

P E R S P E C T I V E

Cash Management- An Insight



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Traditionally, businesses have believed that profits indicate success. While it is true that profits are one of the key indicators of success, many are now starting to realize that there is something more fundamental to their very survival; and that is 'cash'. 'Cash is King'- And this holds true for every business irrespective of its size. The availability of cash balances is a key determinant of a company's competitive ability, because it provides the means to invest in people, technology, and other assets. Efficient Cash Management is therefore indispensable.

What is Cash Management?

Cash Management comprises of a series of activities aimed at efficiently handling the inflow and outflow of cash. This mainly involves diverting cash from where it is to where it is needed. In other words, cash management is the optimization of cash flows, balances and short-term investments.

'Cash' in this context, may refer either to cash in the form of currency, or to other equivalents such as cheques, drafts, deposits, among others. While organizations may hold other assets which can potentially be converted to cash, cash management essentially deals with the management of liquid cash and near-cash assets such as marketable securities and time deposits, which can be readily converted to cash. The primary feature of such cash balance is that it has no earning power. Nonetheless, it is crucial to organizations for three main reasons:

1. **Transaction:** Ready cash balances are vital for routine transactions including purchases, operating expenses, wages, and other payments such as dividends, taxes and so on.
2. **Precaution:** There may be unanticipated cash requirements as a result of sudden increase in inventory costs, delay in collection of receivables, among others. And maintaining ready cash balances is essential to deal with such unforeseen expenses.
3. **Speculation:** Reserving cash balances is also crucial when firms anticipate decline in prices of raw materials, reduction in interest rates for buying securities, availing early payment discounts, among others.

Why Cash Management?

Lack of control over cash flows and inefficient cash management can be very harmful to business. More often than not, it is the improper management of cash that has caused businesses to fail. Effective cash management is therefore a necessity for businesses.

Companies heavily rely on knowing their cash position to manage working capital requirements such as ordering inventory, raw material, or acquisitions/expansion program, for which they need a clear idea of how much cash is required, and when. This is enabled by efficient cash management.

Moreover, a company's cash position is said to be a better indicator of the health of its business, rather than its profit and loss statement. Hence knowing the cash position is crucial for every business to:

- forecast when, how, and where cash needs may arise
- determine which would be the best source for additional cash needs, and
- be prepared to meet cash needs when they arise

And for better visibility into the cash position across banks, across borders, cash management is crucial. It empowers businesses with the ability to forecast cash flows, plan future business strategies, and manage cash accordingly.

Components of Cash Management

Businesses commonly face issues with slow movement of funds, long-drawn reconciliation processes, locked working capital, and loss of float income. Hence there are certain fundamental requirements for efficient cash management, including control over receivables and payables, visibility on cash positions, among others. And to address these needs of corporate customers, banks widely offer cash management services comprising the following:

1. **Account Reconciliation:** Managing cheques, monitoring their clearance, and

keeping track of the true cash balance can be an overwhelming task for businesses because of the huge number of cheques that are processed on a daily basis. Hence banks offer account reconciliation services wherein corporate customers can upload details about the cheques issued on a daily basis. And at the end of the month, the bank statement shows information on cheques which have been cleared and those which have not. This system is also helpful in the process known as 'positive pay', used by banks to prevent cheques from being fraudulently cashed if they are not on the list.

2. **Cash Concentration:** This is a quick and cost-effective method of moving funds from different accounts spread across the country to a single monitored and managed account. This allows businesses to maximize the use of available cash, and to optimize returns on consolidated balances.
3. **Financial Risk Management:** Risk management is the process of measuring risk, and developing and implementing strategies to manage and mitigate risk. Financial risk management plays an important role in cash management, because it focuses on managing risks in relation to changes in interest rates, commodity prices, stock prices, exchange rates, among others.
4. **Liquidity Management:** Forecasting the cash needs of a business is essential for managing cash flows, short-term borrowings, among others. in an efficient manner, in order to ensure that such cash needs can be met if and when they arise. This requirement is addressed through liquidity management services offered by banks. Liquidity management comprises of activities that release the investments locked in working capital, enabling it to contribute to higher profits. It also refers to the specific services provided by banks to enable their customers optimize their interest revenues and reduce interest costs.

Cash Management: Corporate Expectations and Consequent Trends

With growing recognition of the need to adopt cash management strategies, companies are

expecting solutions around standardization, reconciliation, integrated banking systems with corporate systems, and real-time reporting for overall view of the existing cash position. And the current trends in cash management emerge from banks catering to these needs of corporate customers:

Complete Visibility: Corporate customers increasingly expect superior cash forecasting ability, for which they need complete enterprise level visibility into cash balances and movement of cash. This is provided by banks in the form of status reports, direct enquiry, and through consolidated view of accounts held with branches/banks across the globe.

Rich Reporting Modules: In order to make corporate customers understand the need to adopt cash management services, banks are showing cost-benefit analysis reports, and demonstrating the benefits offered by cash management using graphs and illustrations.

Integrated Services: Corporate customers prefer a single platform for all their financial needs in place of disparate systems. Hence the focus is on integrating cash management systems with other activities involving the bank. For example, linking of ERP solutions with banking systems facilitates cash management by enabling effective trade finance process and investment management, among others.

Remote Deposit Capture and Straight-Through Processing (STP): In order to accelerate transactions businesses are looking for solutions that offer straight through processing capability. For example, corporate customers are trying to streamline their transactions and reduce downtime, for which banks offer STP services which enable businesses to conduct entire trade processes and payments electronically.

And to better serve the needs of corporate customers, banks look to technology vendors who offer optimal solutions that can enable more efficient cash management.

The Role of Technology in Optimizing Cash Management

Cash management solutions are not new. The market is mature and many banks offer efficient

cash management solutions. But market forces, economic conditions, and changing corporate trends have generated opportunities for further innovations in this space.

Although traditionally a large number of these solutions have been windows-based, with many corporate customers embracing internet banking, several banks are now migrating to browser-based solutions. Technology has been the driving force in optimizing cash management solutions for corporate customers:

- Browser-based solutions facilitate centralization of cash management thereby enabling better accessibility by users across the organization thereby having a better control of cash flows
- Online banking and STP help quicken payments, thereby accelerating business and streamlining processes by eliminating redundant manual processes
- 360 degree view of accounts offers greater visibility on cash position thereby improving the forecasting ability.

All these facilities help businesses optimize cash management and consequently help improve their cash position.

Scope for Improvement

Cash management solutions are now widely being adopted, and hence there is likely to be an increase in the number of vendors offering these solutions. Correspondingly, corporate customers are also likely to become more demanding, thereby promoting more intense competition amongst vendors. Here are some areas with scope for improvement which vendors can focus on, to provide better services than their competitors:

Eliminating Disparate Systems: Different cash management solutions are being offered for diverse segments. And as businesses grow, managing these disparate systems is increasingly becoming a challenge. Hence vendors should come up with a single platform which can support various cash management products and services as the business grows.

Customizable Solutions: Banks today offer similar solutions to all corporate customers irrespective of their size and business. Hence vendors should try to come up with a customizable platform which can cater to the specific needs of different businesses.

Unified System: Integration of corporate customer systems with banking systems can be very helpful in reconciliation of internal systems with banking systems, and can support account management between the bank and customer. And this offers great scope for vendors.

Today, banks are leveraging cash management systems as a tool to build long-term trust with corporate customers, because these systems will empower bank's customers to be empowered and manage their liquidity position at any given time, thus building a trust and strengthening the relationship that goes beyond transaction banking.

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