Post-Crisis Emerging Role of the Treasurer

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Abstract

The severe credit crisis began in 2007 in the US and expanded globally in 2008-09. It changed the basics of cash and liquidity management. Pre-crisis we had a situation where access to capital was not a direct bottle-neck even at fairly aggressive leveraged balance sheets and sub investment grade rating. During the crisis and in its aftermath corporate treasuries realized they needed to develop more reliable alternatives for funding and raising liquidity. A trend to deleverage, which many times was imposed by financial institutions, meant corporates started to build up cash cushions, in the form of reserve capital for situations of financial stress. This trend was many times also driven by the company’s stakeholders, including shareholders, who requested lower levels of debt and/or increased cash balances. The normalization of the financial markets after the crisis has thus led to improved capital structures and reduced reliance on committed facilities. In response to above mentioned situation, it appears that collaborative financing tools, such as supply chain finance (SCF), are generating significant interest as a way of freeing up working capital.

On the government side, the process for coping with the crisis by countries across the globe has been manifest in four basic phases. The first has been intervention to contain the contagion and restore confidence in the system. This has required extraordinary measures both in scope, cost, and extent of government reach. The second has been coping with the secondary effects of the crisis, particularly the global recession and flight of capital from countries in emerging markets and elsewhere that have been affected by the crisis. The third phase of this process is to make changes in the financial system to reduce risk and prevent future crises. In order to give these proposals political backing, world leaders have called for international meetings to address changes in policy, regulations, oversight, and enforcement. On September 24-25, 2009, heads of the G-20 nations met in Pittsburgh to address the global financial crisis. The fourth phase of the process is dealing
with political, social, and security effects of the financial turmoil. One such effect is the strengthened role of China in financial markets.

**Keywords:** Corporate treasury management, credit crisis 2007-2009, supply chain finance, working capital management, Basel III.

1. Introduction

Cash visibility and working capital management are a priority at a time when credit is no longer readily available – smart choices in both areas are necessary to weather the financial crisis. The current credit crisis has put corporate banking relationships to the test in several ways. Credit is less readily available, and when it is, the cost has increased while terms and conditions are less favorable for the corporate client. Moreover, corporate treasurers have discovered that the collapse of one of their relationship banks is less hypothetical than previously thought. With credit becoming more expensive, the corporate treasurers are looking inside their companies for cheaper cash. Upstreaming even short term cash pockets requires actual visibility on bank accounts. But also working capital management is in the spotlight; shortening the cash conversion cycle even by only one day unlocks almost USD 2,800 in cash for every USD 1 million in sales; it means 0.28% of the sales (= 1 day/360 days).

Supply chain finance (SCF), especially reverse factoring and dynamic discounting, are on the rise. Starting in the 1990s preliminary in the car industry, this form of financing has gained increasing popularity in other industries as well. The first model of SCF combined domestic trade finance with supply chain management through an innovative invoice financing arrangement known as “reverse factoring,” a three-way agreement by which the bank (or “factor”) purchases the receivables of the supplier with legal recourse to the buyer. In this earliest model introduced approximately 20 years ago, reverse factoring was purely a domestic service offered within select industries, especially the automotive sector. Then the last model integrates the pieces of the financial supply chain from end to end, fully automating the buyers’ procure-to-pay and suppliers’ order-to-cash cycles. This new level of integration supports event-triggered financial services along the physical supply chain, such as purchase order tracking, invoice matching services, e-invoicing, open account payments, import/export financing, and reverse factoring. In addition it affords a full transparency into each transaction. This transparency is necessary to allow liquidity providers (whether banks or non-bank finance companies) to apply dynamic pricing in purchasing outstanding invoices. The integration of procurement, invoicing and financing within one single platform represents the full convergence of cash management and trade finance.

The paper is structured as follows: First, in chapter 2, the crisis and its impacts are discussed. Then, in the next chapter 3, reduced opportunities for corporations to invest and borrow are analyzed. Then, in the later chapter 4, working capital as a viable source of funding and investment for some firms is reviewed. In the last chapters, emerging working capital options and its optimization are mentioned.

2. Credit Crisis 2007-2009 and its Impact

Das (2010) states that the sub-prime crisis that began in the US housing market in 2007 snowballed into a global financial and economic crisis. The global financial landscape changed with failure of several large financial institutions and subsequent government intervention to prevent imminent collapse. The lack of trust and uncertainty led to disruptions in the short-term funding markets, and a fall in equity prices. The contagion of the crisis transmitted from the financial sector to the real sector through demand slump, production plunge, unemployment rise, and credit seize. Most worryingly, world trade—the main channel of crisis transmission—fell sharply, GDP growth rates fell for both advanced and developing economies, leading to contraction in global GDP for the first time since World War II. The crisis had prompted countries around the world to come up with aggressive and
unconventional monetary and fiscal measures. There were several instances of coordinated policy actions by the central banks. This averted the escalation of the crisis and prevented a meltdown of financial system.

Mah-Hui (2008) seeks to explain the causes and consequences of the U.S. subprime mortgage crisis, and how this has led to a generalized credit crunch in other financial sectors that ultimately affects the real economy. He postulates that despite the recent financial innovations, the financial strategies - leveraging and funding mismatch - that led to the present crisis are similar to those found in the U.S. savings and loans debacle of the late 80s, and in the Asian financial crisis of the late 90s. However, these strategies contain new innovations that have heightened, not reduced, systemic risks and financial instability. They are as the title implies: “old wine in new bottle”.

Going beyond these financial practices, the underlying structural causes of the crisis are located in the loose monetary policies of central banks, deregulation, and excess liquidity in financial markets that are a consequence of the kind of economic growth that produces various imbalances - trade imbalance, financial sector imbalance, and wealth and income imbalance. The consequences on risks, moral hazards, and rolling bubbles are also discussed.

Campello et al. (2010) survey 1,050 Chief Financial Officers (CFOs) in the U.S., Europe, and Asia to directly assess whether their firms are credit constrained during the global financial crisis of 2008. They study whether corporate spending plans differ conditional on this survey-based measure of financial constraint. Their evidence indicates that constrained firms planned deeper cuts in technical spending, employment, and capital spending. Constrained firms also burned through more cash, drew more heavily on lines of credit for fear that banks would restrict access in the future, and sold more assets to fund their operations.

They also find that the inability to borrow externally caused many firms to bypass attractive investment opportunities, with 86% of constrained United States based CFOs saying their investment in attractive projects was restricted during the credit crisis of 2008. More than half of the respondents said they canceled or postponed their planned investments. They mention that their results also hold in Europe and Asia, and in many cases are stronger in those economies.

Grigore and Mitroi (2009) find that SMEs are now considered the most sensitive sector and worst affected by the economic climate. The financial crisis adversely affects most of the SMEs, reducing the development rate and increasing the number of bankruptcies. Startups in particular are most vulnerable and lacking the resources to survive the downturn. SMEs need to spend as much time as they can focusing on boosting their returns and reducing their overheads. Entrepreneurs are affected in large, and crisis has curtailed their access to the credit. Entrepreneurs who are being upset by this credit crunch should play a vital role in the future economic landscape.

Montoro and Rojas-Suarez (2012) state that the financial systems in emerging market economies (EMEs) during the 2008-09 global financial crisis performed much better than in previous crisis episodes, albeit with significant differences across regions. For example, real credit growth in Asia and Latin America was less affected than in Central and Eastern Europe. Their paper identifies the factors at both the country and the bank levels that contributed to the behavior of real credit growth in Latin America during the global financial crisis. The resilience of real credit during the crisis was highly related to policies, measures, and reforms implemented in the pre-crisis period. In particular, they find that the best explanatory variables were those that gauged the economy's capacity to withstand an external financial shock. Key variables were balance sheet measures such as the economy's overall currency mismatches, and external debt ratios (measuring either total debt or short-term debt).

The quality of pre-crisis credit growth mattered as much as its rate of expansion. Credit expansions that preserved healthy balance sheet measures (the "quality" dimension) proved to be more sustainable. Variables signaling the capacity to set countercyclical monetary and fiscal policies during the crisis were also important determinants.

Moreover, financial soundness characteristics of Latin American banks, such as capitalization, liquidity, and bank efficiency, also played a role in explaining the dynamics of real credit during the
crisis. They also find that foreign banks and banks which had expanded credit growth more before the crisis were also those that cut credit most.

The methodology used in their paper includes the construction of indicators of resilience of real credit growth to adverse external shocks in a large number of emerging markets, not just in Latin America. They mention that as additional data become available, these indicators could be part of a set of analytical tools to assess how emerging market economies are preparing themselves to cope with the adverse effects of global financial turbulence on real credit growth. Njoroge (2009) states that the global financial crisis has led to economic recession in different countries around the world. The purpose of his study was to examine how the global financial crisis is affecting corporate social responsibilities of multinational enterprises in Kenya. For example, to identify the effects of the global financial crisis in regard to downsizing, funding of social projects, and labor standards. Multinational companies have been compelled by circumstances to search for ways of curbing spending including negating on their corporate social responsibilities. The study carried out a two-pronged approach to identify the effects of the financial crisis. The first approach involved a telephone interview survey, while the second approach involved analyzing data from Covalence Company. The results indicated occurrence of downsizing attributed to the global financial crisis. Results also indicated an adverse effect on funding of social projects and minimal effect on compliance to labor standards.

Nanto (2009) mentions that the world is near the bottom of a global recession, that is causing widespread business contraction, increases in unemployment, and shrinking government revenues. Although recent data indicate the large industrialized economies may have reached bottom and are beginning to recover, for the most part, unemployment is still rising. Numerous small banks and households still face huge problems in restoring their balance sheets, and unemployment has combined with sub-prime loans to keep home foreclosures at a high rate. Nearly all industrialized countries and many emerging and developing nations have announced economic stimulus and/or financial sector rescue packages, such as the American Recovery and Reinvestment Act of 2009 (P.L. 111-5). Several countries have resorted to borrowing from the International Monetary Fund as a last resort. The crisis has exposed fundamental weaknesses in financial systems worldwide, demonstrated how interconnected and interdependent economies are today, and has posed vexing policy dilemmas.

The process for coping with the crisis by countries across the globe has been manifest in four basic phases. The first has been intervention to contain the contagion and restore confidence in the system. This has required extraordinary measures both in scope, cost, and extent of government reach. The second has been coping with the secondary effects of the crisis, particularly the global recession and flight of capital from countries in emerging markets and elsewhere that have been affected by the crisis. The third phase of this process is to make changes in the financial system to reduce risk and prevent future crises. In order to give these proposals political backing, world leaders have called for international meetings to address changes in policy, regulations, oversight, and enforcement. On September 24-25, 2009, heads of the G-20 nations met in Pittsburgh to address the global financial crisis. The fourth phase of the process is dealing with political, social, and security effects of the financial turmoil. One such effect is the strengthened role of China in financial markets.

The role for Congress in this financial crisis is multifaceted. While the recent focus has been on combating the recession, the ultimate issue perhaps is how to ensure the smooth and efficient functioning of financial markets to promote the general well-being of the country while protecting taxpayer interests and facilitating business operations without creating a moral hazard. In addition to preventing future crises through legislative, oversight, and domestic regulatory functions, On June 17, 2009, the Department of the Treasury presented the Obama Administration proposal for financial regulatory reform. The proposal focuses on five areas and includes establishing the Federal Reserve as a systemic risk regulator, creating a Council of Regulators, regulating all financial derivatives, creating a Consumer Financial Protection Agency, improving coordination and oversight of international financial markets, and other provisions. Treasury also has submitted to Congress proposed legislation to implement the reforms. The reform agenda now has moved to Congress. Legislation in Congress
addresses many of the issues in the Treasury plan but also may focus on other financial issues. Congress also plays a role in measures to reform and recapitalize the International Monetary Fund, the World Bank, and regional development banks.

**Impact on Cash and Liquidity Management**

The severe credit crisis began in 2007 in the US and expanded globally in 2008-09. It changed the basics of cash and liquidity management. Pre-crisis we had a situation where access to capital was not a direct bottle-neck even at fairly aggressive leveraged balance sheets and sub investment grade rating. During the crisis and in its aftermath corporate treasuries realized they needed to develop more reliable alternatives for funding and raising liquidity. A trend to deleverage, which many times was imposed by financial institutions, meant corporates started to build up cash cushions, in the form of reserve capital for situations of financial stress. This trend was many times also driven by the company’s stakeholders, including shareholders, who requested lower levels of debt and/or increased cash balances. The normalization of the financial markets after the crisis has thus led to improved capital structures and reduced reliance on committed facilities. Besides having higher levels of cash on the balance sheet, corporates also have diversified their channels of funding using more varied debt instruments and spreading into more funding markets (e.g., such as by issuing debt in multiple regions). Corporate treasury and investor relations have in many cases started to cooperate and performing joint road shows and communication directed not only to investors owning company shares but also those holding company debt. This shift in liquidity management and funding strategies is a systemic shift and there are no signs that the corporate sector will return to the relatively lax attitude towards capital availability as they had prior to the credit crisis.

The size of the cash cushions vary across companies dependent on the conditions under which they do business. Here are some factors that reduce the level of cash a firm might hold:

2. Degree of balance sheet leverage, as high levels of leverage require the use of cash to repay debt.
3. Precision of cash forecasting accuracy.
4. Low levels of business risk – for example firms with high levels of operating risk may unexpectedly require sudden inflows of cash for major product and market investments. This is typically the case for the technological and telecom markets for instance.
5. Trust in commitment for the corporate’s banking relations.
7. Low volatility of cash flows (e.g., large pharmaceutical firms, which are dependent on unknown returns from heavy R&D spend will often hold multi-billion dollar cash balances as a hedge against cash flow risk).

One consequence of creating considerable cash cushions is that cash requires investment management of the resultant interest rate and credit risks within the cash portfolio. Another major concern is the cost of carry, as firms may face a negative return on cash when debt is held at a higher interest rate than the cash cushion generates. This cost of carry is regarded as an insurance premium but in situations of high-risk aptitude in the financial markets it may create a motivation to take higher risks in anticipation of higher returns, increasing the overall risk position of the company.

For the European Union based companies, the combination of Single Euro Payments Area (SEPA) and the EC Payment Services Directive enables them to streamline their cash and liquidity management across Europe and benefit from legal harmonization, including simplifying cash management structures and reducing the number of banking relationships to a few trusted partner banks. Another trend relating to both counterparty and liquidity risk is the increased use of escrow. While escrow arrangements were historically used for activities such as mergers and acquisitions, for holding cash pending settlement, escrow is now in use for trade and project finance purposes.
3. Reduced Opportunities for Corporations to Borrow and Invest

Ivashina and Scharfstein (2010) state, that new loans to large borrowers fell by 47% during the peak period of the financial crisis (fourth quarter of 2008) relative to the prior quarter, and by 79% relative to the peak of the credit boom (second quarter of 2007). New lending for real investment (such as working capital and capital expenditures) fell by only 14% in the last quarter of 2008, but contracted nearly as much as new lending for restructuring (LBOs\(^1\), M&As\(^2\), share repurchases) relative to the peak of the credit boom. After the failure of Lehman Brothers in September 2008, there was a run by short-term bank creditors, making it difficult for banks to roll over their short term debt. They find that there was a simultaneous run by borrowers who drew down their credit lines, leading to a spike in commercial and industrial loans reported on bank balance sheets. They examine whether these two stresses on bank liquidity led them to cut lending. In particular, they show that banks cut their lending less if they had better access to deposit financing and thus, they were not as reliant on short-term debt. They also show that banks that were more vulnerable to credit-line drawdowns because they co-syndicated more of their credit lines with Lehman Brothers reduced their lending to a greater extent.

Härle et.al (2010) report that Basel III will have significant impact on the European banking sector. As the rules are written today and based on Q2 2010 balance sheets, by 2019 the industry will need about €1.1 trillion of additional Tier 1 capital, €1.3 trillion of short-term liquidity, and about €2.3 trillion of long-term funding, absent any mitigating actions. The impact on the smaller US banking sector will be similar, though the drivers of impact vary. They estimate that the Tier 1 capital shortfall at $870 billion (€600 billion), the gap in short-term liquidity at $800 billion (€570 billion), and the gap in long-term funding at $3.2 trillion (€2.2 trillion).

The capital need is equivalent to almost 60 percent of all European and US Tier 1 capital outstanding, and the liquidity gap equivalent to roughly 50 percent of all outstanding short-term liquidity. Assuming a 50 percent retained earnings payout ratio and nominal annual balance-sheet growth of 3 percent through 2019, capital requirements in Europe are expected to increase to about €1.2 trillion, short-term liquidity requirements to €1.7 trillion, and long-term funding needs to about €3.4 trillion. They argue that closing these gaps will have a substantial impact on profitability. All other things being equal, Basel III would reduce return on equity (ROE) for the average bank by about 4 percentage points in Europe and about 3 percentage points in the United States. They mention that the retail, corporate, and investment banking segments will be affected in different ways. Retail banks will be affected least, though institutions with very low capital ratios may find them selves under significant pressure. Corporate banks will be affected primarily in specialized lending and trade finance. Investment banks will find several core businesses profoundly affected, particularly trading and securitization businesses. Most banks with substantial capital markets and trading business will likely face significant business-model challenges in the next few years.

Banks are already seeking to manage ROE in the new environment by cutting costs and adjusting prices. They suggest that there are, however, a number of additional interventions, both general and specific to Basel III, that banks should consider such as a) a set of “no regret” interventions to reduce capital and liquidity in efficiency from suboptimal implementation of the new rules, balance-sheet restructuring to improve the quality of capital and reduce capital needs arising from Basel III’s deductions, as well as more effective management of scarce balance-sheet resources, business-model adjustments to create capital- and liquidity-efficient business models, and products, and rethink the scope and even the viability of specific business lines. They estimate that the first two sets of actions could mitigate up to 40 percent of Basel III’s ROE impact, with significant variations for individual banks, depending on their starting position and competitive market dynamics. Overall, it is unlikely that banks will be able to offset Basel III’s impact on profitability.

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\(^1\) Leveraged buyout = acquisition of another company using a significant amount of borrowed money (bonds or loans) to meet the cost of acquisition.

\(^2\) Mergers and Acquisitions.
Rognlie (2011) analyzes why do safe, liquid assets become so expensive in a financial crisis? He states that the demand for “liquidity” and/or “safety” is so interest-inelastic in a financial crisis. ‘It’s not that you have to cut back on your spending on currently-produced goods and services—you have plenty of cash money. But you are unwilling to part with some of your cash money’. He mentions that many assets resemble base money in all these respects, but aren’t quite the same—they can’t be carried around on green pieces of paper or used to satisfy the reserve requirements on checking accounts. He calls these assets cash-like. These assets are T-bills, commercial paper, and repo—plus the money market funds. He further argues that the demand for cash-like assets is so inelastic. He states that for some reason, portfolio substitution away from cash is incredibly slow and weak. Inelastic demand, of course, isn’t sufficient to cause large swings in the premium on cash-like assets. It also needs inelastic supply. He states that corporations, at least in the short run, are unlikely to provide a very elastic supply response to a change in the premium on cash-like assets. He further mentions that that there were very powerful forces keeping the supply of cash-like assets inelastic during the financial crisis.

Foster et.al (2011) state that the stage is set for a clash this year between shareholders and investment bankers over how companies should spend more than $2 trillion of cash sitting on US and European corporate balance sheets. Bankers argue that now is the time in the economic cycle to hunt bargains. Shareholders say that, while some M&A deals could be justified, there should be no spending binge and most of the cash should be paid out in dividends. The authors mention that Bill Miller, chief executive of Legg Mason Capital Management, said: “The economy would be a lot better and investors a lot wealthier if chief executives were to allocate capital to the benefit of owners, instead of hoarding it at a zero percent rate of return on the balance sheet.”

Companies have been conserving cash throughout the two years of the financial crisis amid fears of bank collapses and the capital markets drying up. Surveys suggest that more chief executives want to do deals this year, but bankers say some still lack confidence. The authors mention that Bruce Stout, a senior member of Aberdeen Asset Management’s global team, said that companies have built up their strength enough, and the time had come for shareholders to benefit. He said “There is a danger of companies which are unable to grow their businesses any other way using the cash to buy other companies. Given the poor success rate of corporate takeovers, we would prefer companies return excess cash to shareholders.” A senior banker at an independent mergers and acquisitions adviser said: “The tension between those who want M&A, and those who want capital to be redistributed will play an even more important part this year.” The authors further state that in a broking circular September, 2010, UBS Investment Research warned cash sitting on the books is not generating a return and drags down returns on equity. UBS strategists said cash balances have reached €270bn for European companies, and expect free cash flow of €340bn this year and €400bn in 2012.

US companies had more than $1.9 trillion of cash at the end of September, the most recent date for which global asset manager Alliance Bernstein has figures. The ratio of cash to total assets reached 7.4% during that period, the highest it has been since Alliance Bernstein began collating the figures in 1960.

Polak et.al (2011) discuss the role of the modern corporate treasurer in a multinational company, and its transformation in response to current challenges companies and treasurers face. The most significant incident driving change in the role of the corporate treasurer is the credit crisis that occurred in 2007-2009. The crisis replaced a focus on earnings with a focus on cash and liquidity, and marked the end of easy availability of cash for most corporates and the beginning of a situation in which the financial markets were no longer able to reliably supply corporate demand for financing. The crisis saw the end of a credit expansion initiated in the 1980s by the deregulation of the financial markets. Increased focus on liquidity and financial risk management changed the role of the treasurer dramatically. During the crisis, many sectors of the markets totally ceased to function, e.g. the ability to hedge foreign exchange and interest rate exposures was constrained for certain emerging markets and certain structured securities, such as Auction Rate Securities, became wholly illiquid. These disruptions led to an inability to hedge, manage liquidity or even properly measure certain risks any longer. Embedded risks - e.g., in vendor and customer contracts - also emerged as a critical focus
and corporations were forced to take a broader view of risk in light of weaknesses and risks exposed by the crisis.

They mention that as a result of these changes, treasury is no longer merely a function for cash management, funding, and hedge accounting. Treasury is now a strategic function securing liquidity and understanding the true risk profile of the corporation. The treasurer is now much more involved in the management of the business, and has become a business leader instead of an administrator. This transformation in role has placed a much higher demand on the skill sets of the treasurer, and he or she must command the arts of communication and sales as any business area manager would.

They state that the ideas in their paper optimally apply to multinational companies operating in global environments that present challenges in language barriers and different time zones across the globe. The paper addresses a) The change in the role of the treasurer resulting from the change in financial markets’ functionality and the new restrictions in cash availability and risk hedging introduced during the credit crisis. This includes new strategies for cash and liquidity management. The process of optimal centralization and segregation of operational duties across regional centers, a single global center at the headquarters, and local units. b) Factors to consider when identifying optimal locations for regional centers. c) The role of outsourcing in meeting emerging challenges while optimizing efficiency and organizational structure. While the challenges faced by the largest multinational corporations are complex, pressure on greater efficiency applies to mid-size companies too, and small to mid-size enterprises (e.g., those with less than 1 billion Euro annual turnover) may access additional competencies, and improve efficiency by removing the process out of the company entirely.

Campello et al. (2010) survey 1,050 chief financial officers (CFOs) in the U.S., Europe, and Asia to directly assess whether their firms are credit constrained during the global financial crisis of 2008. They study whether corporate spending plans differ conditional on this survey-based measure of financial constraint. Their evidence indicates that constrained firms planned deeper cuts in tech spending, employment, and capital spending. Constrained firms also burned through more cash, drew more heavily on lines of credit for fear banks would restrict access in the future, and sold more assets to fund their operations. They also find that the inability to borrow externally caused many firms to bypass attractive investment opportunities, with 86% of constrained U.S. CFOs saying their investment in attractive projects was restricted during the credit crisis of 2008. More than half of the respondents said they canceled or postponed their planned investments. They mention that their results also hold in Europe and Asia, and in many cases are stronger in those economies.


Yang (2011) tests firms’ financing behavior, especially the causal relation between trade credit and bank credit around the time of the recent sub-prime financial crises. He finds bank credit and accounts payable/receivable are simultaneously determined, and there is a substitute/complementary effect between bank credit and accounts payable/receivable. Moreover, he tests a cross-sectional response to crisis, and finds that firms with a more vulnerable financial position (i.e., financially constrained firms) are more likely to be negatively affected by crisis and, in turn, are more likely to cut their supply of credit to customers, and increase their use of credit from suppliers.

Seifert (2008) state that financial researchers have developed theories as to why companies offer trade credit. Some of the most prominent reasons on supply side are competitive pressure, better credit information on buyers than banks, and prohibition of direct price discrimination. On demand side, the reasons are transactional pooling when buyers demand trade credit to pool payments and reduce cash balances, control protection when buyers prefer trade rather than bank credit because suppliers are less likely to liquidate, and credit rationing when buyers cannot obtain bank finance and therefore turn to suppliers. He further mentions that in times of financial crisis, firms in US generate more than 15% of their financing from accounts payable. Internationally, these levels can be even higher. Working capital is a significant driver of profitability. In an average company, decreasing working capital by 30% leads to a 16% increase in after-tax returns on invested capital. It is thus hardly
surprising that the traditional view has been to reduce working capital. They state that taking the US economy as a whole, companies seem to have paid more attention to inventory than trade credit. Analysts have repeatedly stressed the need to improve cash collection cycles. In some countries, for example, France, there has even been recent government action to cap payment delays at 60 calendar days. Seifert also states that a comparison of accounting data of industrialized nations shows that median accounts receivable ranged from 16% to 33% of sales in 2006. With its exception of Italy, those levels were stable over time. Moreover trade credit varies across industries. US data suggest that relative accounts receivable and payable increase further away they are from the end consumer, that is, the nearer they are in the upstream of supply chain. He further states that while it seems that firms generally adhere to industry norms, there is evidence from interviews with 30 managers that they vary credit terms. There are over 1,000 different credit terms globally.

Ojeaga (2009) mentions that the characteristic features of the Nigerian banks show that the banking sector before the global financial crisis was sound and vibrant enough to support the nation’s economic growth and development. This is evident from the questionnaire that was distributed to stakeholders in the banking industry. But the management teams attempt to boost the standards of their banks and also to have high returns on investments, and therefore have exposed some of the banks to the financial crisis. The impacts of the crisis could have been avoided if there were precautionary measures. The study, suggests the following: a) The Nigerian banks do not have access to long term deposits that would enable them to grant long term loans to their customers. This made the banks to over rely on foreign financial institution and banks for credit lines. In order to avoid this, the Nigerian government through the Central Bank of Nigeria (CBN) should organize and strengthen the growth of institutions like the pension fund, housing fund, health insurance fund etc. This could be achieved through a financial liberalization policy. b) The Nigerian government should find alternative ways to fund their budget deficit so as to reduce the pressure of financing projects in the real sector of the Nigerian economy by banks. c) Nigeria Deposits Insurance Corporation should strengthen its legal frame on insuring of deposit fund. This will create confidence in the mind of the public. d) Banks should stop giving out loans to invest in the stocks of banks that are quoted in the Nigerian stock market.

4.1. Relevance of Working Capital Management to the Corporate Treasury

Many companies still underestimate the importance of working capital management as a lever for freeing up cash from inventory, accounts receivable, and accounts payable. By effectively managing these components, companies can sharply reduce their dependence on outside funding and can use the released cash for further investments or acquisitions. This will not only lead to more financial flexibility, but also create value and have a strong impact on a company’s enterprise value by reducing capital employed and thus increasing asset productivity. High working capital ratios often mean that too much money is tied up in receivables and inventories. Typically, the knee-jerk reaction to this problem is to apply the “big squeeze” by aggressively collecting receivables, ruthlessly delaying payments to suppliers and cutting inventories across the board. But that only attacks the symptoms of working capital issues, not the root causes. A more effective approach is to fundamentally rethink and streamline key processes across the value chain. This will not only free up cash but lead to significant cost reductions at the same time.

In a constantly changing and volatile environment, the companies need to focus mostly on improving their operational processes to ensure an efficient supply chain. Vigilance in adapting to changing business demands can help them to improve profitability; furthermore, with top-management increasingly aware of the benefits of self-financing, corporate treasurers are now paying close attention to their company’s working capital. On the one hand, buyers are looking to extend payment terms, whilst on the other hand suppliers are trying to resist any extension. With unsustainable pressure on suppliers, and most of them are already operating on paper-thin margins, to reduce prices still further, comes the escalating risk of suppliers failure. Whilst suppliers failure is set to remain high, other
economic statistics highlight the root of the problem. According to the European Central Bank survey\(^3\) that has been ‘an unchanged net tightening of credit standards’ and ‘the cost of (banks’) capital position and their ability to access market financing contributed to a tightening of credit standards’.

As per Kerle (2010) approximately 80% of European based companies reported having encountered difficulties in obtaining traditional bank credit. Additionally, no immediate recovery is in sight, with the situation not expected to improve until end of 2010.

4.2. Supply Chain Finance

In response to above mentioned situation, it appears that collaborative financing tools, such as supply chain finance (SCF), are generating significant interest as a way of freeing up working capital. When they are employed effectively, the SCF can help manage risk, optimize working capital and cash flow, and also improve the flow of transaction data between trade counterparties without a need for costly implementation processes.

SCF programmes are increasing in popularity especially in the EU-27 member countries, these programmes often involve asset-based structures where the key asset is outstanding invoice debt owed to smaller suppliers by a large, highly rated buyer company. The SCF schemes are usually arranged between the bank and the large buyer, then offered to participants in the supply chain.

Supply chain finance is all about optimizing the flow of money in and out of a business across it supply chain or to it’s customers. The time it takes to pay a supplier and the terms on which payments are made (e.g. a discount for early settlement) can have a significant impact on the cash position of both the buyer and supplier. It is important therefore to ensure that the details of these transactions are optimized. There is no strict definition of supply chain finance but, broadly speaking, it refers to tools techniques and products that help businesses optimize their cash flow by managing payments to suppliers and receipts from customers. These techniques can be as simple as extending payment terms to suppliers or demanding cash on delivery from a customer. More sophisticated examples of supply chain finance techniques include dynamic discounting and reverse factoring.

Today, the treasurer is pivotal to finding and unlocking the potential of new solutions to manage the risk of their business around the world, going above and beyond a traditional funding capability. For example, receivables discounting was previously part of the treasurer’s focus in their interactions with banks, whereas today we see the treasurer also taking the lead in sourcing other working capital optimization solutions such as SCF.

The various SCF programs available today reflect one of three models – reverse factoring, international reverse factoring, and integrated working capital platform, which have developed since the concept of SCF first appeared in supply chain literature in the late 1980s.

Introduced in the 1980s, the first model of SCF combined domestic trade finance with supply chain management through an innovative invoice financing arrangement known as “reverse factoring,” a three-way agreement by which the bank (or “factor”) purchases the receivables of the supplier with legal recourse to the buyer. In this earliest model, reverse factoring was purely a domestic service offered within select industries. A large, investment-grade company could extend its days payables outstanding while allowing its suppliers (typically smaller, less creditworthy companies) to reduce their days sales outstanding at a favorable rate. The second model of SCF emerged as many large companies began sourcing their supplies from the companies around the world. Finally, the third model integrates the pieces of the financial supply chain from end to end, fully automating the buyers’procure-to-pay and suppliers’ order-to cash cycles. This new level of integration supports event-triggered financial services along the physical supply chain (e.g., purchase order tracking, invoice matching services, e-invoicing, open account payments, import/export financing, reverse factoring) and afford full transparency into each transaction. This transparency will allow liquidity providers (whether banks or non-bank finance companies) to apply dynamic pricing in purchasing outstanding invoices.

\(^3\) ECB, Euro Area Bank Lending. April 2010, 28 April 2010
4.2.1. Reverse Factoring

Reverse factoring is a form of supply chain financing. It was introduced in 1980s and generally applied by automobile constructors with the aim of attaining higher profit margins by way of helping their suppliers to quickly and easily finance their receivables. Reverse factoring has also been applied in the retail industry because of the interest where payment delays continue to be a major issue for businesses. In the 1990s and early 2000s, the demand for using reverse factoring declined because of the economic contexts that did not allow it to be an efficient way of financing. In the event of global economic crisis of late 2008 where banks tightened their credit policies which resulted in increased costs of finance, firms were not able to obtain credit and faced huge amounts of deadweight cost of capital. Reverse factoring took hold at the height of the crisis and provided a solid working capital solution to ensure working capital stability and keep operations going. In recent years, the concept of reverse factoring as a financial instrument has become popular.

There are basically three parties involved in a reverse factoring transaction including the ordering party (buyer), the supplier and the factor (bank). Figure 1 shows the mechanics of reverse factoring. The process is started by the buyer (B), which often is a large company. The buyer works together with a bank to provide a financing solution to the suppliers. The bank purchases accounts receivables only from high-quality buyers (for example, any receivable owed by B from any suppliers, including S, Q and R). The bank only needs to collect credit information and calculate the credit risk for B. In reverse factoring, the buyer retains the credit risk and is accountable in case of default of invoices or payment (Klapper, 2005). The suppliers, on the other hand, can choose the receivables they want to receive cash and others to be paid at due date.

Overall, reverse factoring involves a mutual collaboration among the suppliers, buyer and bank. It offers suppliers a collaborative financing solution in which they are able to sell its accounts receivables to the bank in exchange for immediate cash and improve cash flow across the supply chain as a whole. Reverse factoring is seen as an effective cash flow optimization tool for companies that outsource large volume of services or for small companies that have large groups of clients. It provides a mutually beneficial cash flow solution for businesses that regularly purchase goods and/or services from the same suppliers, in addition to the suppliers themselves.

![Figure 1: Reverse Factoring](image)

All the three actors benefited from reverse factoring transaction for a number of reasons. Reverse factoring offers suppliers cheaper short term credit and access to off balance sheet. The accounts receivables are sold to the bank, and immediately converted into cash which increases the liquidity of the supplier’s assets and improves working capital management. They are not reported as bank loan on the balance sheet. Since accounts receivables were paid earlier by the bank (financier), the suppliers can more easily manage their cash flow, invoices and reduce the cost of capital. They can access funding immediately due to lower costs and faster processing (i.e. reducing the time between providing a service and getting paid). The interest applied for the deduction is less than the one the suppliers would have got if they did it on their own. The suppliers would be able to secure future trade with larger firms which typically request longer credit periods and access more capital against the
value of the receivables than through other financing solutions. If there is any problem concerning the payment of the receivables, the bank will have to get their money from the buyer, and not the suppliers. Reverse factoring gathers all the suppliers in one financier and centralizes most of the invoices.

Since reverse factoring is a form of buyer initiated supply chain finance, the buyer will benefit from the extended payment period, price reduction or a fee from the bank. The cash conversion cycle decreases and as a result increases the liquidity of the buyer’s assets. In case of price reduction or a fee, the buyer will benefit from a lower unit cost and a higher margin. Reverse factoring provides the buyer the opportunity to build stronger working relationships with the suppliers and further improves supply chain efficiency.

For the bank (the financier), the benefit is in the extra income from buying the accounts receivables at a discount. Since the bank works directly with the buyer, the bank can get access to more detailed credit and supply chain information. The bank can reach faster and more easily all of the suppliers, expand its existing business by cross-selling existing solutions and do business with them. It has access to a new market with only limited risk, and therefore is able to increase its market share. The bank also benefited from its compliance with the new Basel III regulations in which the risk on a reverse factoring arrangement is much lower compared to normal loans and the bank does not need to hold as much capital reserves to back its funding to the firms.

4.2.2. International Reverse Factoring
Reverse factoring can benefit both domestic and international supply chains. However in practice, international reverse factoring has more profit potential than domestic reverse factoring. Reverse factoring is potentially more beneficial in international trade transactions because payment periods in international trade are longer than in domestic trade (World Bank, 2004), and international reverse factoring provides a unique way to arrange payment terms more flexibly and to receive better purchasing terms from foreign suppliers at the same time. International reverse factoring is no different from the domestic reverse factoring except for the inclusion of a local bank in the supplier’s country. The local bank can be a branch of the buyer’s partner bank, or it can be another bank that has a local footprint. This local footprint is important so banks can leverage their local network and knowledge. For the foreign bank, it can take a margin of the total reverse factoring fees. Figure 2 shows the transaction of reverse factoring at an international level. In this case, supplier is the exporter and buyer is the importer. The process is started by the buyer. The buyer authorizes the local (import) bank to cover its liabilities (accounts payables) against foreign suppliers. The import bank assesses the creditworthiness of the buyer and informs the foreign (export) bank to negotiate factoring contract with interested suppliers based on the approved buyer’s credit line. The supplier receives immediate liquidity by the funding of the export bank once he/she sells his/her receivables against the respective buyer. The supplier is protected against bad debts to nearly 100 percent within the approved credit limit and can export his goods to the buyer on flexible open account terms.

The export bank then assigns the purchased receivables to the import bank, and in return, the import bank transfers payment of the invoices to the export bank. The buyer can take advantage of the open account terms to improve his liquidity, working capital ratio and purchasing conditions. The costs and administrative burdens of letter of credit procedures will reduce and the buyer can develop new exporters or increase the loyalty of his strategic important suppliers. In case of the buyer's inability to pay the outstanding receivables, the import bank is obliged to pay the invoice amount.

In an international reverse factoring transaction, payments are made in the buyer’s currency. The bank pays the supplier in the domestic currency and the buyer at maturity pays the bank also in the same currency. There is some exchange rate risk at the supplier because the supplier receives the domestic currency and operates in the foreign currency. To value the benefit from reverse factoring for the supplier, the interest rates have to be expressed in the same currency charged by the export factor.
4.2.3. Integrated Working Capital Platform

Many trade banks are now focused on developing an integrated working capital platform to meet the constant growing of global trade. The demand for this platform arises due to companies’ needs of the physical and financially efficient supply chains. Working capital is defined as the current assets minus the current liabilities. It entails all assets of the current assets that are transformed into liquid assets within one production cycle or at least within one year.

An integrated working capital platform in this case, can be referred to centralization of account receivables and payables whereby companies combine supply chain and payment structures using the same platform. The ability to centralize collections combined with an existing centralized payments capability completes the working capital equation. By centralizing account receivables and payables, vendor payments and customer collections can be better aligned and the gap between ‘days sales outstanding’ and ‘days payables outstanding’ is narrowed. An integrated working capital also improves cost savings and greater efficiency of processes across the entire working capital cycle.

An integrated working capital platform requires improvements in the regulatory environment and technology, discipline and human capital by a company to instill a strong focus on processes with clearly defined roles and responsibilities. It brings significant efficiency and better overall use of companies’ funds, all in support of businesses reaching its objectives. Overall, the centralization of account payables and receivables facilitates process excellence and efficiency and real end-to-end process optimization across businesses.

5. Emerging Working Capital Management

Seifert (2008) states that trade credit impacts supply chain relations, and managing it aggressively might damage these relations. Publicly traded firms experiencing supply chain disruptions, for example, have reported negative stock market reactions to such announcements with the decline in market capitalization being as high as 10%. He mentions that given these two risk of hurting sales and damaging relations, it seems that companies should take a differentiated approach to managing trade credit. Three series of question scan help in this situation where managers have to think what kind of relationship they want to build with both suppliers and customers.

First, if the relationship is of long-term nature, then in case there are more fixed costs, then the companies should understand their partner’s cost of capital, and try to create win-win situations by using trade credit to broker advantageous capital access to supply chain partners, or reduce outstanding days to eliminate unnecessary costs. Second, if the relationship is of a more transactional nature, managers should determine their company’s competitive position. If the market position is weak, then the company should offer industry standard terms to attract customers, and use trade credit to attract additional customers once sales slows down.

However, if the market position is strong, then the company should consider its cost base. What proportion of costs varies with production? If there are high fixed costs, then the company should offer industry standard terms to attract customers, and use trade credit to attract additional customers once
sales slows down. On the other hand, if there are low fixed costs, then company should ask customers for direct payment, or use discount schemes to speed up payments. Also, the company should negotiate long payment delays with suppliers.

Going beyond the simple adaption of payment terms, finance professionals have combined financial insights with electronic payment platforms, and thus created supply chain finance solutions (SCF). He further mentions that in the short term, a few immediate steps should help prevent companies becoming victims of the financial crisis such as monitoring actual payments and deviations from agreed credit terms, assessing key suppliers and customers’ financial situations, and offering liquidity in selected cases. For the medium term, companies should review their trade credit strategies, and apply the right mix depending upon their situation.

Wan et.al (2011) examine the impacts of the global financial crisis (GFC) on SMEs, and catalogued a sample of government responses to the issue. They mention that prior to the GFC, SMEs were already facing obstacles. Consequently, many governments had already implemented tax, regulatory, financing, and innovation policies to assist SMEs. With the advent of the GFC, SMEs face additional challenges that interact with each other to exacerbate the situation. In particular, SMEs are especially facing additional obstacles with respect to financing, working capital, and demand.

In response, governments of various countries in APEC economies have carried out a variety of ‘anti-crisis packages’ that include loan guarantee programs, direct government lending, risk capital measures, reducing market risk, working capital measures, leasing market measures, reducing taxes, export facilitation, and easing procurement payments that seek to help SMES. Generally, these packages include measures to stimulate demand, enhance credit, and stimulate the labor –market. The focus of these initiatives was primarily geared to facilitating access to capital. In particular, governments often chose to inaugurate or expand loan guarantees programs. They further mention that three implications follow from this finding. First, loan guarantee programs only address one dimension of the GFC –related challenges faced by SMEs. However, this is not a new approach. It would appear that governments have resorted to the familiar with relatively few measures that help other needs of SMEs.

Second, loan guarantee programs have, in many countries, simply not worked. They have not been good value for taxpayers’ funds. To the extent that loan guarantee programs were so widely used, there remains a need for research to understand better the design and the parameters of loan guarantee schemes that are associated with effectiveness and efficiency.

Third, loan guarantee provided by government create contingent liabilities that may need to be funded by tax monies. To some degree, this approach potentially understates the quantum of funds that governments must allocate for recovery from the GFC. Depending upon the size of the program, the contingent liability could be substantial.

Payne and Associates (2011) state that for entrepreneurs, crowd funding is an easy and fast way to raise startup capital while creating an online buzz for the new company. Raising crowd funding may, however, reduce avenues to follow-on funding and access to expert mentoring.

For investors, crowd funding provides easy access to investment in exciting startups in an asset class not previously available for those not accredited investors. But crowd funding increases the likelihood of encountering online fraud, reduces the opportunity to vet (due diligence) new investment opportunities, and probably reduces available feedback to investors on company progress. Grasping the importance of a diversified portfolio and the need for patience is critical to success. On the surface, crowd funding sounds like a wonderful new opportunity for John Q. Public to invest in startup ventures and help the US economy create new jobs. This is a false promise, in his opinion. Funding startup ventures is very high risk investing and should be left to those with both the experience in validating such investment, and the patience to wait for the few potential winners to mature. As is often the case, the adjectives “fast” and “easy” may not be the best features of capital fundraising sources for entrepreneurs.

Das (2010) mentions that in Singapore, New Bridging Loan program (BLP) has been enhanced to cater to loans of upto SG $ 5 million, up from S$ 500,000. The government raised its share of risk
on these loans to 80 percent, up from the previous 50%, with risk to the financial institution as 20%. This is expected to meet the working capital needs of most small to mid-sized firms, as well as some bigger ones. The new BLP is applicable for all new loans from February 2009, and included refinancing of existing loans when they were due. The scheme caters to loans of up to four years maturity. The government, also for the first time decided to take on a significant share of the risk in trade financing. This is important for the companies that had existing orders, and who needed loans to fulfill their orders as well as insurance against the risk of their buyers defaulting on payments.

Auboin and Meier-Ewert (2003) mention that an analysis of the implications of recent financial crises affecting emerging economies in the 1990's points to the failure by private markets and other relevant institutions to meet the demand for cross-border and domestic short-term trade-finance in such periods, thereby affecting, in some countries and for certain periods, imports and exports to a point of stoppage. These experiences seem to suggest that there is scope for carefully targeted public intervention, as currently proposed by regional development banks and other actors, which have put in place ad-hoc schemes to maintain a minimum flow of trade finance during periods of scarcity, through systems of direct credit or credit guarantees. Their paper explores the reasons behind the drying up of trade finance, both short and long-term, in particular as banks tend to concentrate on the more profitable and less risky segments of credit markets. It also describes ad-hoc schemes put in place by regional and multilateral institutions to keep minimal amounts of trade finance available at any time. They examine a number of questions regarding the regulatory framework surrounding trade finance products, and looks at World Trade Organization (WTO) rules in this regard. It also examines other areas where the WTO can play a role in facilitating and contributing to a global solution. Organization for Economic Co-operation and Development (OECD, 2009) mentions that it is important to stress that SMEs are generally more vulnerable in times of crisis for many reasons among which are: a) it is more difficult for them to downsize as they are already small; b) they are individually less diversified in their economic activities; c) they have a weaker financial structure (i.e. lower capitalization); d) they have a lower or no credit rating; e) they are heavily dependent on credit; and f) they have fewer financing options. SMEs in global value chains are even more vulnerable as they often bear the brunt of the difficulties of the large firms.

For SMEs, there are two related stress factors: a) increased payment delays on receivables which added - together with an increase in inventories- result in an endemic shortage of working capital and a decrease in liquidity, and b) an increase in reported defaults, insolvencies and bankruptcies.

Extended payment delays on receivables, especially in times of reduced sales, are leading rapidly to a depletion of working capital in many countries. Increased insolvency rates appear to confirm SMEs’ increased inability to obtain short-term financing.

The main factors exacerbating the banks’ attitude towards lending to SMEs are: a) the poor SME economic prospects already discussed; b) stagnation in inter-bank lending and increased cost of capital; and c) the desire to rebuild bank balance sheets.

In consequence, by choosing to keep only the strongest clients, banks and other financial institutions are contributing to a polarization process. For example, Korea reported that lending to blue-chip SMEs has increased whereas lending to SMEs with poorer credit ratings has deteriorated. For many banks this may be a sensible survival strategy and their survival is vital. In some countries it is also a case of returning to “normal” lending practices after a number of years of excessive flexibility and generosity in lending.

The stagnation in lending is true even of banks in countries where governments have deliberately strengthened banks’ balance sheets to allow them to grant additional credit to SMEs and/or where credit guarantee schemes exist. As it will be seen later in the summary, most countries have not only recapitalized their banks, but also extended the funds and guarantees available for SME financing. But the effects of the incentives to lend to SMEs put in place by governments in some countries (such as the provision of additional capital) have not yet yielded the desired results. Some governments are
closely monitoring this situation or have put in place “credit mediators” to ease the flow of credit to SMEs or have enacted binding codes of conduct for SME lending.

Confronted with worsening access to credit, SMEs are exploring alternative sources of finance such as the mobilization of reserves, self-financing and factoring. Global venture capital fundraising slowed down between 2007 and 2008. The anti-crisis packages and accompanying measures address, in many countries, the financing problems of SMEs.

The measures put in place by countries can be classified in three different groups: (a) measures supporting sales and preventing depletion of SMEs’ working capital such as export credit and insurance, factoring for receivables, tax reductions and deferrals, and better payment discipline by governments, (b) measures to enhance SME’s access to finance, mainly to credit through bank recapitalization and expansion of existing loan and credit guarantee schemes; (c) measures aimed at helping SMEs to maintain their investment level and more generally their capacity to respond in the near future to a possible surge in demand through investment grants and credits, accelerated depreciation, and R&D financing.

6. Government Involvement

Many governments have implemented measures to maintain or increase cash flows. For instance, they have allowed accelerated depreciation for investments already undertaken. Some countries are also giving tax credits, cuts, deferrals and refunds.

Governments are taking moves to shorten payment delays for public procurement (Australia, France, Hungary, Italy, the Netherlands, New Zealand, and UK) and enforce payment discipline (France). The most widely used policy measure to increase access to finance has been until now the extension of loans and loan guarantees. In some countries, the governments have found the response of the newly recapitalized banks to the needs of SMEs unsatisfactory or insufficient even though guarantees are available. These countries have resorted to discipline measures that in some cases complement the incentives, in order to pressure banks to continue lending to enterprises. Belgium and France have appointed a “credit mediator”, who at regional and central levels, may intervene to ease difficulties and help enterprises obtain bank funding. The US has chosen to strictly monitor, on a monthly basis, the credit activities of banks that have been rescued by public funding. Furthermore, it is requiring all banks to report on a quarterly basis. Ireland has enacted a legally binding code of conduct on SME bank lending. The Belgian Ministry for SMEs is giving pre-fund agreements directly to SMEs which can be taken to the banks to obtain guaranteed loans.

In addition to the policy measures reviewed above, countries may wish to consider the following policy recommendations related to measures which are more institutional or structural in nature to remedy the long-standing deficiencies in the SME financial environment:

• Encourage banking competition across economies and, to alleviate the stagnation in bank lending, consider the monitoring of SME lending by banks through timely reporting and the establishment of a code of conduct for SME lending by banks.

• To know the real situation of SMEs, policy makers also need more timely and SME specific data on the supply of and demand for financing so that they can determine if their measures are working. Already several OECD countries are improving transparency in bank lending by encouraging the timely public disclosure by banks of the composition of their loan portfolios by size of firm.

• As SMEs often lack face-to-face contact with bank managers due to the current impersonal structure of the modern banking system, banks could consider using their scoring methods for assessing SME credit-worthiness with appropriate discretion so that adequate room would be left for the specificities of the client, as happens with “relationship banking”. Appropriately balanced use of any assessment method could help in cases where the circumstances and viability of individual businesses can be accounted for. Consequently, staffing local branches with personnel who have adequate skills in dealing with SME
lending becomes important. Banks could also enter partnerships with business service providers to help them reduce the risks in SME lending.

- Evidence was offered that automatic systems of credit evaluation do not always function to the effect that viable companies can obtain credit, which could be addressed with a more appropriate and discriminate use of these methods. Systems are needed to evaluate the credit risk of SMEs on a company basis rather than on a sectoral basis, while being consistent with prudential management practices in terms of sectoral allocation of funds.

- The specific financing needs of micro-enterprises (less than 10 employees in the EU) which dominate the SME sector were considered at the Round Table. Research on start-ups by the Ewing Marion Kauffman Foundation (United States) revealed that they also need modest capital injections and that the most important source was outside credit averaging USD 32,000. This could be provided through micro-finance in countries which do not already have such schemes.

- Improving the means by which SMEs are informed about the availability of SME-related government support measures, especially those that are responses to the current crisis, is crucial for the implementation of government policy and programmes. It could be facilitated in partnership with business service providers or business associations. As indicated in the OECD Brasilia Action Statement “…informing SMEs of the range of financing options (e.g., public guarantee programmes, business angels, and bank loans) will ensure greater take-up of schemes”.

- Also competence building should spur the demand for financing among SMEs. The managerial competencies of SMEs - especially in the field of finance - have to be supported. Governments should take the opportunity offered by SME owners’ realisation that they did not have all the skills needed to help their firms survive the crisis to encourage participation in general managerial skills development, including mentoring and business advice.

SMEs should be engaged in the design of relevant finance-related policies and programs from the outset to ensure that their perspectives and needs are well understood and taken into account. Examples were given of regular communication and consultation with the representatives of SMEs through forums and round tables to raise awareness and to assess the effectiveness of existing measures and programs to help SMEs to access finance.

The OECD Brasilia Action Statement highlighted the fact that access to appropriate types of financing structures and facilities are especially required to allow SMEs and entrepreneurs to take advantage of the opportunities provided by innovation.

Ever since the financial markets crisis erupted in 2008, there has been an increased interest in supply chain finance (SCF), also called reverse factoring, as companies and their banks sought to free up cash flow in the supply chain, while reducing risk at the same time. Traditionally, the global supply chain has not been considered the domain of the treasurer. But within the increasingly complex business environment that is the hallmark of globalization, the supply chain stands front and center among the treasurer’s concerns.

Corporates are constantly looking at different ways of optimizing and releasing working capital in their financial supply chains. Some of the common strategies include:

- Working with the sales department to shorten credit terms: shorter payment terms for your customers will reduce your need for (and cost of) funding and will free up working capital.
- Ensuring that correct documents are presented under a letter of credit (L/C), so the L/C can be discounted immediately.
- Working with the procurement department so that they understand the importance of quick invoice approval processes, allowing cash discounts for prompt payment where possible.
Some companies have gone so far as to extend day's payables outstanding (DPO) into the 120-day range. A supply chain finance (SCF) programmes from a bank can help to achieve this.

Inventories have been streamlined and the supply chain designed to optimize transport hubs and warehouse locations, while reducing the raw materials and finished goods inventories.

7. Working Capital Management Optimization
Working capital policy involves decisions about a company’s current assets and current liabilities; what they consist of, how they are used, and how their mix affects the risk versus return characteristics of the company. Working capital policies, through their effect on the company’s expected future returns and the risk associated with these returns, ultimately have an impact on shareholder wealth. Effective working capital management is crucial to a company’s long—term growth and survival and is used by companies to maintain liquidity, that is, the ability to meet their cash obligations as they come due. In many industries, working capital (current assets) constitutes a relative large proportion of total assets, from 30-40% in the manufacturing sector up to 50-60% in the wholesaling and retail sectors.

Working capital directly impacts three of the largest categories on a balance sheet of any company: accounts receivable, inventories, and accounts payable. These three have the largest impact on a company’s cash flow, and therefore on a company’s “life line.”

- Inventory: reductions of stock in hand and lead times.
- Payables: renegotiate payment terms.
- Inventory: improvements in forecasting accuracy.
- Payables: stretching of payments.
- Inventory: reduction of slow moving and obsolete stock.
- Receivables: reduction in customer payment terms.
- Receivables: acceleration of billing process.
- Payables: reduction in payment frequency.
- Receivables: offer cash settlement discounts.

8. Short-Term Investment in Volatile Markets
On the other hand, when choosing a short-term investment, the treasurer needs to consider especially the following key risks:

- Credit risk – or default risk, is the risk that principal and coupon/interest may not be recovered due to counterparty failure or adverse market conditions. Especially after the latest credit crisis, credit quality and security should remain a prime concern. The risk is important in treasury transactions, primarily in placing of deposits with banks and foreign exchange and derivative transactions.
- Liquidity risk – liquidity risk, prior 2007 perhaps the fundamental risk of treasury, is the risk that a company ceases to have access to the cash it needs in order to meet its financial obligations as they become due. First it applies at the overall level of the company in its most consolidated form (it is so called ‘funding liquidity risk’); second is the risk of breakdown in financial markets which usually operate smoothly (= ‘market’ liquidity risk).
- Interest rate risk – the price sensitivity to changing interest rates.

Before 2007, counterparty risk tended to be focused mostly on liquidity management strategies. Today, although the risk that a counterparty bank will discontinue its business is lower than a few months ago, companies need to have a confidence that their banking partners will be in a good stead over the long term period. The corporate treasurers have flocked to outsource their cash investment amid the volatile markets of 2007 – 2009. Rising risk aversion has seen a flight to quality instruments,
with treasurers focusing on both security and liquidity, rather than on yield. Ever since interest rates for most of the currencies except of the Australian dollar and Polish zloty started to sink to very low levels, few regulators have been able to indicate how long the low interest rate environment is likely to persist. As interest rates being low, and liquidity has also been constrained, the corporate treasurers have not been inclined to tie up their cash over a longer period in case it is required for contingency during a market downturn, or for strategic investments such as mergers and acquisitions. Also, corporate treasurers have been disinclined to tie up the cash in longer-term instruments at low rates, as they may miss the opportunity to invest at more favorable rates should conditions improve. While interest rates in year 2012 are still low, there is also greater confidence among the treasurers especially from Europe and North America, that this is likely to remain the case for some period to come.

Conclusion
The severe credit crisis began in 2007 in the US and expanded globally in 2008-09. It changed the basics of cash and liquidity management. Pre-crisis we had a situation where access to capital was not a direct bottle-neck even at fairly aggressive leveraged balance sheets and sub investment grade rating. During the crisis and in its aftermath corporate treasuries realized they needed to develop more reliable alternatives for funding and raising liquidity. A trend to deleverage, which many times was imposed by financial institutions, meant corporates started to build up cash cushions, in the form of reserve capital for situations of financial stress. This trend was many times also driven by the company’s stakeholders, including shareholders, who requested lower levels of debt and/or increased cash balances. The normalization of the financial markets after the crisis has thus led to improved capital structures and reduced reliance on committed facilities. In response to above mentioned situation, it appears that collaborative financing tools, such as supply chain finance (SCF), are generating significant interest as a way of freeing up working capital. When they are employed effectively, the SCF can help manage risk, optimize working capital and cash flow, and also improve the flow of transaction data between trade counterparties without a need for costly implementation processes. SCF programmes are increasing in popularity especially in the EU-27 member countries, these programmes often involve asset-based structures where the key asset is outstanding invoice debt owed to smaller suppliers by a large, highly rated buyer company. The SCF schemes are usually arranged between the bank and the large buyer, then offered to participants in the supply chain.

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