WHITEPAPER

The stewardship of the balance sheet: Addressing the roles of evolving treasury

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As the steward of the balance sheet, the treasurer must manage the assets and liabilities of the bank, ensure access to sufficient funding and liquidity, and maximize returns, all while ensuring the solvency of the organization.

Meanwhile, more stringent regulatory requirements for capital and liquidity, coupled with the drive for surplus cash and capital reserve to guard against market volatility, are curtailing many of the activities that normally contribute to profits. The treasurer, therefore, is confronted with the formidable challenge of balancing two often conflicting objectives: ensuring access to liquidity while maximizing return.

At the same time, viewing and managing the overall cash position and risk exposures in fast-moving cycles and volatile markets is critical. A fragmented IT landscape can act as a considerable drag and pose operational hazards.

As banks look to strengthen the balance sheet, refinance debt and improve the quality and management of short- and long-term funding, the role of the treasurer will be critical for success. However, the treasurer will need the support of a comprehensive technology platform that enables access to the wealth of information and analysis that is required to protect the bank while allowing them to act as an effective steward of the balance sheet.

Assure liquidity: Ensuring the bank can forecast and meet its obligations

As funding by traditional external sources, such as interbank funding, declines and risk appetites diminish, calls for banks to provide more collateral to secure funding have increased. As a result, while some banks continue to struggle, others are becoming “overly liquid.” So, the treasurer must ensure that the bank has ongoing access to sufficient liquidity to honor its commitments and be a reliable liquidity partner. There are three key ways the treasurer can meet these core objectives:

1. **Develop a strong liquidity strategy – supporting decisions with rich analysis tools**

   Bank treasurers need to be able to easily identify the impact of every activity or the bank’s position and formulate liquidity policies and strategies to make timely and correct funding decisions. For this, the bank needs to establish a single information system that provides an accurate view of its current liquidity position and exposure to risk, as well as analytical tools that show the effects of future market movements or events on liquidity.

2. **Closely track liquidity positions and market movements – controlling risk through constant data analysis**

   Having formulated a robust liquidity strategy to underpin the bank’s funding decisions, the treasury must be able to constantly and proactively monitor the success and viability of that strategy. Only with complete and forward-looking analysis can a bank ensure that it manages the risks that, at any point in the future, may prevent it from meeting its obligations.

3. **Strengthen, integrate and automate payment processes– enabling the efficient execution of transactions, reconciliations and reporting**

   To optimize its liquidity and risk strategy, the treasury needs confidence in the core payment activities that underpin the bank’s business. Thus, the treasurer needs an inclusive set of information from multiple, disparate payment processing sources. It must also be able to count on a high degree of frequency and confidence in the data.

   Highly automated payment systems and powerful process management capabilities can enable the bank to respond more quickly to sudden crises as well as collect payments and manage liquidity more efficiently in times of high stress.

Assure solvency: Protecting the nest egg

The inadequacy of bank practices around predicting and managing risk was one of the lessons of the financial crisis, and this was further exacerbated by the drying up of funding sources. Notably, there was also a significant disparity between the risks being taken by banks and the way those risks were perceived by their board of directors.

As steward of the balance sheet, the treasury must above all make sure that the capital value of the bank's assets is preserved. This means setting aside a sufficient "nest egg" to ensure the survival of the organization. There are three key ways the treasurer can help protect this nest egg:

1. **Formulate a robust credit and market risk management strategy – supporting decisions with constant analysis of the capital at risk**

   Global banks, in particular, must step up their vigilance and control when it comes to credit, operational and market risk – along with increasing transparency – to improve the quality of credit decisions.

2. **Monitor the bank's day-to-day and projected capital positions – controlling risk by analyzing real-time data and modeling potential market movements**

   Today's markets require a single, centralized risk data system that not only provides a clear view of the bank's day-to-day business but also keeps pace with a rapidly evolving and increasingly complex array of products. Such a system can provide timely and accurate information on a wide range of risk types, particularly concentrations, settlement, pricing/model and market risks.

3. **Ensure compliance with external regulation and internal policies – tightening operational processes for efficient capital management and timely, accurate reporting**

   If banks wish to accommodate evolving regulation, they need to simplify and standardize their typical fragmented and complex systems, and integrate flexible regulatory reporting tools. Most critically, one central source of data must sit at the heart of the system to support all internal and external reporting to accurately reflect all risks the bank is exposed to.

Protect revenue: Reducing noise in financial results

One of the treasurer's core objectives is to maximize the return on assets under stewardship. However, shareholders require stability in reported earnings as well as financial return. A number of factors threaten this stability, but by managing these, the treasurer can mute the "noise" that they create and provide the clarity that the treasurer requires and in turn needs to deliver to stakeholders.

For example, without agile and fully integrated treasury management processes – that in turn feed into a centralized data management system – the treasurer cannot make assessments and decisions accurately or at the right time.

Efficient, highly automated and intelligent processes are therefore essential for running day-to-day treasury operations and will ultimately support the treasurer's role as steward of the balance sheet.

With an effective treasury management system, the treasurer can maintain stability and protect revenue by mitigating the impact of noise on the bank's front-, middle- and back-office operations and harnessing technology to address two key, related challenges:

1. **Minimize operational and environmental friction – streamlining processes across the bank**

   In today's complex and unpredictable financial environment, treasuries need rigorous controls and processes to successfully filter and manage a variety of noises. By improving, streamlining and integrating their operations, treasury management systems, and information systems and delivering high levels of automation and visibility across payment, settlement and reconciliation processes, banks can address the cumulative challenges of noises such as volatility, instrument complexity, lack of transparency, innovation, regulatory change and compliance, changes to operational processes and policies, organizational change and operational losses.

2. **Manage market behavior – using advanced trading and hedging techniques to help stabilize earnings**

   As steward of the balance sheet, the treasurer is constantly confronted with the realities of "tenor mismatch" between the bank's assets and liabilities, especially in times of market volatility and fluctuating interest rates. To manage volatility, treasuries need tools for hedging, advanced asset liability management analysis such as funds transfer pricing and dynamic balance sheet simulation, and hedge accounting.

Serve customers: Improve visibility and control beyond the treasury

As part of the day-to-day operations of a bank, the treasurer must support and monitor activities that originate both within and outside the treasury. While transactions that are initiated internally are normally immediately visible to the treasurer, it is vital that the same levels of visibility are available for those that take place beyond the treasury – especially when they may have a considerable impact on treasury operations.

As more and more competitors offer additional services to customers, banks must be able to respond to shifting market trends and opportunities, whether that means asset class diversity or geographical location. While this provides banks with opportunities for additional revenue, it also carries risks that must be managed by the treasury. The treasurer can manage customer flow by supporting the front, middle and back offices in three ways:

1. **Gain a detailed view of all customer transactions and trading activities – capturing trade flows outside the treasury to help manage associated risks**

   All customer flow activities have a direct impact on a bank's liquidity position, requiring close interaction between and vigilance from the ALM and treasury teams. Banks can ensure that both teams have the transparency, consistency and accuracy they need by utilizing technology and integrating systems throughout the organization.

2. **Closely monitor the bank's customer position – minimizing the impact of margin requirements and market movements**

   In order to extend customer relationships and increase wallet share, banks need to be able to service customer requests and bring new products to market across a diverse arena of activities while reducing credit risk exposure and the impact of margin requirements. Therefore, it's essential that accurate credit exposure information be available across all client dealings, including capital market transactions, core and retail banking, any trade finance, leasing, loans and other credit activities.

   At the same time, banks need to upgrade their client servicing models to build greater automation through function-rich portals and client relationship management systems, which will increase efficiency and control operational risk.

3. **Improve efficiency and profitability across all customer transaction processes – supporting payment investigation and the prediction of end-of-day positions**

   In today's competitive market environment, banks must also be able to provide new types of transaction support services, such as foreign exchange services and money market transactions. These activities can become profitable sources of revenue and liquidity provided that satisfactory risk management practices are enforced and high levels of automation and operational efficiency are achieved.

   By streamlining and integrating their transaction support services as part of a single, efficient technology and data management framework, banks can more accurately predict their end-of-day liquidity positions across a multitude of disparate customer accounts – and as a result, improve their overall management of liquidity.

   FIS' Ambit Treasury Management addresses the strategic, operational and risk management requirements of a bank's treasury across the front, middle and back office, helping the treasurer to safeguard and steward the bank's financial assets and effectively manage its liabilities. The solution suite helps the treasurer assure liquidity by providing comprehensive up-to-date data on cash, funding and exposures; assure solvency by providing a centralized source of information for robust reporting, planning and decision-making; protect revenue by providing an accurate view of asset/liability positions, the hedging overlay and performance attributions; and finally, manage the impact of customer flow on liquidity by providing greater visibility and control beyond treasury.

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