



Transparency in trade, cash and credit: an idea whose time has come

By ALEXANDER R. MALAKET, CITP, PRESIDENT
OPUS ADVISORY SERVICES INTERNATIONAL INC.

Transparency is a notion that has received a great deal of attention over the past year in particular, as relating to financial dealings in the GCC, the Middle East and the MENA region more broadly.

Is this simply the latest buzzword to circulate in business and financial circles? Is it a thinly-veiled, self-serving attempt by outside interests to change the way business has been done in the region for years?

There may, however, be an element of both in the current discussions around transparency. It's undoubtedly true that there are substantive, timely and important issues to consider around this concept – issues linked to irreversible developments driven by globalisation. These include the increasing integration of the global financial sector, and the evolution of local business practices in the Middle East.

Financial markets, regardless of the political, cultural and even legal context within which they operate, are directly and fundamentally impacted by perception and expectation: expectations about financial results can have greater impact on the health of a company or sector than the actual, objective financial results themselves.

Perception and expectation are both shaped by information flow.

As the movement of capital is increasingly global in nature, the importance of perception and expectation is amplified, and the need for comparable reference points (financial metrics, reporting standards, credit information) becomes increasingly important, to ensure, for example, that businesses and economies in the Middle East attract inward capital. Without this, it is understandable if the region finds itself lagging behind other markets that put transparency at the heart of their banking and financial standards.

In that context, the drivers for greater transparency begin to look more like a natural, evolutionary process tied directly to the increasing integration of global financial markets.

Similarly, as corporates (particularly midcaps) in the GCC begin to look at business opportunities beyond domestic borders and beyond regional markets, the disciplines of financial management will become increasingly important to the effective

running of these businesses on a cross-border basis.

Transparency is a key issue at both the macroeconomic level and the enterprise-level of the business environment, as has been clearly illustrated by recent events in Dubai, Saudi Arabia and elsewhere – and the critical role of perception and expectation has similarly been brought into sharp focus in the context of the global crisis.

The economies of the Middle East are influenced by both local enterprise and by foreign entities operating in the region; the latter group, from Europe, the Americas, Asia and beyond, operate on the basis of financial and business practices which govern their operations at home.

The former, which include locally-based organisations, remain very relationship-focused, many still led by their founding entrepreneurs who have not had the luxury of time to review financial processes and practices, with a view to optimising these.

Some large, international financial institutions draw a distinction between their international clients operating in the Middle East and their local clients based in the region – at least in part because of the difference in approach related to financial practices, credit management (broadly speaking, transparency) in commercial transactions. The complex organisational and legal structures of local businesses, some of which have 200 or more affiliate or subsidiary companies, with financial flows (value) rolling up to a parent/holding company entity, is an important factor in defining the nature of the dynamic between bank and corporate client. In these types of organisations, the question of transparency is critically important. And it is one that MENA businesses have to confront.

As one senior executive noted, transparency links directly to issues of corporate governance. Given the rapid evolution of local businesses, and the still highly concentrated model of decision-making in many corporate entities in the region, the question of transparency encompasses both the availability of information and timely access to senior decision-makers (those with signing authority) in client organisations.

In view of the increasing international aspirations of businesses all over the Middle East, and the attractive potential/growth patterns in leading economies in the region, plus the posi-

tive perception around Islamic banking and finance practices, reinforced through the global crisis, a careful consideration of the value and advantages of transparency is well-timed.

Etienne Bernard, head of Global Transaction Services, Eurozone & Middle East at RBS in Dubai, notes: “Under current conditions, and in light of the organisational complexity which characterises many of our clients in the Middle East, we are working closely with financial executives and senior leaders to be able to design solutions which help to enhance the treasury business of our customers. Part of our value proposition as an international bank is to facilitate a greater appreciation for the value of transparency, and further, to work with local businesses through events, conferences, workshops and training, to help the process shift from concept to action.”

The critical importance of regulatory issues and requirements, globally and in the region, is perhaps well illustrated by the application of Basel II capital adequacy requirements across a variety of jurisdictions in the world.

While bank regulation related to capital reserves may seem esoteric and far-removed from the conduct of business and the world of deal-making, the reality is that corporate executives who understand the restrictions – and opportunities – represented by Basel II for financial institutions, will be better positioned to extract maximum value from their banking relationships, but only if that insight is accompanied by a concerted effort by corporates to ensure timely communication and transparency with their bankers.

Basel II can, under the right circumstances, allow a more favourable capital treatment (i.e. reduced reserve requirement) for trade finance transactions than for a straight loan, for example. Financial professionals can work with their bankers to access this (generally less expensive) capital, creating a win/win for the bank and the corporate client. Similarly, candid discussion about a company’s mix of assets – both on and off-balance sheet – can lead to valuable consideration of strategies available for optimising the mix of credit solutions provided to a corporate customer.

In addition to facilitating access to additional financing options, transparency and timely communication can be important in the context of effective/enhanced risk management. Both trade and cash management solutions can be integral to effective financial risk management, but the ideal solution for a company or transaction can only be developed and deployed based on an intimate knowledge of a client company’s business.

The global crisis has certainly motivated greater attention to risk – including risk internal to a business as well as counter-

party risk (perhaps for the first time, this includes risk related to financial institution failure, not just risk related to a buyer or supplier).

While finance and treasury functions had historically operated with minimum staff and resources, the crisis has driven companies to expand their finance and treasury operations, and to look actively for solutions which optimise these areas of activity within the corporate organisation. The role of treasury in identifying, managing and mitigating risk is now more central within many corporates.

Momentum is reported to be building in this, but for some, the pace of implementation of change related to risk, treasury and financial functions is slow – partly because of ongoing issues with transparency and partly due to the continued concentration of decision-making and signing authority among corporate clients in the Middle East.

An alternative view is that the movement toward transparency is well underway and showing momentum and support from the financial sector and the business community – particularly larger enterprises in the region.

Farrukh Siddiqui, executive director and head of trade services in the Middle East for J.P. Morgan Treasury Services in Dubai observes: “We are seeing a welcome and positive trend in the region, where clients – both corporate and FI – are very keen to provide the information required, to facilitate sound credit and risk management decisions.”

Transparency, like the increasing burdens of regulatory requirements, can be ignored, resisted, or embraced as inevitable – but perhaps it represents opportunity in the guise of an apparent challenge. As with many new rules, standards and practices, what first appears to be a burden can, with clever implementation, be turned into an opportunity to improve performance.

Fundamentally, transparency links directly and inevitably shapes the nature of the relationship between businesses and their bankers – and also between financial institutions seeking to collaborate in pursuit of opportunity and in the service of their mutual clients.

Asif Raza, managing director, and head of Treasury & Securities Services in the Middle East and North Africa at J.P. Morgan observes: “The requirements related to ‘KYC’ [Know your client] have become increasingly important in markets across the globe, including the MENA region; recent events in global markets have motivated greater focus on transparency and communication, among corporates and FIs; indeed, the oversight of Central Banks in the region has been very effective. As an international bank, we take a partnership approach, and are very focused on a certain client segment, where fundamentals are solid and good banking and financial practices are the norm.”

Just as the regulatory requirements around KYC become increasingly onerous for financial institutions around the globe – with substantial justification, one could argue – the effective execution of due diligence and the discipline imposed by KYC requirements has been valuable to the conduct of business. The benefits of transacting on the basis of Islamic finance are gaining



increasing traction, with clients in the region actively looking for Islamic finance versions of conventional banking products. At the same time, there is a sense that effective due diligence and truly ‘knowing one’s client’ as well as the nature of the business being conducted, causes a discussion around transparency to become redundant.

In the absence of such intimate knowledge of a client’s business, the focus returns to the notion that transparency is an element of good corporate governance. This inevitably will include an element of timely and candid communication. In that context, the relationship between banker and corporate client can – and should – be a relationship based on partnership, and the connection between transparency and partnership can create value for all concerned. The same is true for business relationships between financial institutions.

Transparency is not simply a matter of regulatory imperative, nor is it just an academic concept, or a theoretical construct meant to reflect a ‘perfect world’. It is, on the contrary, a fundamental enabler and facilitator of good business practice – an essential lubricant to the efficient conduct of business, especially across borders, and especially in post-crisis times when confidence has been proven to be at the core of global financial stability.

At the level of business relationships, adequate transparency can be critical in encouraging partnerships and in supporting critical business alliances in the pursuit of opportunities that would otherwise be out of reach.

Notes Bernard at RBS: “There is significant opportunity in the Middle East for banks and financial institutions to collaborate in

the context of large projects; indeed, the earlier we are engaged in dialogue by our corporate clients, the more quickly – and creatively – we can work to mobilise local and international resources in support of an opportunity. We can then bring to bear all the (considerable) resources and networks at our disposal, for example, structuring innovative trade solutions to the benefit of our client and partner bank, and ultimately, to the benefit of the region in which such projects are executed. For all of this to work, however, each interaction must be properly informed – transparency is not an option, but an absolute necessity.”

Some of the practical implications related to transparency are (ironically) perhaps less obvious: to paraphrase one senior executive, if banks or corporates fail to provide information, or fail to demonstrate commitment to adequate levels of transparency and communication, they are simply eliminated from consideration as prospective clients or partners.

Is it an accident that the largest and most successful organisations in the MENA region have gradually embraced the notion of transparency? Is it a matter of coincidence that there is significant demand in the region for conferences, training and other activities around risk management and the idea of transparency? Not at all.

Transparency is efficient. Transparency is good business practice. Opacity is expensive – both in real terms and in terms of lost opportunity. In the end, the discussion – and the practices in the MENA region – are evolving in a direction that will serve the economies and the businesses of the region well, in the context of an increasingly global business environment. ■

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