Latin America: The Journey to Treasury Regionalization

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How it is approached depends on the profile of the business; how well it will work depends on the degree of preparation and understanding.

Introduction

Large U.S. and European multinational companies that have operated in Latin America for decades today continue to expand their Latin American enterprises. Over 80 percent of the "Global 500" operate in one or more of the region's key economies of Brazil, Argentina and Mexico. Many of these companies already generate more than 10 percent of their earnings from Latin America and forecasts for future long-term growth remain strong despite transitory economic downturns.

Other companies have more recently entered the region because of numerous opportunities created by privatization in industries such as telecommunications, oil, gas and electricity. Regardless of the length of time companies have operated in the region, all of them share one challenge: the need to effectively manage cash and risk in one or more countries in the region.

Just five years ago, most corporate treasury and banking professionals expected treasury regionalization in Latin America to look very similar to the models that had evolved in Europe. In fact, there was speculation at that time that Uruguay would become the treasury center "capital" of the region. However, currency and cross-border restrictions in many Latin American countries made the cash pooling and cross-border techniques used in Europe virtually impossible to implement. In some respects, the same holds true today.

What has changed in the last five years is that both banks and companies are now more focused on what can be done rather than what can't be done in treasury regionalization within Latin America. Local and international banks recognize they will only succeed if they develop and offer cash and treasury management products and solutions that reflect new standards in local payments and collections and electronic banking systems. As multinationals begin to "push the envelope" with their Latin American banks, they recognize that they can begin their journey to treasury regionalization, even if it is in incremental steps. Many are already doing this.

One thing, however, is clear – there is no single approach to treasury regionalization that works for all companies as they strive to succeed in Latin America. Each company must, in fact, take a holistic view that balances its overall corporate business line strategy with its global treasury policies and regionalization goals.

Defining Regionalization

The scope and nature of a company's business in Latin America, as well as its overall global treasury strategy and objectives, will determine how it approaches cash and treasury management in the region. In addition, the extent of a company's presence in the region will determine whether it organizes itself as a single region or as sub-regions (i.e. Brazil, Southern Cone, Andean, Central America) within the region.

Although the term "regionalization" may mean different things to different companies, NLRussell Associates defines regionalization as "an approach taken by a company to take advantage of manufacturing, financial and/or other operating efficiencies among a group of subsidiaries in a specific region." The term may also include both centralization and standardization of company policies and processes.

Although companies may share similar regionalization goals and objectives, the actual path each takes to achieve those goals can vary greatly. Consequently, regionalization is best viewed not as a final destination but as a journey with numerous stops along the way.

Goals of Regionalization

The major goals of treasury regionalization are usually to:

- improve the management of cash, liquidity and risk
- increase operational efficiencies
- reduce costs
- enhance internal and external service levels

Achieving these goals may appear simple however, it does require a clear plan, corporate commitment, dedicated resources and capable banking partner(s).

Different Approaches to Regionalization

While companies may take different approaches to managing their cash and treasury operations in Latin America, they share a number of common elements including:

- implementation of corporate treasury policies
- centralization of risk management
- development and implementation of standard processes
- installation of a common accounting system
- streamlining of cash and treasury management operations in each country
- implementation of a treasury management system
- establishment of shared service centers (SSCs)

The extent to which a company incorporates some or all of these elements into its treasury management strategy is a function of its priorities and desired degree of centralization and/or regionalization. And, depending on the company, different initiatives will be tackled and completed before others.

The Regional Treasury Migration Model

A company's journey to regionalization may take many paths. The Regional Treasury Migration Model (RTMM) identifies a relationship between a company's characteristics and the way in which it manages treasury and selects cash management banks. It places company characteristics into four quadrants which can be compared and contrasted and used for identifying and evaluating regionalization trends in Latin America. The model, developed by NLRussell Associates, is based on interviews by the author with more than 100 multinational companies.

The RTMM is like a virtual roadmap and can be used to anticipate and predict future behaviors and needs of companies. Furthermore, the model reinforces the importance for companies to balance their current decisions, especially with respect to selecting banking partners, with their future needs and regionalization goals. For banks, using the model to better understand a company's migration path, will facilitate and ensure the development of products and solutions that both anticipate and meet corporate needs.

Regional Treasury Migration Model℠

Global Treasury

Cash Management Banking Relationships	**Decentralized Systems**	**Centralized Systems**
Single or Primary Bank	**B** • Subsidiaries use same single or primary c.m. bank in each country • Accounting Systems may vary from country to country • No regional treasury or shared service centers in the region • Electronic banking information from single or primary bank may be used by local (or global) treasury	**C** • Subsidiaries use same single or primary c.m. bank in each country • Common accounting systems in all countries in region • Regional treasury or shared service centers exist in region • Electronic banking information from single or primary bank may be used by local, regional and/or global treasury • Focus is to set up connections to regional center and/or global treasury
Multiple Banks	**A** • Subsidiaries use several local c.m. banks in each country • Accounting systems vary from country to country • No regional treasury or shared service centers today • May use local electronic banking information	**D** • Subsidiaries use one or more local c.m. banks in each country • Common accounting systems in all countries in region • Shared service center(s) may exist in region • Focus is to integrate electronic banking information into regional centers and/or global treasury from each country

Regional Treasury Migration Model (RTMM) is a service mark of NLRussell Associates
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Quadrant A companies are either beginning their regional journey or have taken a decidedly decentralized approach to cash and treasury management. They focus on the local country level, with each subsidiary selecting and managing its local banking partners. These companies do not use common accounting systems, regionally or globally. Electronic banking information is accessed and used at the local country level. In many respects companies in Quadrant A, although they are multinational subsidiaries, act like independent companies, responsible for establishing and managing their own policies, procedures and day-to-day cash and treasury management operations.

Quadrant B companies want to work with a single or primary cash management bank in the region or sub-regions. These companies do not have a regional treasury or SSC in the region and may or may not use common accounting systems. However, they do want to benefit from the advantages and efficiencies that can be derived from working with a single or primary cash management bank. Reduced banking fees and enhanced service levels can often result from combining transaction volumes with the same bank across multiple countries. In addition, a company in Quadrant B is positioned to migrate to Quadrant C to take advantage of additional benefits from using a treasury center or an SSC.

Quadrant C companies like those in Quadrant B prefer to work with a single or primary cash management bank across all the countries in the region or sub-regions. However, these companies also want to centralize transaction processing and other financial functions. To this end, Quadrant C companies have common accounting systems and are establishing SSCs to perform a variety of accounting and/or treasury management functions for a group of countries. The SSC functions typically include accounts payable, payment processing, bank account reconciliation and may also include activities such as centralized credit management and purchasing. Companies in Quadrant C use a single or primary cash management bank, and like Quadrant B, also benefit from simplified bank relationship management, common electronic banking systems and reduced banking fees. Quadrant C companies frequently develop interfaces and links between local country electronic banking information and their corporate accounting and/or treasury management systems.

The RTMM is like a virtual road map and can be used to anticipate and predict future behaviors and needs of companies

Quadrant D companies elect to work with more than one cash management bank in each country instead of using a single or primary cash management bank for multiple countries. These companies tend to have a very large in-country presence, both in terms of physical operations and sales. They frequently have numerous business lines or production facilities in individual countries. Their large size and/or complexity usually means that there is no single primary bank that can provide the breadth of local cash management services they need in all countries where they do business. Quadrant D companies use common accounting systems. However, because of the complexity or size of the local country operations, these companies are more likely to establish "country" SSCs rather than an SSC for the region or sub-regions. Some companies in Quadrant D may decide to consolidate functions performed in local country SSCs into regional or sub-region SSCs. When this occurs, the benefit from using a single or primary cash management bank will become more attractive to companies in Quadrant D. This may, however, mean a trade-off between some capabilities at the local country level and the benefits of centralizing payment processing and other financial functions.

Implications of the RTMM for Companies and Banks

The RTMM illustrates that a company's journey to treasury regionalization can take different paths and will be determined by whatever combination of elements the company believes will generate the cost savings and benefits it aims to achieve. For example, the benefits of bank consolidation may drive a company from Quadrant A to B (or eventually to C). In contrast, a company that focuses first on the synergies of common accounting systems will migrate from Quadrant A to D or directly to C.

As companies consolidate banking relationships in the region, they must evaluate the bank's local and regional capabilities in relation to their overall goals for treasury regionalization.

It is important for companies to identify and partner with "best in class" local and/or international banks in Latin America. These institutions should be leaders in developing new and innovative local country and regional cash management services. Companies need to conduct an extensive review of their existing cash and treasury management operations and evaluate current and prospective cash management banks in each country where they have operations. As companies consolidate banking relationships in the region, they must evaluate the bank's local and regional capabilities in relation to their overall goals for treasury regionalization.

Local and international banks in Latin America need to understand and consistently anticipate the banking and cash management service requirements of their corporate clients. In particular, banks in Latin America must focus on developing or expanding local country electronic payment and collection services and advanced electronic banking systems. Those banks able to offer strong local country cash management services and seamless regional "connectivity" will be best positioned to meet the needs of companies in Quadrants A and D *and* the needs of companies migrating to Quadrants B and C.

Summary

The development and implementation of a regional treasury strategy can help many companies enhance and optimize cash and liquidity management. Regionalization can also increase operational efficiencies, lower costs and improve service levels. While achieving these benefits may appear simple, it requires a clear plan, corporate commitment and dedicated resources.

Latin American cash and treasury management will continue to evolve rapidly during the next few years, presenting treasurers with unprecedented opportunities to reduce costs, streamline and automate operations and increase productivity. Treasurers who wish to move forward in this dynamic environment will view regionalization -- not as a destination -- but as a journey with many stops along the way. As with any journey, a detailed roadmap will be a key factor to success. ■

(***Author's Note:*** *In reviewing the RTMM, it is important to distinguish between the development of a corporate treasury policy and the execution of that policy. Policies are typically established at the corporate treasury level, however, depending on the company, some activities may be executed either centrally or locally. Since it is the execution of policy that affects a company's actual treasury migration path in the RTMM, policy formation issues have been excluded from the model.)*

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