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Business performance


Go with the

flow

By Morgan Acker



Cash management is a fundamental consideration for any business. For smaller companies who can't afford to upset vital lenders and suppliers, it can be a matter of survival. New financial products are giving SME financial managers access to tools that were once the preserve of big corporations.



While small and medium sized enterprises (SMEs) are starting to develop more sophisticated cash management techniques, many are still at the low end of a steep learning curve. Bankers complain that finance managers in SMEs commonly fail to match credit facilities to their actual funding needs and make costly, avoidable mistakes, such as funding the purchase of equipment with an overdraft.

SMEs typically rely on a strong relationship with their main bank for credit. The products and services have barely changed over the decades: from lock box, to payroll, cheque reconciliation and letters of credit. However, banks and financial institutions are starting to devise more sophisticated solutions to help them manage what can be large pools of idle cash.

Did you know

Small and medium sized enterprises make up 95 percent of businesses in Asia, employing over 80 percent of the workforce and contributing some 60 percent of its economic output, according to Asia Pacific Economic Cooperation (APEC) statistics.

For the banks, the attractions are twofold: the new financial products for SMEs mean better margins, while the growing clout of SMEs has created a relatively untapped sector. Many Hong Kong SMEs have grown into sizeable companies, turning over millions of dollars a year and employing hundreds of people in different jurisdictions. Akash Rathke, Citigroup's regional head of Global Payments and Services,

Cash management »»Who offers what

Globally, six banks dominate the cash management business: ABN AMRO, Bank of America, Citigroup, Deutsche Bank, HSBC and JP Morgan Chase. In Hong Kong, HSBC, Citibank and Standard Chartered lead the way.

All three offer extensive online facilities for even the smallest of companies. Standard Chartered's Flexi Credit programme offers credit without fixed asset collateral, matching financial needs based on local accounts receivable and 24-hour online access to receivables records. Citibank's Cash Concentration allows companies to pool funds in an effort to eliminate idle cash and improve cash forecasting.

HSBC, the region's leader in SME and mid cap banking, offers a walk-in centre for SMEs at its headquarter branch. One of its big selling points is its international presence, with a network of alliances and partnerships to help customers streamline their accounts receivables.

estimates there has been an increase of 20 to 30 percent in cash deployment by SMEs over the past 18 months. In other words, companies are leveraging more cash into new ventures or purchases, rather than allocating it to structured investment policies.

Complexity vs. simplicity

As the services offered to SMEs get more sophisticated, finance managers and accountants have a chance to play with tools previously only available to big corporations. Accounting firms like Baker Tilly are helping their clients to navigate these offerings. "We don't see huge demand yet," says partner Bruno Arboit, "but there are services we can recommend to our customers, to help them better manage their cash."

"SMEs now have much the same tools available to them as the multinationals, and the level of sophistication is gradually improving," says Rathke. "But for old, family owned or sole proprietor companies, the move towards these electronic offerings is gradual. Sweeping is becoming common in China and India, and regulations

support such practices. Hong Kong companies are more comfortable with tools like physical cash pooling."

Help is also at hand from academic quarters. At the Chinese University of Hong Kong's Entrepreneurship Centre, Philip McMaster advocates strict cash planning and monitoring, generating actual revenue before spending. "My mission is to build self-confidence and individual financial competence, encourage bootstrapping and weaning people off their destructive addiction to debt," he says. "Small companies need to know how to creatively use the tools available to them. That means knowing

Cash terms

Sweeping

A system to transfer funds from a company's different operations into a high-yield master account.

Netting

The process of offsetting receivables and payables, to reduce settlement risk.

what exists, understanding how products have been used historically, and having the guts and imagination to adapt them to your unique situation.”

So are the banks' new cash management products encouraging companies to take unnecessary risks? Rathke admits that SMEs don't always have solid investment policies and may take bigger risks with their assets than the multinationals. He believes a proper balance needs to be struck. “Rather than chasing higher returns at higher risk to the company's fixed assets, finance managers need to implement clear investment policies, and choose a bank that is committed to cash management for long term continuity. The bank should help establish proper stop loss and profit booking norms.”

SMEs think MNCs

Younger and more adventurous companies are adapting to innovative new tools, such as factoring and clustering. Factoring uses receivables instead of real estate as collateral. Receivables are sold to the bank at a discount, the factoring house collects them and the company gets the balance,



minus a fee. Clustering involves grouping SMEs in similar ventures to combine their expertise and bargaining power, thereby reducing costs.

Banks offering cash management services need a low cost strategy of their own, which means an aggressive consolidation of technology systems and relocation of operations to low cost parts of the world. Centralising cash management functions such as liquidity management and cash flow management in shared services centres (SSCs) helps bring down costs. Where SSCs were once the private club of major corporations, smaller firms are finding out how much they can save through outsourcing. In addition to the obvious economies of scale, this creates standardised processes and enhanced control, as data flows through a single centre.

“Large companies in Asia have been using SSCs for some time,” says Lawrence Webb, HSBC's head of Payments and Cash Management, Asia-Pacific. “The more established SMEs are looking for efficiencies in managing their working capital. They

are starting to understand the benefits of outsourcing non-core activities, something the larger multinationals have long enjoyed. There are also a number of specialist outsourcing companies catering to SMEs for processing of invoices, payments, tax, payroll, in Hong Kong and in other countries in Asia.”

Technology is also driving other trends in cash management. Many SMEs are moving rapidly from paper-based to electronic offices, and are using enterprise resource planning (ERP) software and systems integration. Products recently rolled out in the region include host-to-host and single platform web-based delivery channels, integrated payment solutions, detailed advice to beneficiaries and payers, integrated collection solutions, and automated reconciliation and invoice matching for accounts receivable.

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While Webb thinks there is still a high reliance on the paper office in Hong Kong, the opportunity to reduce costs will continue to drive changes. Having invested heavily in ERP systems, companies are learning to integrate with their suppliers, including financial institutions. Most banks and accounting firms have developed proprietary software and are reluctant to use open and direct payment channels.

However customers are equally reluctant to accept closed solutions if these commit them to one bank. HSBC has taken a lead in allowing customers to integrate their own ERP or accounting systems with the bank’s products.

As the banks compete to provide cash flow services, there will be some clear benefit to SMEs: Better returns – and more ways to stay afloat. A*

Principles of »»cash management

- ▶ Look at your past cash flow statements to understand when and where your cash needs will occur.
- ▶ Identify sources for meeting additional cash needs. Do you need a contingency fund as part of your annual budget?
- ▶ Keep your bank informed of your requirements and maintain good relationships with creditors.
- ▶ Make short- and long-term cash flow projections, and review them on a monthly basis.

