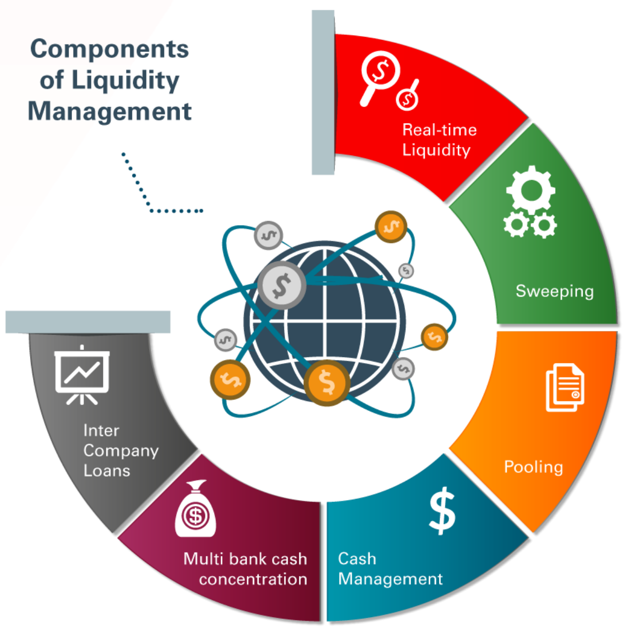

Figure 3: Key Components of Liquidity Management - Oracle

Banks should provide liquidity solutions that will provide customers with an overview of their global multicurrency cash and investments. The solution should allow for information to be extracted in multiple ways while delivering more granular and time-sensitive information. The solution must have the capability to provide liquidity positions in all of the currencies in which the bank conducts business and capture all sources of liquidity risk. The solution should also be tightly integrated with other systems like receivable and payable solutions, sales systems and analytical tools for advanced insights and faster decision making.

Real-time Liquidity

With instant domestic payments and faster cross-border payments becoming more prevalent, treasurers have increasing access to “real-time” functions. The payments space has been the first to upgrade to Real-time, with instant domestic payment schemes joined by SWIFT’s global payments initiative (gpi), accelerating payments across the globe. Managing liquidity in real-time has also become critical for corporates. For instance, when a corporate account does not have sufficient balance to honor an incoming debit, the said account should be funded by other corporate accounts in Real-time based on certain pre-defined rules provided the contribution accounts themselves have sufficient balance.

WHY IS REAL-TIME LIQUIDITY IMPORTANT FOR CORPORATES

There is great potential to be unlocked in real-time capacity applied to liquidity management. Real-Time Liquidity is a timely and efficient solution for issues arising from inbound and outbound payments. For example, if a client makes a payment in the morning and does not have enough funds to cover it in a specific account, the bank can still honor payment if it is able to accumulate the funds between the group structures.

WHAT ROLE BANKS CAN PLAY

To remain relevant and derive greater benefits from changing dynamics of corporate payments, banks should invest in new and innovative capabilities to support the growing need for real-time and cross-border payments. Banks can offer Real-Time Liquidity as a value added service to select corporates enabling them to honor payments on a real time basis. This will further help bank create a base on which further intraday real time liquidity measures can be implemented.

Sweeping

Sweeping enables automated funds transfer from various sub accounts into a single master account for consolidation of liquidity. The amounts in the sub accounts can be transferred to the master account as per business rules setup and these funds can either be invested to earn higher rate of interest or they can be used to fund sub accounts which are in debit.

WHY IS SWEEPING IMPORTANT FOR CORPORATES

Cash Concentration is an important requirement for corporates who have lines of business across the globe and regularly need to move funds across borders involving multiple currencies and several accounts. Concentration of cash scattered across several locations and accounts into a single operating account with real time visibility with minimum costs is of great relevance to companies.

WHAT ROLE BANKS CAN PLAY

Banks can help customers save heavy interest costs, optimize the utilization of cash and reduce the need for external borrowing by offering an efficient sweeping module that offers multiple sweeping options like zero balancing sweeps, Target based sweeping and trigger based sweeping. In addition to the automated movement of funds based on predefined rules and parameters, monitoring and control can be made easier by offering a robust reporting module supported with operational dashboards, easy reconciliation techniques and seamless user interface.

Pooling

Pooling otherwise known as Notional pooling means virtually netting balances across a group via central treasury platforms in dedicated locations. It allows for calculating interest on the combined credit and debit balances of the accounts of all those companies which are part of the pooling arrangement, without physically transferring any funds between their accounts.

WHY IS POOLING IMPORTANT FOR CORPORATES

Notional pooling is subject to varying regulations. It is beneficial to corporates which operate in a decentralized set up. Subsidiaries benefit from a centralized liquidity position, while still retaining autonomy in their daily cash management. This flexible arrangement may offer increased interest income, and reduced interest expense, to the group and its subsidiaries. Also as physical movement of cash is not required, there are no transaction costs involved.

WHAT ROLE BANKS CAN PLAY

An efficient pooling module will offer the flexibility of various pooling models which calculate interest at account level or pool level and allocate or reallocate the same based on various distribution methods like fair share, reverse fair share and centrally. For countries where pooling is restricted due to regulations, offerings like interest enhancement or interest optimization can be offered. Hybrid models where pooling can be combined with global cash concentration structures for more complex liquidity requirements can be offered.

Notionally Pooled Balances may be further deployed as part of an overnight investment option like time deposits or money market mutual funds with the option to redeem the earnings at various frequencies. Pool positions and visibility of funds is easy to track due to availability of batch and online reports which can be accessed via portal or delivered via pre-defined channels.

Cash Management

Cash management is the most efficient mechanism for collection, disbursement, and investment of cash in an organization while maintaining the company's liquidity.

WHY IS CASH MANAGEMENT IMPORTANT FOR CORPORATES

Effective cash management enables corporates to manage their payables & receivables with desired liquidity levels to manage their business effectively. Good cash management increases the efficiency of operations and reduces overall cost of doing business

WHAT ROLE BANKS CAN PLAY

With changing technology, banks are now in a position to offer sophisticated cash management platform to its corporates that goes beyond traditional cash management offerings of payable/receivable management. The modern cash management platform helps bank deliver value to corporates by enabling them to connect digitally with their suppliers/dealers and help automate invoicing, payments and associated reconciliation. As a part of these offerings, banks are increasingly providing a multi-currency virtual account management platform which can help corporates manage their payable/receivables with automated reconciliation. Banks are also enabling corporates to manage Liquidity using traditional techniques like Sweep & Notional Pooling on Virtual Account structures. These Virtual Account Management platforms typically have a self-service proposition with a variety of dashboards and reports to help corporates manage their requirements.

These new generation platforms offer a sophisticated User Interface with dashboards and have the ability to connect to plethora of systems to gather information and accurately predict the cash flow positions of corporates in near real time.

As technologies like Blockchain and Machine learning become mainstream, banks are looking at cash management platforms to help them use the wealth of information they hold and evolve from transaction executions to trusted advisors for corporates.

Multi Bank Cash Concentration (MBCC)

It is an automated means of Concentrating Balances held at third party banks of the corporate.

WHY IS MULTI BANK CASH CONCENTRATION IMPORTANT FOR CORPORATES

Corporates maintain several regional banking relationships for localized services which help them transact efficiently and with low costs. However as part of the bigger cash concentration requirement, there is a need to mobilize funds from these third party bank accounts to the master account which is held with the primary bank. Hence there is a need for corporates to avail the MBCC facility.

WHAT ROLE BANKS CAN PLAY

Banks which are in a position to offer MBCC are always at a distinct advantage as they are often designated by Corporates as their primary bank or lead bank for carrying out business. Banks offering MBCC most likely end up garnering the major portion of the client's business and also consolidate funds from other banks as part of Zero Balancing Sweep. In addition, they also cater to a corporate's need of maintaining the regional banking relationships for truly localized services and optimizing the yield from liquidity consolidation.

Banks can help corporates by extending the capabilities of the sweep module to include MBCC which would address:

- Automated concentration of funds across third party bank accounts in different regions and different currencies
- Concentration using payment networks like SWIFT
- Flexibility of addition and modification of accounts and multiple frequency options like daily/weekly/monthly
- Currency conversion for cross currency MBCC sweeps.
- Robust reporting

Intercompany Loans

Intercompany loans are loans made from one business unit of a company to another, primarily to shift cash to a business unit that would otherwise experience a cash shortfall or into a business unit (usually corporate) where the funds are aggregated for investment purposes.

WHY ARE INTERCOMPANY LOANS IMPORTANT FOR CORPORATES

Corporate customers get better control and visibility over cash balances lent to Treasury or group entities. These solutions can help in adherence to approved cross-border lending quotas/ thin capitalization ratios and avoid unfavorable tax consequences

WHAT ROLE BANKS CAN PLAY

With intercompany lending solutions, banks can help corporates manage the overall exposure to group entities and control the level of lending and borrowing undertaken between group entities. With automated lending limits, corporates can have visibility into exposure between accounts or even across structures.

Based on market needs, banks can offer different types of loans like perpetual loans, short term loans, loans with no stated repayment date, fixed term loans etc. A solution which tracks interest payable /receivable and provides the flexibility to approve/amend the terms of payments including foreclosure/waive off would be of immense value to banks in handling nuances of intercompany loans. Similarly the facility to record interest accruals as well as a record of withholding tax on interest payments will help them cover the tax angle. As a valued partner for corporates, banks can also provide a self-service portal which will give corporates a global view of lending across subsidiaries.

ORACLE’S PROPOSITION FOR LIQUIDITY MANAGEMENT

Oracle’s Liquidity Management solution enables banks to run a single centralized standalone liquidity management system based on contemporary technology with the ability to support comprehensive liquidity management techniques. The solution supports techniques such as pooling, sweeping, real-time liquidity, interest optimization and additional avenues for higher yield investments like money markets and term deposits with flexibility to cater to country regulatory restrictions.

ENABLE REAL-TIME CAPABILITIES

Using Oracle’s Liquidity Management solution banks can provide real-time, accurate and consolidated information to facilitate efficient / effective liquidity management for corporate customers. Oracle helps banks enable complete visibility into cash positions for their corporate customers. This results in better utilization of available funds and reduced interest costs through short-term bank borrowings.

BUSINESSES CAN REMAIN COMPETITIVE

Global Enterprises are developing cautiously optimistic business strategies that involve the need for efficient utilization of their global liquidity. Oracle’s Liquidity Management Solution supports advanced techniques such as interest optimization and additional avenues for higher yield investments with flexibility to cater to country regulatory restrictions. These capabilities reduce organizational and structural inefficiencies that are detrimental to liquidity management.

SUPPORT MULTI-COUNTRY, MULTI-BRANCH, MULTI-CURRENCY LIQUIDITY MANAGEMENT

Oracle’s Liquidity Management Solution supports a multi-country, multi-branch, multi-currency liquidity structure. This enables the system to keep track of balances in accounts, calculate interest on the accounts as well as track the history of the sweep/pool structure. The solution helps in optimizing liquidity both domestically and across currencies and borders. The solution supports cross-border techniques like follow-the-sun and against-the-sun sweeping to centralize cash on a global basis.

OFFER COMPREHENSIVE SELF-SERVICE CAPABILITITES FOR SEAMLESS EXPERIENCE

Oracle Banking Digital Experience has been designed to provide an intuitive experience while accessing a banking channel. The solution helps the bank and its corporate customers optimize their global cash position with its extensive self-service capabilities for liquidity management. Corporate customers gets the holistic view of their liquidity structures and they can create new structures; pause/resume structures; have a view of last 5 sweeps; see positions by region. This can help corporates get a real-time understanding of liquidity position across the globe. With Oracle solutions, banks can give corporates a holistic omni-channel digital banking experience.

LEVERAGE PRE-BUILT APIS FOR EFFICIENT LIQUIDITY MANAGEMENT

Oracle Banking Liquidity Management offers pre-built RESTFul APIs enabling banks to provide user experiences specific to customer needs. The solutions will not only be efficient, but will also drive emphasis on user experience and present information in a convenient and actionable manner.

WAY FORWARD

Oracle will continue to invest in newer techniques like tax efficient sweeps, investment sweeps, drain the pool sweeps etc to enable banks to offer a comprehensive solution. Oracle will also offer functionalities that will provide support for benefit modelling enabling banks/corporates to select the best way to pool their resources to enable maximum liquidity benefit.

Oracle is looking at emerging trends to present Blockchain use cases in liquidity & cash management that enables intra-day liquidity monitoring & real time transaction reconciliation. Blockchain will help institutions reimagine and restructure their operating models and processes.

There is a move across the industry towards reducing capital expenditure and taking on more operating expenses, leading to a proliferation of cloud-based, SaaS solutions, in all areas including liquidity management. To help minimize cost and be more efficient, Oracle is exploring low-cost deployment models – like cloud in the cash and liquidity management space.

Oracles' focus on emerging technologies like Machine Learning and Artificial Intelligence are differentiators that make it a leader in the banking solutions industry. With the advent of machine learning, banks having actual transactional data will be able to draw far more realistic inferences and make the process far more scientific and accurate. This can create tangible value by reducing operational cost and automating the decision making process. Oracle believes that big data analytics can create opportunities for banks to automate cash forecasting processes completely and replace the current manual and error prone process with Artificial Intelligence platforms.

ORACLE CORPORATION

Worldwide Headquarters
500 Oracle Parkway, Redwood Shores, CA 94065 USA

Worldwide Inquiries
TELE + 1.650.506.7000 + 1.800.ORACLE1
FAX + 1.650.506.7200
oracle.com

CONNECT WITH US

Call +1.800.ORACLE1 or visit oracle.com. Outside North America, find your local office at oracle.com/contact.

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Integrated Cloud Applications & Platform Services

White Paper The Evolving Role of Banks in Corporate Liquidity Management
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