3 INTERVIEW

Automating the cash execution process

Interviewer

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Interviewee

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SUMMARY

- *The three main issues currently impacting the treasury cash management process are: the effects of regulation, ensuring treasury functions are flexible, and doing more with less while maintaining oversight and control.*
- *Automation has been employed to strengthen the cash execution process as a whole and connect components by using an optimum secure location.*
- *Any changes to the function require open-mindedness and a wider range of strategy, which focus on the reduction of operational drag in order to prioritise alpha.*
- *When deciding whether to innovate inhouse or employ external solutions, Chief Operating Officers have to consider whether internal resources would be better spent elsewhere.*
- *Securing funding and support from key stakeholders depends on how far initiatives can deliver on pre-defined internal values, while still managing their expectations.*
- *Existing relationships with product and technology vendors are expected to evolve as the business evolves. Strategic partners have to be selected, in order to build mutually beneficial relationships.*

Dominique Kistan: Starting from a broad basis, what are the three main issues impacting the treasury cash management process today?

Nick Kurzel: Broadly speaking, navigating through the regulatory maze remains the single most consistent theme being discussed amongst buy-side treasurers in the current market. Evidently, uncleared margin will have the majority of this spotlight, but I believe that the effects of its regulatory predecessors will continue to have significant impact on a treasurer's ability to deliver consistent operational alpha for the business.

Investors are increasingly looking to their investment managers to provide further customization within their product offering suites which could be fund structure, strategy or asset class mix. It is now crucial for a treasury function to be flexible and be able to offer a variety of solutions to match each investor's individual utility preference. This may be due to lower or higher risk tolerances, or just because the investor would like the additional optionality. Either way, having an adaptable model that can be tailored to match your investment liquidity or risk profiles, ensures that the treasury function is not inhibitive but more of a facilitator towards new business opportunities.

Keeping pace with the ever-evolving paradox of doing more with less, as there is an industry wide push to automate operational processes and we see this coming in various forms. The options are building in house software, using one of the vast external technology vendors in the market or looking at a fully outsourced model. It is important from a treasurer's perspective to understand which processes fit best under each category and where those subsequent costs can be absorbed. It is also imperative that if you go down that outsourcing route, that you continue to maintain oversight and control of those processes.

> THE BIGGEST SHIFT THAT I SEE IN TERMS OF RESPONSIBILITY AND ROLES IS THE REFOCUSING OF YOUR PRIORITIES AWAY FROM MANUAL OPERATIONAL TASKS TO SPENDING MORE TIME ADDING REAL VALUE

Dominique: When you mention the treasury function needing to be flexible, how are you approaching and facilitating this flexibility?

Nick: The objective is to build an automated operational function that allows you to focus more on adding value for your clients. Utilizing the technology that exists now is key to achieving this. Ultimately, you want to remove the fat from these processes and allow your team or treasury department to be spending as much time on value-adding responsibilities as possible.

Dominique: In terms of choosing between in-house versus outsourcing solutions, what has worked for you?

Nick: At Aspect, we employ a hybrid model. In our view, there are processes which naturally lend themselves to being outsourced but equally others which do not. For the latter we are open to using external vendor solutions or developing systems internally. The decision-making around this will depend on what external solutions exist as well has how easily these can be integrated into our internal architecture. By way of example, we have partnered with Goldman Sachs Asset Management (GSAM) to improve repetitive trade instructions processes, in which they had expertise. They formulated a solution for our problem on their technology platform, and we estimated it would have taken significant resources to complete the same process in-house.

There isn't a one size fits all model, you need to be flexible and understand each process, and where you feel it best fits in. What is difficult with this is where these costs are absorbed, and whether it is a question of the company footing a bill or not. Areas of expertise, track record and development cost all factor into these decisions.

Dominique: To what extent has the use of automation in the cash execution process been regulatory and risk management driven, and how have these changed the way you approach new processes?

Nick: It is important in the current regulatory environment to have an automated cash management ecosystem so that your cash and collateral can pass through securely and efficiently. Inefficient cash management processes adversely impact your bottom line. From a risk management perspective, being able to connect all components of your cash management network via swift or SFTP will ensure that you can allocate cash or collateral to an optimum secure location. An example of this would be automating a money market fund trading via your custodian or prime brokerage accounts to sweep excess daily balances. Asset managers with sophisticated platforms, for example GSAM, are able to provide options and expertise for such requests.

From a regulatory perspective, understanding your margin composition and how it is calculated will help free up cash and collateral which can then be invested to increase your operational alpha. Optimizing where you clear your swaps portfolio to minimize the liquidity add on is a good example of this. As clearing houses

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transition to VAR based technologies, this style of regulatory driven change is going to require more thought and analytics.

There is also the elephant in the room, which is Uncleared Margin Rules, which is going to come with a host of new marginals and operational challenges for buy-side treasurers to consider. Ultimately, I don't feel that regulatory change and risk management need to be considered as mutually exclusive drivers of automation. The incentive for a treasurer to automate should be to strengthen the cash management processes as a whole and facilitate stronger governance within that risk management framework.

In terms of new processes, we look at whether we are going to build in-house, use an external vendor or outsource. Once we identify where the process best fits then it is just about determining what the most cost-effective solution and how that is integrated into your wider internal processes.

Dominique: Has your role been impacted by the automation of the cash management and treasury function, if so, how?

Nick: We have definitely had a transformational 36 months in the treasury department in terms of automation and open mindedness to change. Our legacy treasury systems were built using proprietary software which at the time were adequate to support our business requirements. As the business began to diversify and offer a wider range of systematic strategies along with regulatory costs starting to bare their teeth on the cash management function, we realized that we needed to adapt our treasury operating model. This was carried out in two phases, the first was to look to automate anything that was operational in nature. The second was to look to design flexible operating models and focus on value-adding responsibilities.

A good example of a treasury process that can easily be automated is the daily cash wire process. The model we have transitioned to is a hybrid between outsourcing and utilizing an external fintech vendor. We leverage off our relationship with our administrator and a fintech collateral management platform. We noticed that there are synergies between what our administrator provides us in the morning in terms of net asset value (NAV), which has allowed us to outsource margin process functions and components.

The administrator reconciles portfolio data and filters directly into our treasury and management system and this system is also connected to our brokers. Essentially, we then have an automated system based on various predefined rule sets. This automatically runs and identifies breaks which our administrator reviews as part of their daily handover and responsibilities. Assuming there are no breaks, all of our margin movements are electronically agreed and then sit in a queue for an investment manager to approve, as well as approve the associated wired movements. The cash wires are then sent out to our custodians from the platform using swift connectivity, which is extremely secure and reliable. The treasury function also receives top day margin reporting such that oversight review is conducted prior to approving any of those wires.

This process was an initiative that we implemented two years ago and saves us 5 hours a day which is almost the equivalent of a dedicated head count. So, you can see that there is value in automation of this kind of nature.

We also automated part of our money market fund transaction process by partnering with GSAM to automatically generate trades based on information we provided and applying payment instructions from a pre-agreed list. The reduction in risk and time spent on manual tasks has really opened up people's time and benefitted the day-to-day treasury function significantly. This also allowed us to remove a separate platform from the workflow entirely and allowed automated reporting to be integrated into our existing systems. It's this kind of automation that helps us focus on further improvements and ensure the business is truly scalable.

The new treasury operating model that we have implemented has certainly allowed us to spend more time looking at external relationships that are more analytically focused. An example of a new relationship that we have is with another fintech company that offers margin, cost of trading, analytics, which I see as quite complimentary to the operational margin process we have automated. This style of relationship allows the treasury team to think more about marginal optimization and better allocation positions to look to reduce the operational drag and add some alpha back into the portfolio. The biggest shift that I see in terms of responsibility and roles is the refocusing of your priorities away from manual operational tasks to spending more time adding real value.

Dominique: How do COOs select internal and external solutions, and what elements of treasury must automation be balanced against?

Nick: The role of a COO these days has become much broader within the buy-side community and to this extent, COOs seem to be much more guided by their heads of department as to which initiatives require business prioritization and what solutions exist, be it internal or external. Determining whether to go internal or external comes down to whether there is an affordable external solution available and is this internal resource better spent elsewhere within the business.

One of the factors that is important to define in the initial stages is what value your firm places on the project that you are looking to automate and subsequently what would you be willing to pay externally. This will assist when you begin reviewing what external solutions are available in the market and count the various pricing models that exist. The general rule of thumb with treasury automation is that if there is any discretionary trading element or decision to be made in the process then you shouldn't be looking to automate it. The only exception is when you are trading stable NAV money market fund products, as these can generally be included in your eco system of cash movements that I mentioned earlier, perhaps within pre-defined investment guidelines such as a split across funds for excess cash each day.

Dominique: Whose responsibility is the oversight aspect when it comes to automation?

Nick: Oversight is integral to automation in the sense that if you are using external vendors, you have to conduct a financial and IT security due diligence initially. You can even go as far as an external penetration test orchestrated by an independent party.

In terms of the actual process itself, you can't automate unless you understand exactly how the process works both from a technology perspective, as well as a technical expertise perspective. Ultimately, as the investment manager you want to be able to say to your investors that you still have full control, oversight and responsibility of every process. You are certainly not outsourcing the responsibility, just the underlying process.

Dominique: How do you go about securing funding and support from internal sponsors for new systems, improvements and automation?

Nick: There is always going to be an element of bureaucracy and red tape that you need to navigate through when you are trying to secure internal funding. It helps to have a predefined internal value and potentially have already signed an agreed spend on an initiative. This will allow that once you've got through that process it should be a proposal to your Executive Board.

If you can ensure that key stakeholders within the business are aware and support your initiatives in the early stages and are kept informed throughout the process, then this should help having any unforeseen internal resistance crop up. This resistance to change isn't uncommon but can drain momentum if not dealt with appropriately.

From a treasury perspective, it is also important that you manage expectations and articulate the rational for each initiative. What can help is that if you can translate that cost into a basis point impact to a fund and then assign a notional value to the project. This can help sell this to senior management.

Dominique: Has there ever been any pushback from key stakeholders and how have you overcome this challenge?

Nick: Ultimately there is always pushback in some form, as businesses as a whole are trying to promote more entrepreneurship, being open minded to cloud technologies, trying to be more agile and flexible and do more with less.

That said, you will always come up against some resistance to change, as it is just human nature. You need to be able to be strong willed in your convictions with these projects. If you are responsible for your department then you need to be comfortable with what you feel adds value and what the industry trends are. Then it is about educating senior management who may not be as technologically minded in your specific area, on the benefits of the project, and what the wider value to the business will be. If you start with what it is going to cost, as opposed to what the overall value is, then it can make it a more difficult situation.

Dominique: How have your existing relationships with product and technology vendors changed in the past year? Where do you see their focus and investment, and does it align with your priorities?

Nick: Our relationships with our technology vendors continue to evolve as our business evolves. We are always looking for strategic partners where relationships are mutually beneficial. Areas such as corporate and social responsibility come up in this issue, as well as culture and like-minded innovation, which are all the kinds of strategic partners that we would look to align ourselves with. We certainly see value in having a host of strategic partners within the industry but you do need to take your time in terms of selecting these partners and making sure that you understand what problems you are trying to solve in terms of your business before you go forward and align yourself to a external vendor.

Dominique: Thank you for sharing your thoughts on this topic.