Corporate Risk Management Survey 2024

Navigate uncertainty to drive growth with insights from senior finance leaders

HSBC

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Foreword

Ever since the global financial crisis, companies have faced multiple, often overlapping crises that have placed a significant strain on their finances. From managing Covid-19 pandemic disruptions and rampant inflation to dealing with escalating international conflicts and volatile foreign exchange (FX) and interest rate markets, adaptive risk management has become an increasingly vital remit of the corporate treasury function. In turn, the continuous cycle of uncertainty requires the treasury function to not only mitigate risks but find ways to benefit from them.

The Corporate Risk Management Survey 2024 marks the third edition of our triennial study. It looks at how the treasury function has evolved over the past three years and the trends likely to shape its future development.

Since our last survey in 2021, the risk management landscape has become even more complicated. Many treasury teams were caught off guard by a sharp rise in interest rates as central banks sought to tame soaring inflation, resulting in higher financing costs – something finance leaders expect to persist as a challenge over the next three years.

At the same time, ongoing geopolitical tensions are impacting trade and investment, creating further liquidity and FX risk challenges as companies seek new trade relationships and adjust their supply chains in response. The latter are also impacted by expanding ESG regulation.

Drawing on expertise from HSBC's corporate treasury specialists, this report shares actionable insights to help your treasury risk management function navigate these multiple waves of uncertainty. From strengthening strategic partnerships with the wider business to embracing technology and artificial intelligence (AI) to help redefine the treasury of the future, we outline the opportunities that can help your treasury team navigate uncertainty to drive growth.

> "The continuous cycle of uncertainty requires the treasury function to not only mitigate risks but find ways to benefit from them"

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Methodology

This report summarises the findings from two surveys across different levels of corporate finance decision-makers, combining the view from the top with the aspirations and challenges of those at an operating level. Interviews with HSBC contributors were conducted in August 2024 and references to the market environment are reflective of this.

In mid-2024, HSBC surveyed 529 senior treasury professionals from multinational corporates across a range of sectors. The survey was conducted in a multiple-choice, online format and was open for a six-week period until 30 July 2024. Europe, Middle East, and Africa (EMEA) provided 53% of participants, with 36% from the Asia-Pacific (APAC) region and 11% from the Americas. Some 35% of participants worked for companies that generated annual revenues of less than $1bn in their latest financial year, while 36% recorded revenues of $1-5bn, 17% recorded revenues of $5-20bn and 13% saw more than $20bn.*

In parallel, the UK-based media and research company, Raconteur, was commissioned to survey a further 300 CFOs and their equivalents (the most senior member of a finance department) from multinational corporates across a range of sectors on behalf of HSBC. Of those, 100 corporates had revenues of $250m-1bn, a further 100 had revenues of $1-10bn, and the final 100 had revenues of $10bn+. Within each of these three revenue groups, 40 respondents were located within the EMEA region, 20 within the Americas and 40 from APAC.

** $ denotes USD throughout*

1 Executive summary

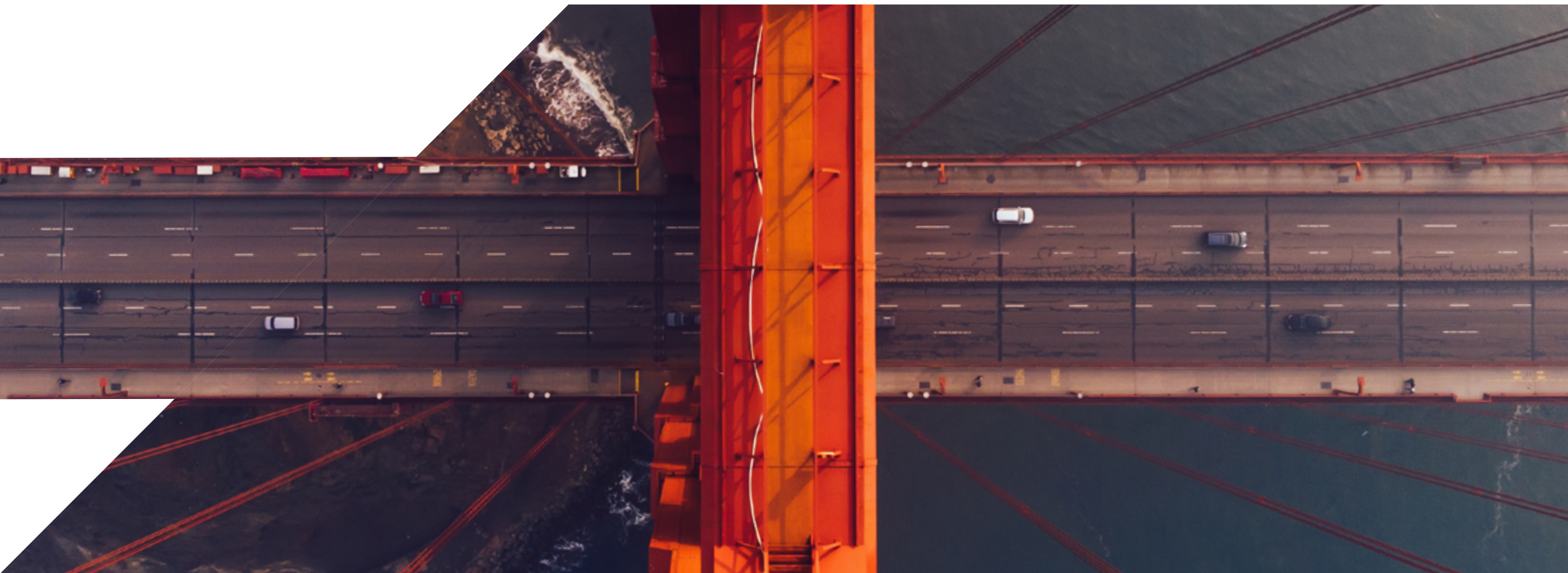
With companies battling disruption on multiple fronts, managing financial risk has become a juggling act. Treasury departments are tasked not only with mitigating risk but also increasingly with providing the financial safety that allows businesses to pursue new opportunities.

This multilayered challenge means the job of treasury risk managers is more complex today. Many risks faced by treasury functions are difficult to predict because they are not driven by macroeconomic events alone. Take FX risk as an example, with 47% of survey respondents saying it is an area they feel their business is least well-equipped to deal with. This vulnerability is partly due to exchange rates moving significantly in reaction to unexpected geopolitical events, rising inflation making forecasted revenue and cost volumes inaccurate, and continued disruptions to supply chain and sales logistics delaying cash flow timing.

Treasurers are also still struggling with the internal quality of cash flow forecasting data. Some 93% of respondents said those data inaccuracies had led to avoidable losses over the past two years alone, either due to overborrowing or liquidity shortfalls.

Inflation is seen as unlikely to disappear in the near term, with 48% of respondents expecting it to contribute to higher financing costs over the next three years. This is prompting treasury teams to assess their split between floating-rate and fixed-rate debt. With lower risk capacity, the direction of travel is often to increase certainty. This possibly explains why 37% of respondents have increased their share of fixed-rate debt during the past three years, with 44% expecting this to further increase in the coming three years.

The treasury function’s reputation continues to improve, with 68% agreeing that treasury plays a key role in strategy decisions (up from 41% in 2021, with the perception especially improving in APAC , with 78% of respondents in agreement). While 44% of respondents agree that communication between treasury and the C-suite has improved, most respondents still view it as only moderately effective. Only 4% rate it as highly effective, pointing to further room for improvement.



47% of finance leaders say they are 'least prepared' to deal with FX risk

93% of finance leaders say their business has suffered avoidable losses as a result of inaccurate forecasting in the past two years

68% of finance leaders say that treasury plays a key role in strategic decisions

99% of finance leaders are at least somewhat concerned about ESG visibility into their suppliers

61% of finance leaders believe AI will benefit their company's profitability over the next three years

"Despite the uncertainty surrounding businesses, financial leaders are optimistic about revenue growth prospects in the near future"

Despite the uncertainty surrounding businesses, many financial leaders are optimistic about revenue growth prospects in the near future. Respondents most frequently attribute this to rising customer demand and quicker adoption of new technologies (both on 75%), as well as a reduction in geopolitical tensions (52%). Some challenges are likely to endure, with 58% of respondents worrying about high inflation and 55% concerned about a prolonged economic downturn.

ESG and supply chain risk is also rising in importance for treasurers, with 32% of companies already incorporating ESG guidelines and policies into their supply chain. Nearly all respondents (99%) said they are at least somewhat concerned about ESG visibility into their suppliers, while 56% are very concerned about their ability to meet ESG reporting requirements; this is particularly prominent in Europe, where ESG regulation is most advanced. A growing number of respondents expect to work with banks or other financial partners to financially support suppliers in their ESG efforts, but 27% also anticipate cancelling supplier contracts because of ESG issues over the next three years.

The emergence of AI is expected to create tailwinds for businesses and their treasury function. Some 61% believe AI will positively benefit their company's profitability over the next three years, while another 61% believe it will become very or extremely useful for risk management decisions over that time frame. There also appears to be strong support for AI adoption within businesses. However, AI adoption does not come free of challenges. For example, 62% of respondents are concerned about a lack of access to talent and skills.

By recognising and embracing the challenges ahead, treasurers will be well positioned to navigate uncertainty, help their companies better manage the current risk environment and put themselves on a sounder footing for growth in the years ahead.

2 Navigating the risk management landscape

In a world of polycrisis, where businesses are dealing with operational challenges and financial pressures on multiple fronts, the risk management landscape has become ever more complex.

According to our latest Corporate Risk Management Survey, CFOs and other financial leaders say that FX risk (47%), supply chain risk (35%) and climate risk (34%) are the factors their companies are least well placed to deal with.

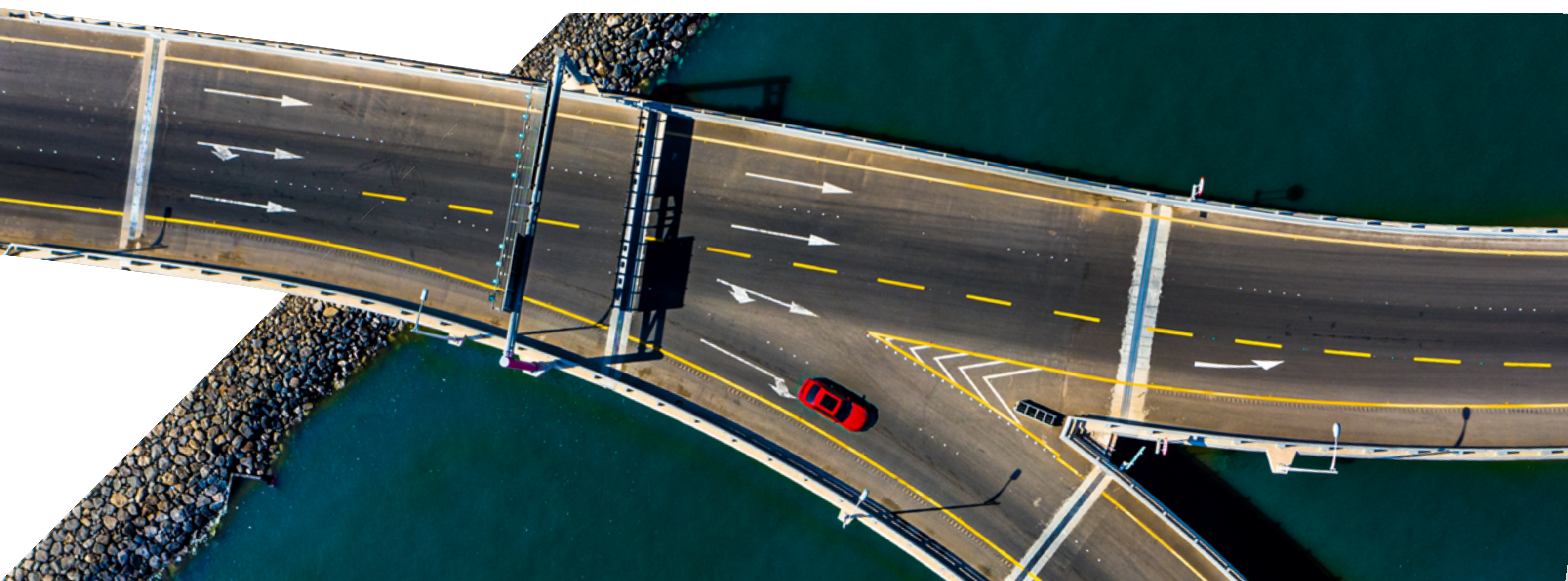
The unpredictable backdrop is one reason why finance leaders feel it is difficult to manage FX risk, as it can be challenging to forecast factors that could trigger any sudden foreign currency moves.

"The foreign exchange markets, at times, are not driven by macroeconomic fundamentals," says Rahul Badhwar, Global Head of Corporate Sales at HSBC. "For example, a record number of nations are going to the polls this year, meaning elections and geopolitics have often been the dominant force driving the direction of currencies. Unlike economic variables such as GDP, interest rates and inflation, geopolitical outcomes can be difficult to forecast. Market volatility driven by these factors thus becomes difficult to predict and manage."

Given this level of uncertainty, one potential solution is to maintain a degree of flexibility when hedging. For example, Badhwar says that if a company hedges 100% of its FX exposure using forwards, this can limit its ability to respond to excessive volatility or tail risk moves.

"For some companies, this lack of flexibility is a non-issue. If that is the case, forwards are fine. However, depending on the sector a company operates in, the need to adjust its end-product pricing, especially when faced with extreme FX volatility, is a must," says Badhwar.

This is where solutions such as FX options that provide flexibility come in. Flexibility can also be obtained by maintaining a hedge ratio below 100%. In the end, what works best for a company will depend upon its risk management objectives and risk appetite.



Respondents are generally optimistic about their company's growth prospects, with 35% anticipating this to result in increasing FX exposures (compared to only 4% expecting a decrease) as they enter new markets or work with new suppliers. More than half of those expecting additional FX exposure attribute it mainly to organic growth, compared to 14% who believe it will be driven by M&A.

As corporate clients expand their search for customers or supply chains into new markets, they are likely to face additional FX risk. One way to limit growing FX risk is to establish new relationships with customers and suppliers that transact in the functional currency of the corporate, says Badhwar.

"However, this is not always possible. It is therefore imperative that companies understand the nuances of the currency markets they are entering with regards to liquidity and capital controls, for example," he says. "Managing FX risk in some emerging markets can be very different from managing a G10 FX exposure."

While FX risk is identified as the most challenging area for corporates, its importance varies across the organisation, with 28% of CFOs and 58% of treasurers putting it as a top three area of attention.

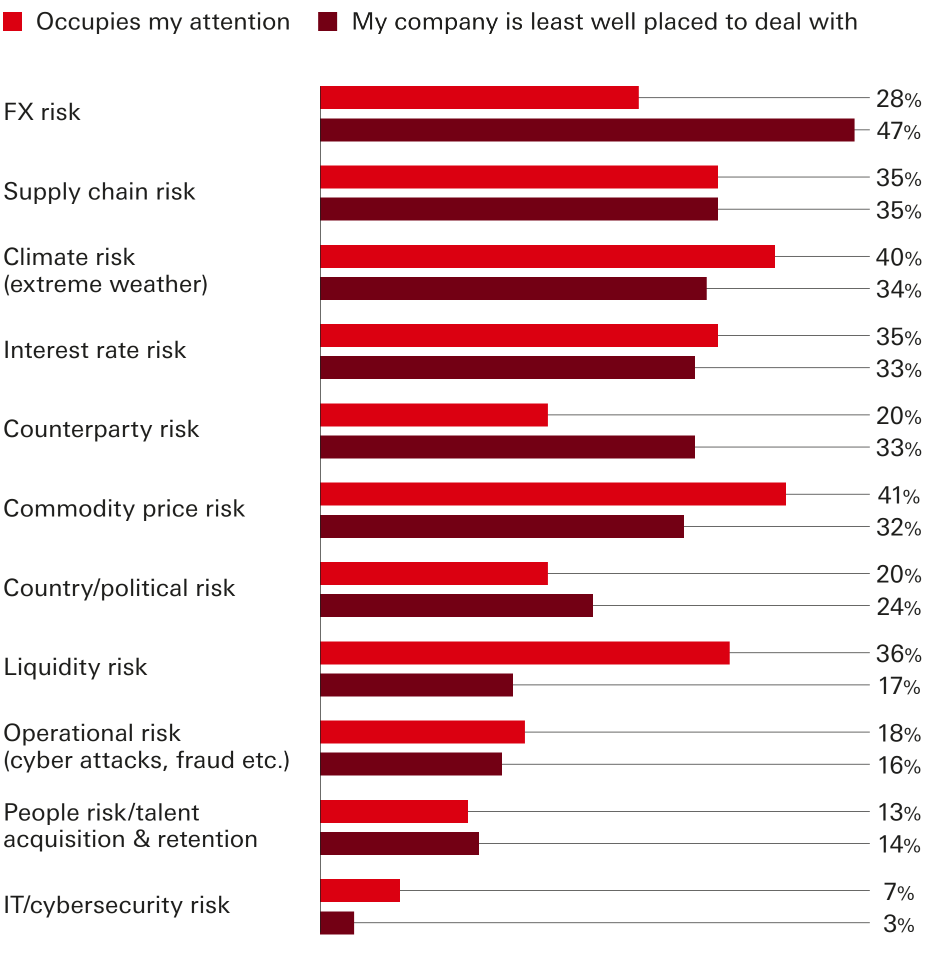
For treasury teams, interest rate risk has posed a renewed challenge. Many businesses are still feeling the scars from the sharp rise in rates in the wake of the pandemic. In the US, for example, the Fed hiked interest rates 11 times between March 2022 and July 2023, increasing the benchmark Fed Funds rate by five percentage points.

"Managing the surge in inflation post-pandemic has not been an easy task. Many central banks have admittedly been a little late in the start of their tightening cycle because they underestimated the resiliency of inflation," says Badhwar. "This also meant that for corporates, managing interest cost and exposure was anything but easy - at times, views about the future direction of rates were nearly as volatile as rates themselves."

With the cost of funding a key focus in the current economic climate, predicting the pace and timing for monetary policy adjustments remains a challenge. For instance, at the start of 2024, the Fed had been expected to deliver three rate cuts over the course of the year and longer-term market interest rates had adjusted with that expectation. By June, that had dwindled to just one anticipated cut (of 0.25% p.a.) before moving up to implied cuts of more than 1.00% in August.

Fig. 1

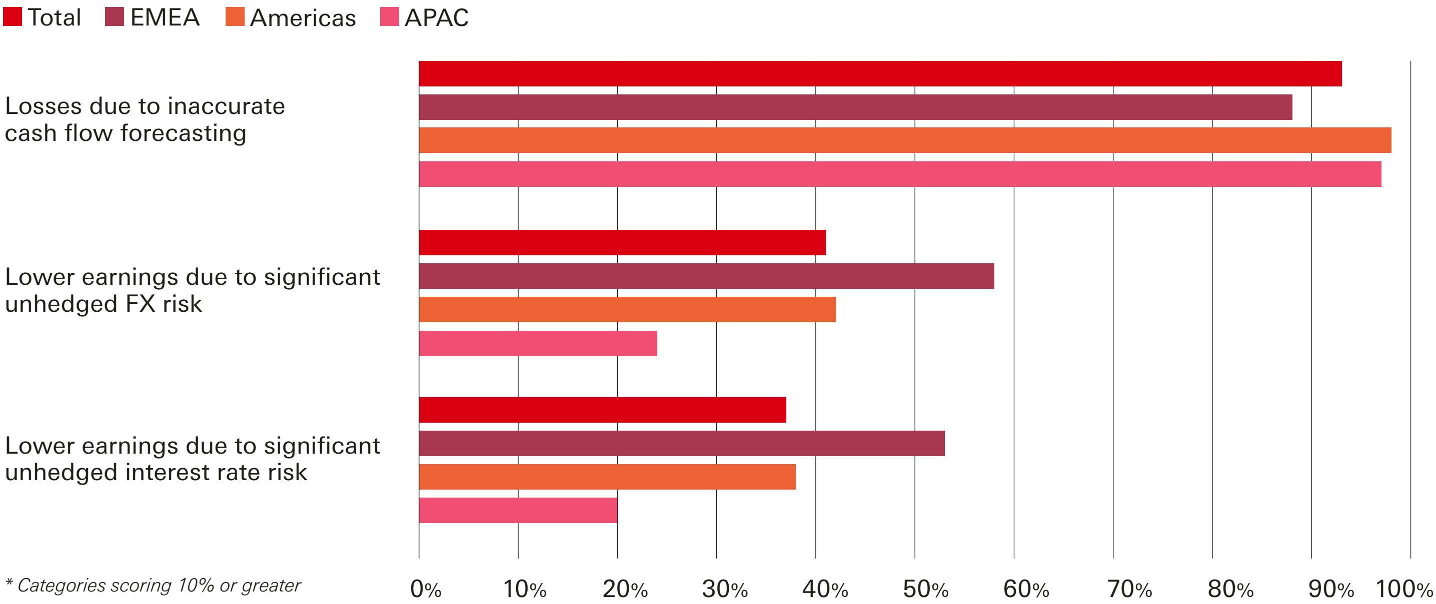
A wide range of risks occupy the attention of finance leaders, with many also unsure of how capable their business is of potentially dealing with them



** Respondents could select up to three choices*

Fig. 2

In the past two years, have you incurred costs in any of the following areas* that you think your treasury department could (or should) have been able to avoid?



** Categories scoring 10% or greater*

> "Managing the surge in inflation post-pandemic has not been an easy task"

"Taking long-term funding and hedging decisions has been anything but a walk in the park for corporates," says Badhwar. "The future outlook for US interest rates, for example, has often seen a substantial change based on a single piece of economic data. With the interest rate cycle now on the verge of a pivot, the key question for corporates is going to be if they are as comfortable swapping into floating as they were into fixed. This is because some corporates see paying fixed rates as a hedge but moving to floating rates as taking a view."

Interest rate risk can be hard to forecast, but there are broader implications when forecasting falls short of reality. For example, 93% of CFOs said that recent losses from inaccurate forecasts resulted in over-borrowing and/or liquidity shortfalls across group entities. There is a view that such a significant impact could have been avoided. Those impacts were felt more frequently in the EMEA region, where companies also flagged unhedged FX risk (58%) and interest rate risk (53%) as areas that hit financial results. By comparison, less than a quarter of APAC-based respondents felt a strong negative impact from unhedged market risks.

Unsurprisingly, more than half of treasurers in EMEA (60%) and 49% overall said the accuracy of underlying data remains the largest challenge for FX cash flow hedging programmes.

"Data visibility is a problem for many companies," says Holger Zeuner, Head of Thought Leadership EMEA within HSBC's Corporate Sales team. "They might not always have timely visibility into where a liquidity shortfall exists across their global entities."

Those liquidity shortfalls may have come from inflationary pressures ramping up costs that could not be fully passed on to customers. Geopolitics may also have added to liquidity challenges for companies operating across multiple markets, such as dealing with unexpected capital controls or other restrictions that may have made it difficult to move cash in and out of those countries.

"Those are examples of fires lighting up that treasuries needed to deal with but where the liquidity management solution wasn't always available as perfectly and as timely as desired," says Zeuner.

3 Shifting risk horizons

While some risks are ever-present, their impact on treasury teams continues to evolve. Take the lingering effects of inflation. Over the past three years, this has led to lower operating profit margins (53%) and higher financing costs (46%) for many companies, while a similar percentage of respondents expect higher financing costs to continue being a factor over the coming three years (48%).

Those higher financing costs are prompting firms to revisit their debt financing mix and interest rate profile. While 37% of CFOs reported an increase in their fixed-rate debt over the past three years, 44% expect to see an increase over the next three years. That is even more prominent for companies in EMEA (54%) and those generating more than $10bn in annual revenue (64%). Most respondents said this expectation is down to the interest rate outlook (56%), though a fifth said the main driver is a different risk capacity, something that was also more prominent for companies in EMEA (28%),

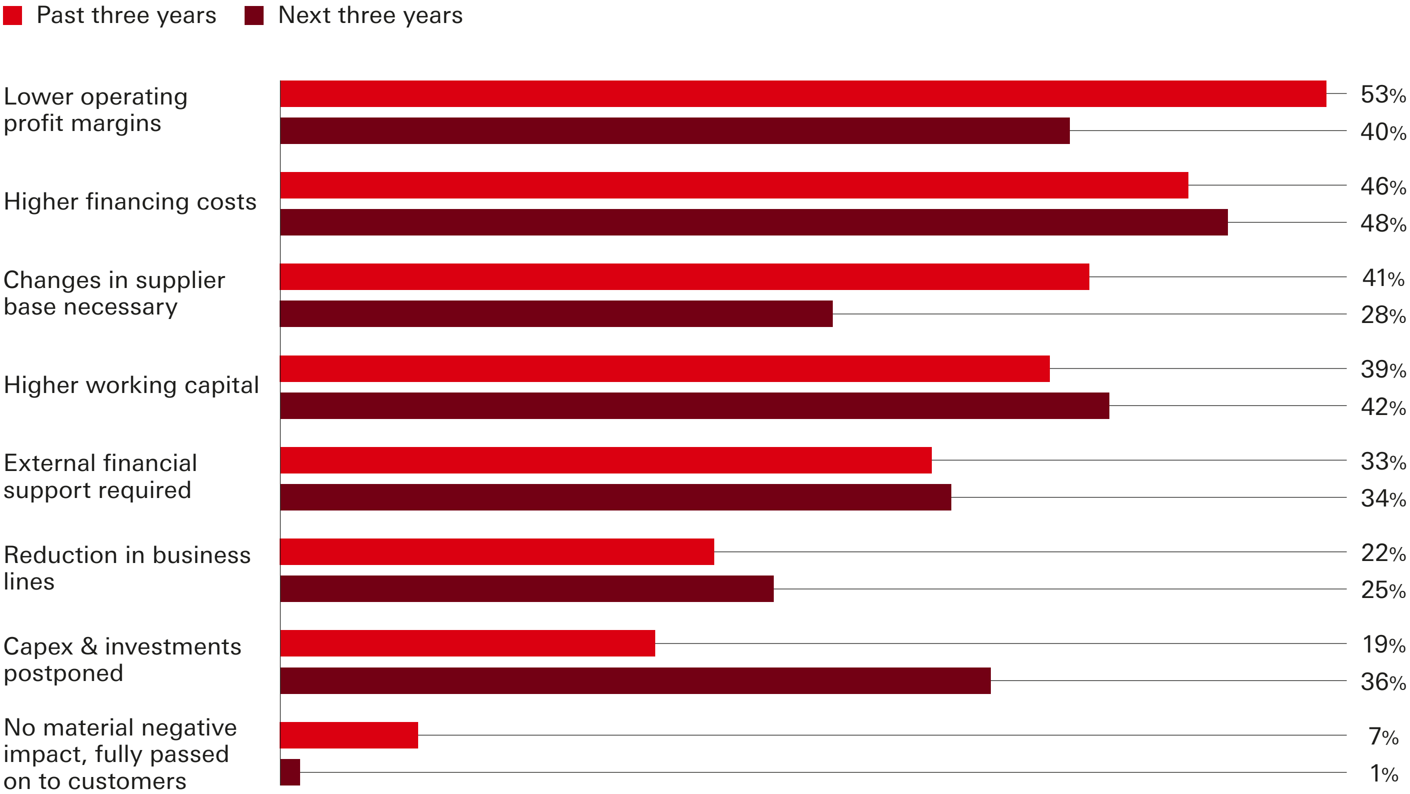
This is likely a result of some treasury risk managers having been caught off guard by the pace of the rate rise. Given the impact this had on financing costs, they don't want to be overexposed to floating-rate debt even with a different market outlook today. A second and perhaps more pertinent reason is that the yield curve is currently inverted in US dollars, euros and other European currencies, making the interest expense on fixed-rate debt lower than on floating-rate debt in the initial interest rate periods.

"Many treasurers are challenged on a near-term cost target as part of their objectives. If you have a five-year loan in dollars, sterling or euros, for the first one-to-two years your interest expense is currently expected to be lower if you pay fixed," says Zeuner. "That resides well with treasury teams' cost objectives given they are asked to reduce costs over the next 12 months or so, and not incentivised to take a view on longer-term interest rate developments."

To better manage interest rate risk, companies should determine a structural target range between fixed and floating-rate debt, taking account

Fig. 3

The main impacts of rising inflation on businesses over the past three years and those expected in the next three years*



** Respondents could select up to three choices*

> "Higher financing costs are prompting firms to revisit their debt financing mix and interest rate profile"

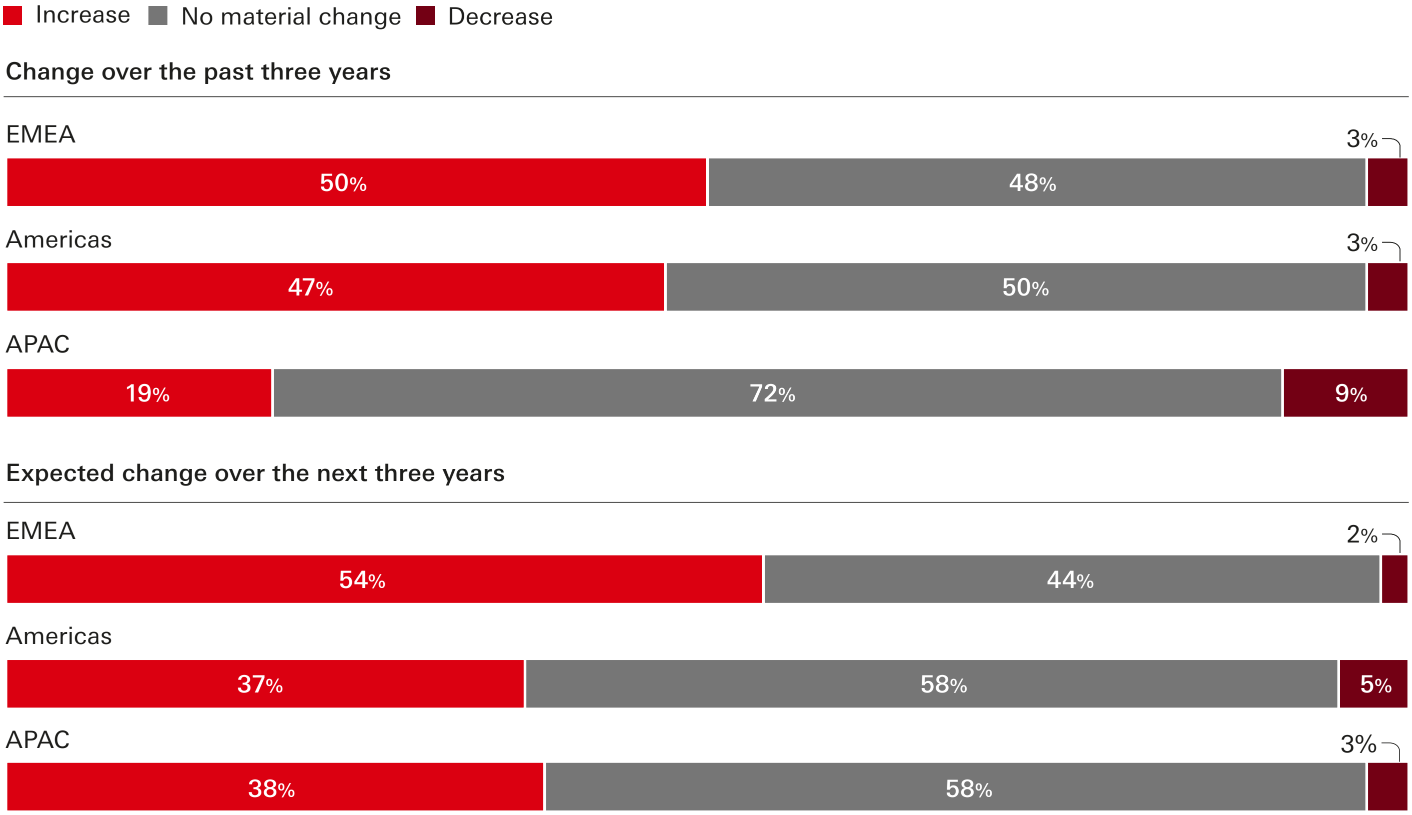
of broader factors such as their business's cyclicality and any strategic cash buffers deposited at floating rates. Maintaining flexibility within this target range allows companies to prepare for worst-case scenarios while also benefiting if rates come down, as many economists currently expect, says Zeuner.

"Adjusting the debt profile now towards a higher long-term target share of floating-rate debt would add a couple of basis points in cost near term. That's the challenge for treasurers in those companies to solve – when do they pull the trigger?" says Zeuner, referring to the inverted yield curve.

Those higher financing costs are having a knock-on impact on other areas of the business, such as capex and other investments. The number of respondents who said they expect to postpone some spending over the next three years jumped to 36% compared to 19% over the past three years. Those plans will likely remain on hold until there is more certainty on the interest rate environment and related cost pressures ease more meaningfully.

Fig. 4

How the proportion of fixed-rate debt has changed for businesses in the past three years – and how finance leaders expect it to change over the next three years



Setting up a future-proof risk management strategy

Rahul Badhwar, Global Head of Corporate Sales, HSBC

"If I were to put myself into the shoes of a corporate looking at risk management, one of the first questions I would ask myself is: 'What risk am I exposed to?' This could be foreign exchange risk, interest rate risk, or commodity risk, for example. The next thing is to quantify the risk to determine its true significance. It is also important to understand the financial metrics impacted by the risk and the appetite of management to digest the impact.

These answers form a basis for the development of a risk management policy. There should be a clear understanding that when choosing how to hedge a risk, it is often about risk vs reward. There are various solutions to hedge an exposure, but deciding which is best depends upon the risk appetite of key stakeholders. The central truth about hedging solutions, more often than not, is that a higher reward goes hand in hand with higher risk or cost.

When it comes to risk management policies, it is also important to have consistency. It is difficult to achieve a one-size-fits-all outcome because there will be scenarios when the risk management policy may not work. Evaluating a policy makes sense, but frequently changing a policy based on hindsight might not succeed: remember, markets move in cycles.

In the end, a clear risk management policy with clear objectives, backed by stakeholders, is often the best way to deal with the vagaries of the market and avoid nasty surprises."

4 The evolution of treasury as strategic advisors

As the treasury function expands and becomes an increasingly important strategic partner to the wider business, treasurers have an opportunity to redefine what 'best in class' looks like. As many as 50% of CFOs and finance leaders said they rate their treasury department as best in class for liquidity management, followed by interest rate risk management (36%) and group financing (35%). Liquidity management competency was most pronounced in APAC, where 70% of respondents ranked their teams as best in class.

"Liquidity management is the bread and butter of the treasury, so that's a key area you need to be good in," says Zeuner. "It's also an area where you find a high degree of automation, so there is a pretty well-established toolbox available to manage liquidity across various entities."

On average, finance leaders believe their treasury is best in class in just over three areas while highlighting room for improvement in just under three. Respondents ranked working capital utilisation as the area where they are most frequently seeking improvement (43%), with only 12% pointing to liquidity management. The relatively small proportion of respondents highlighting room for improvement in liquidity management suggests that those losses due to overborrowing and/or liquidity shortfalls discussed earlier are being attributed to data inaccuracies rather than the treasurer's skillset and toolbox.

"I've yet to meet a company that is maximising value from its working capital – whether it's the payable side, receivable side or inventory side, there's inevitably value being left on the table," says Vivek Ramachandran, Head of Global Trade Solutions at HSBC. "What's really changed now is working capital is no longer just the treasurer's remit, it's also on the CFO's agenda.

Fig. 5

The areas of their treasury department that finance leaders rate as 'best in class' and those where they would most like to see improvements

That's probably what's getting companies to ensure they think about working capital from an integrated end-to-end perspective and look at structured solutions to solve that challenge."

FX risk management was seen as best in class by just one in five respondents, showing no improvement compared to 2021. That is likely due to the challenges of managing FX risk and the broader data visibility issues discussed previously.

"Treasury can only act on the underlying data when it comes to FX. If that exposure is on the other side of the world and the data coming in is delayed or imperfect, then risk management can't really correct such shortcomings," says Zeuner. "FX is a risk that can never be fully avoided within multinational corporates, so there will always be some FX impact: the more markets move, the larger that impact might be."

There is also a continuing trend towards more centralised decision-making when it comes to hedging (88% vs. 82% in 2021), suggesting a move towards greater harmonisation of data processes and IT systems across a company's different entities. This enables more consistent policies and increased automation. There has been a particular impact on larger businesses: 68% of organisations with over $20bn in annual revenues have set up their own in-house banks to manage main financial processes globally within a single entity. These structures bring two benefits, says Zeuner, enabling businesses to reduce costs and manage exposures across different group entities more efficiently.

Centralised decision-making can also provide more strategic guidance to the business. Most respondents (68%) agree that their treasury function already plays a key role in strategic decisions, up from 41% three years ago.

"Strong communication within the organisation is always required to identify and take timely actions"

Fig. 6

Finance leaders' perceptions of the treasury function

68% agree that their treasury function plays a key role in strategic decisions (inc.M&A and capital allocation)

61% have found new ways to leverage the analytical skills of their treasury department in the past three years

57% believe their treasury team has the required skills to play a highly strategic role in their business

53% are using or considering outsourcing to enhance the profile and efficiency of their treasury

41% say the responsibilities of their treasury have become broader in the past three years

Fig. 7

The current efficacy of communications between the treasury and the C-suite

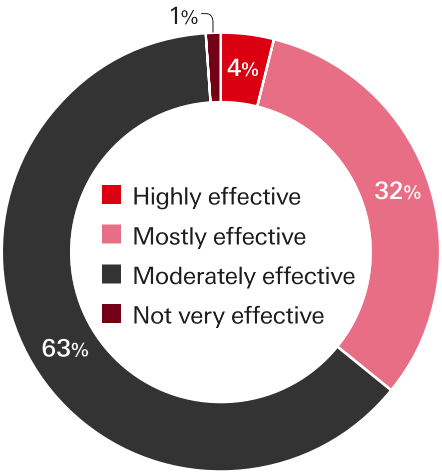
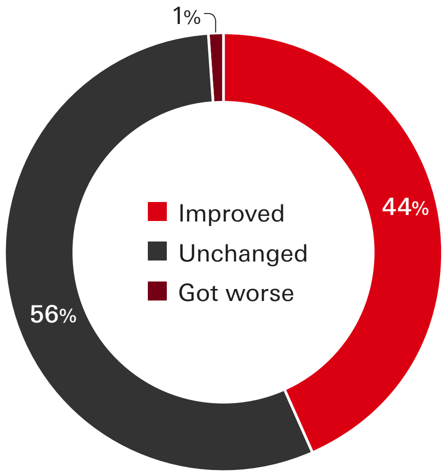


Fig. 8

How communication between the C-suite and treasury has changed over the past three years



A key driver of this positive change is the development in APAC, where only 14% were deemed a key partner in strategic decision-making three years ago, compared to 78% today.

Internal communication is a persistent challenge. Almost two thirds of respondents believe communication between treasury teams and the C-suite is only moderately effective (63%), while just 4% view it as highly effective. The direction of travel is positive, at least. Some 44% of respondents believe communication has improved over the past three years, while only 1% believe it has declined. This is more pronounced at companies with higher revenues, with 59% saying dialogue has improved compared to 31% at smaller businesses.

"One reason that larger companies tend to be more efficient with communication is that they have more resources and usually more integrated systems," says Zeuner.

On top of this, it could be that smaller businesses just haven't had the same pressing or frequent need to communicate with the C-suite, as their exposure to various crises and markets has been more limited. Highly effective communication, however, is vital to creating a best-in-class treasury function that can deliver on expectations of becoming a more strategic partner.

"There needs to be a strong feedback loop between treasury and the underlying business units. Effective risk management in treasury relies on understanding and thinking a step ahead of what could happen. For instance, considering the impact that supply chain shortages in certain markets have on financial risk," says Zeuner. "Strong communication within the organisation is always required to identify and take timely actions - and this is what we see in those teams that are best in class and leading on risk."

5 Greater resilience fuels growth optimism

Senior finance leaders are optimistic about their company's growth prospects, despite the challenging risk landscape. Perhaps surprisingly, 54% of respondents flagged Europe as one of their company's two main regions with revenue growth potential over the next three years, followed by the wider APAC region (excluding China and the Association of South-East Asian Nations [ASEAN]) (42%) and their respective domestic market (32%).

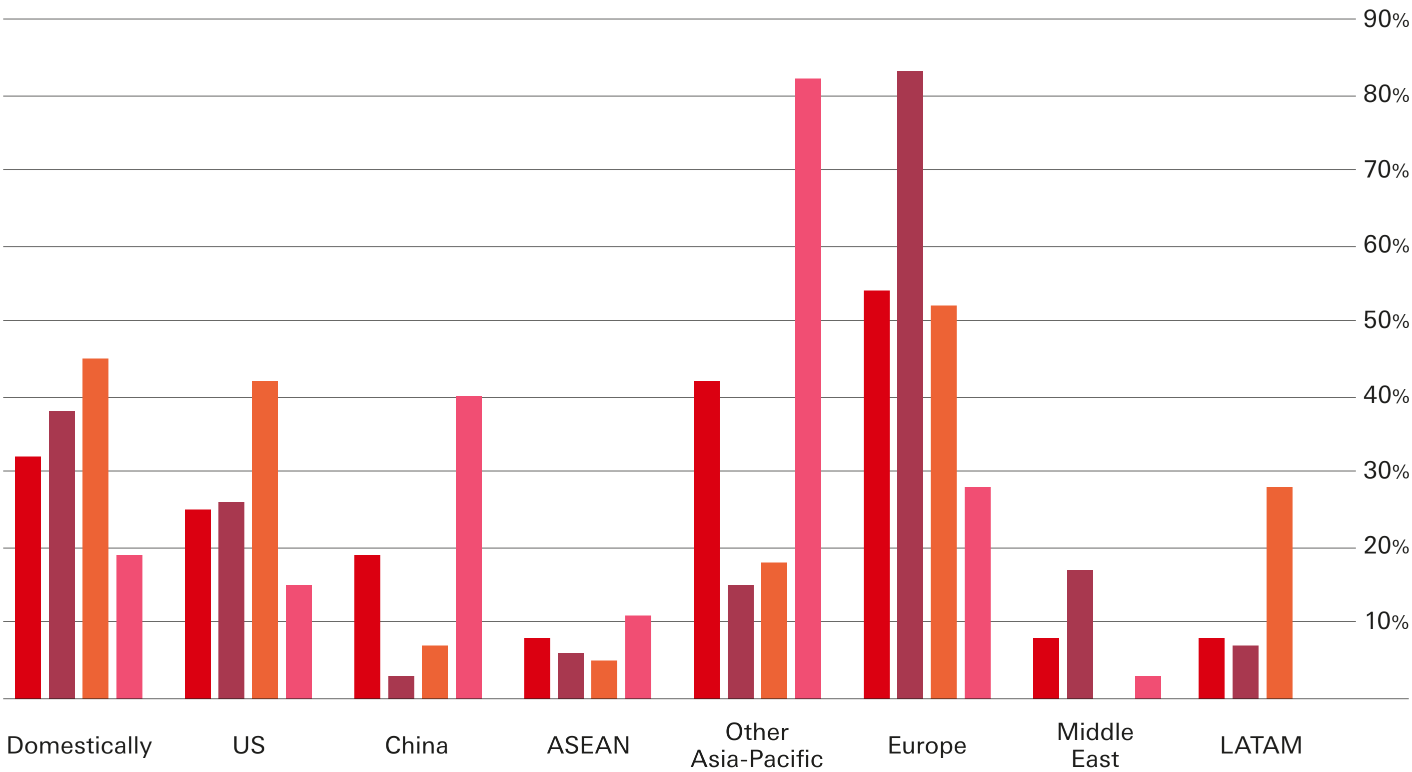
While respondents in EMEA were most likely to pick Europe (83%) and respondents in APAC were most likely to pick Asia-Pacific excluding China and ASEAN (82%), 52% of respondents in the Americas also rated Europe as having larger potential over the next three years. This is a change from previous survey results where Europe was only seen as a key growth market by 22% of American companies: it raises the prospect of a resurgent transatlantic trade corridor.

"This could be an indication of 'friend-shoring', or greater trade between allies," says Shanella Rajanayagam, Senior Trade Economist within HSBC Global Research.

Fig. 9

The regions and countries with the the largest revenue growth potential over the next three years

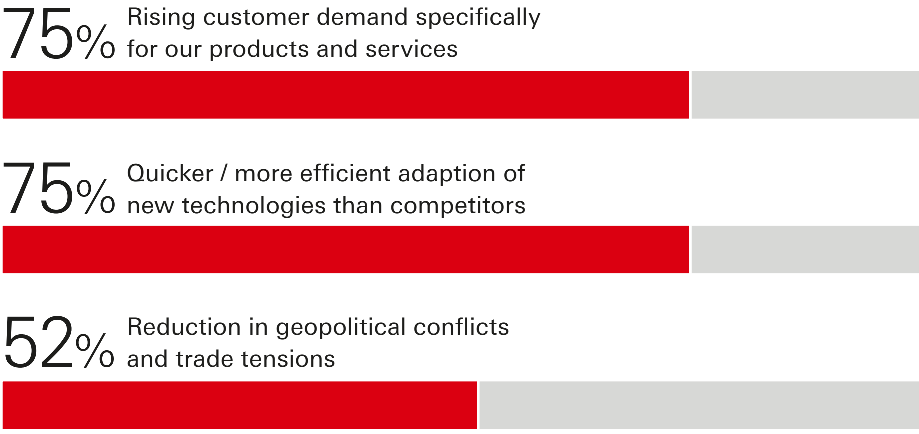
Total EMEA Americas APAC



** Respondents could select two choices*

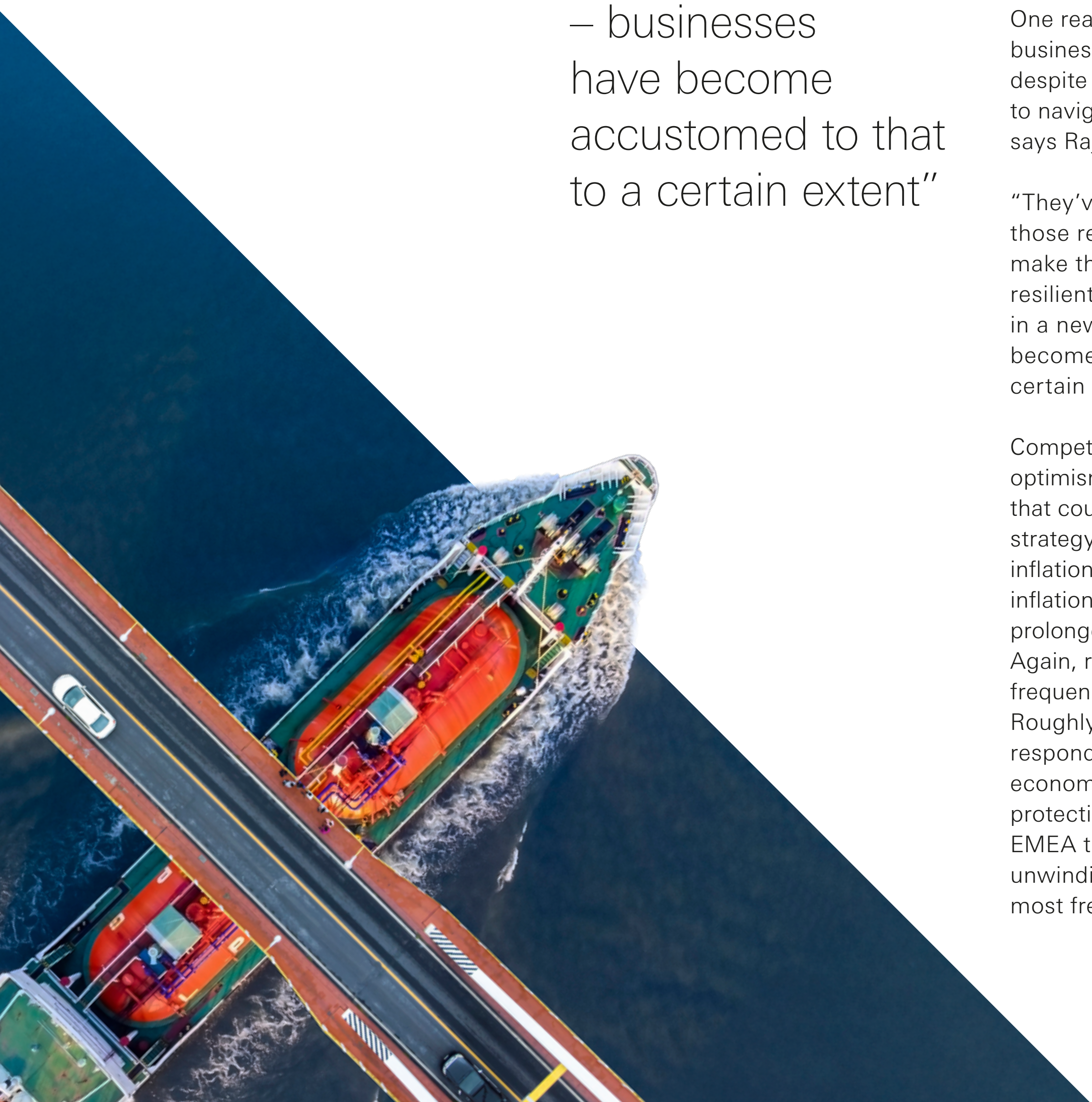
Fig. 10

Top three factors* most important to growing company earnings over the next three years



** Categories scoring 50% or greater*

"We're operating in a new world – businesses have become accustomed to that to a certain extent"



Three in four respondents named both rising customer demands and the efficient adoption of new technologies as the most important factors to the growth of their business in the next three years. This was followed by a further 52% of respondents hoping for growth to be spurred by a reduction in geopolitical conflicts and trade tensions.

"On the trade front, we see geopolitical tensions as the key downside risk. We have been flagging this since the beginning of this year, not only the risk that such tensions persist, but that they could escalate," says Rajanayagam.

Despite this possibility, respondents are fairly sanguine about the prospects of escalating tensions between the US and China or the EU and China. Only about a fifth of respondents cited a hardening of trade tensions between those regions as a major concern. One reason for this optimism is that businesses have proven resilient despite the challenges they have had to navigate over the past few years, says Rajanayagam.

"They've used their learnings from those recent disruptive events to make their supply chains a bit more resilient," she says. "We're operating in a new world - businesses have become accustomed to that to a certain extent."

Competing with the revenue growth optimism are several macro concerns that could impact the financing strategy. Top of that list is higher inflation or a longer period of high inflation (58%), followed by fears of a prolonged economic downturn (55%). Again, regional differences in the frequency of other factors are notable. Roughly three in four APAC respondents picked inflation and economic downturn, with a rise of protectionism a distant third at 33%. In EMEA the latter rises to 44%, with an unwinding of asset price bubbles (49%) most frequently chosen.

The rise of protectionism is less of a concern than persistent inflation, but remains a significant risk to global trade and could derail revenue growth prospects.

"There has been a step change since the last US administration, with a number of other economies following suit with their own protectionist policies," says Rajanayagam. "The EU, for example, has taken measures to strengthen its trade defence toolkit. The World Trade Organization's appeals court isn't functioning. It's almost as if countries are free to levy as much protectionism as they want without too much recourse."

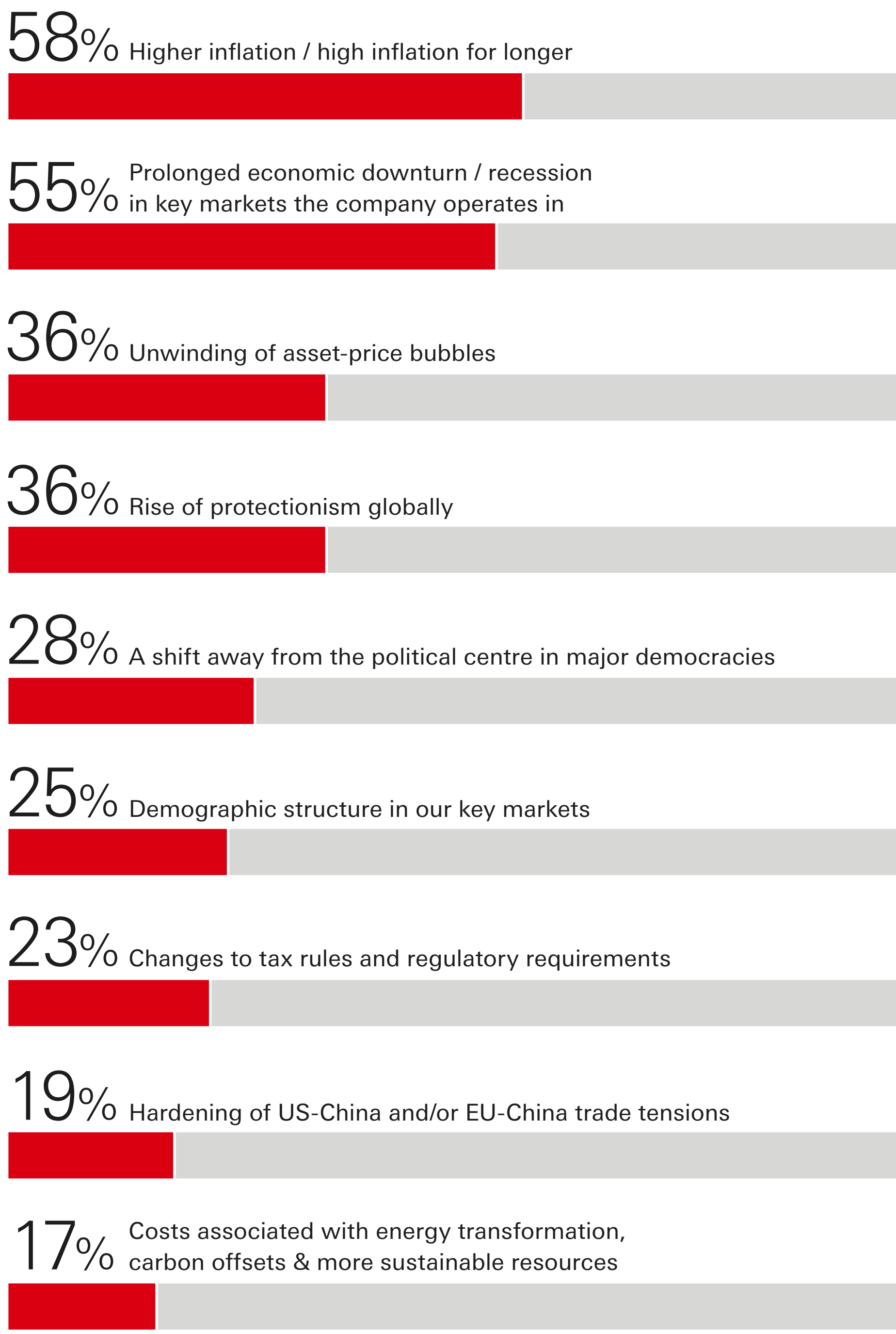
Corporate profits may also be shaped by emerging themes, both positive and negative. For example, most respondents (61%) believe AI will benefit their company's profitability over the next three years, while only 17% perceive it to be a challenge for profitability.

However, there is far more uncertainty about the impact of other future trends on companies' bottom line. While the development of emerging economies is seen as a slight net positive (46% expecting a benefit compared to 42% who think it will challenge their profitability), process automation is viewed as a net negative (35% vs 53%), as well as urbanisation and megacities (20% vs 33%) and remote and hybrid working (24% vs 32%). Fittingly, the transition to net zero balances out to 0% (30% say it will be beneficial to their profitability and 30% say it will be challenging).

By plugging into the drivers of potential growth, treasury teams can provide more effective advice that can help deliver on the company's wider strategic goals.

Fig. 11

Top macro concerns in relation to financial strategies



6 Supply chain management and the impact of ESG

ESG and supply chain risk are high up on the treasury risk management agenda amid growing scrutiny and expanding regulations. Faced with the prospect of financial penalties and associated reputational damage, some businesses are taking action.

Almost a third of companies (32%) have already incorporated ESG guidelines and policies into their supply chain and another 40% into sales logistics.

This process typically occurs in three stages, says Vivek Ramachandran. At a minimum, companies are requiring suppliers to share their ESG credentials. Some are then creating scorecards and setting targets for suppliers to meet certain requirements. And the most advanced companies on this journey are incentivising suppliers with either preferential financing terms or a commitment to place more orders, says Ramachandran, and some are

"Efforts to cut costs have also made supply chains more complex and reduced transparency"

even cutting ties if suppliers fail to meet those standards.

"But as the data shows, only a third of respondents are doing any of these three things, so there's a long way to go," he adds.

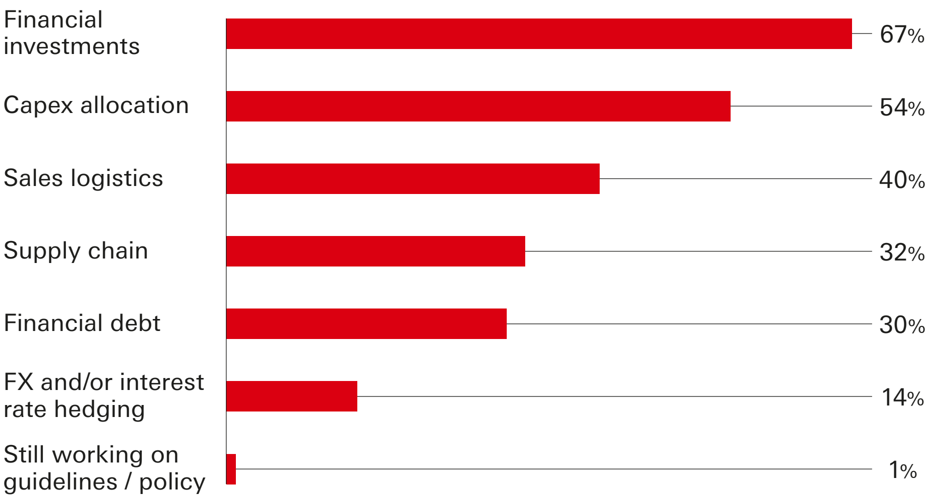
Why are many organisations struggling with this process? Perhaps the answer is historical. For many decades, supply chains have been solely focused on minimising costs and procuring products at the cheapest possible price, says Ramachandran.

Those efforts to cut costs have also made supply chains more complex and reduced transparency. For instance, 99% of respondents said they are somewhat (69%) or very (30%) concerned about ESG visibility across their supply chains, with 56% very concerned about their ability to fulfil ESG reporting requirements.

The level of concern tends to rise with a company's revenue size and the stringency of regulations in their location. Respondents in EMEA (of which half are based in the EU, where ESG rules are most advanced) were to a larger degree very concerned about reporting requirements (68% compared to 39% in APAC).

Fig. 12

The business areas in which ESG guidelines and policies have already been incorporated



Practical steps to reducing supply chain risk

"There are three things that companies should do to assess and manage supply chain risk. First, you need to start with transparency and building the information about who is in each supply chain.

The second point is not to treat suppliers purely as vendors but to recognise them as strategic relationships. Done right, you can then influence supplier behaviour. For example, many of the large anchor buyers are now putting in place incentives in their supply chain finance programmes as well as helping suppliers mitigate risk and get stronger, therefore meeting multiple strategic objectives at the same time.

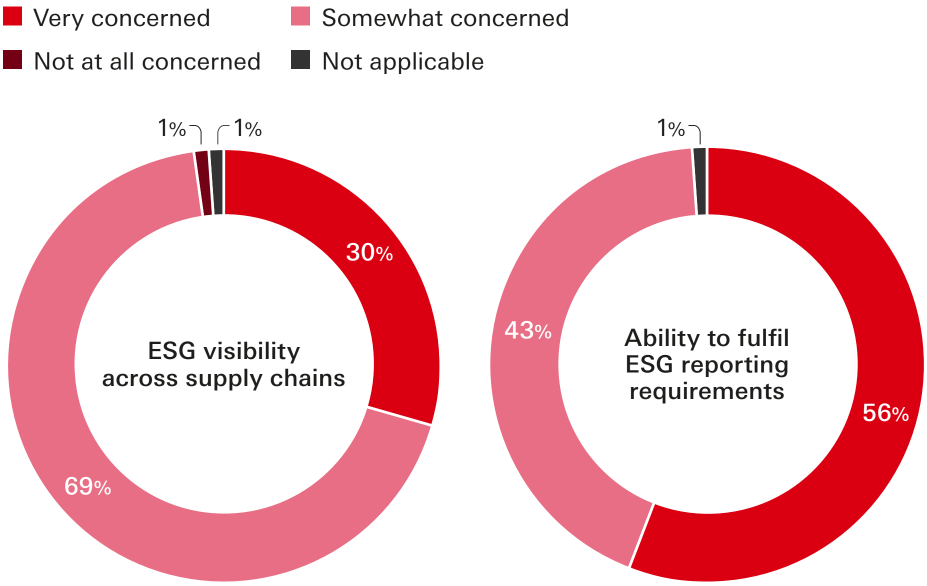
The third element is to look at payables, receivables and inventory as a continuum of options that can both drive sales and influence behaviours. You've got more tools at your disposal than you realise.

Getting started can be daunting, but once you embark on this journey, you'll realise the benefits are relatively quick to reap. Don't dismiss it as too difficult or think it can wait just because it's not an urgent issue. The next three to five years are the time to act, not just think about it."

Vivek Ramachandran, Head of Global Trade Solutions, HSBC

Fig. 13

Levels of concern around ESG visibility and reporting



"Companies willing to take steps towards more accountability for practices through their supply chain is potentially encouraging from an ESG perspective"

"It's fair to say the average company has minimal insight into who's in their supply chain beyond their tier one suppliers," says Ramachandran. "If you take the retail apparel sector as an example, the average brand will contract with a manufacturer and may have visibility into the yarn supplier or the fabric mill, but beyond that it is very limited, so transparency is the number one challenge."

The fact that suppliers cater to multiple buyers means there are often no common standards. It is also costly to implement and adhere to ESG requirements, which means the project can get sidelined if there is high pressure on short-term costs. This is an area where banks and financial partners are expected to add value: there has been a significant increase in businesses looking into financial support solutions for their suppliers (23% over the next three years compared to just 3% over the last three years).

These concerns are manifesting in the 'nearshoring' trend, which is expected to continue. Over the next three years, 45% of respondents said they expect to work with more local suppliers, similar to the 43% who have already pursued such efforts over the past three years. Additionally, 27% expect that ESG aspects will require them to cancel some supplier contracts in the future compared to 19% who have already acted on this front in the past three years.

"We went through a period during Covid where supply chain resilience was really put to the test. It takes years to build up a trusted supplier relationship, so making sure that you don't have too much concentration risk and you have a resilient supply chain can be at odds with changing suppliers due to ESG scorecards in some cases", says Ramachandran. "That's the trade-off that companies are working through, but the fact you now have companies willing to take steps towards more accountability for practices through their supply chain is potentially encouraging from an ESG perspective."

ESG is also having an impact on companies' own debt instruments. In 2021, 59% of companies said that less than 10% of their gross debt was linked to ESG criteria. But for 41% of respondents in the latest survey, more than 30% of their gross debt has ESG features.

7

AI, innovation and the treasury of tomorrow

The advance of emerging technologies such as AI has the potential to reshape the treasury function, while underpinning treasury's shift into a strategic business partner.

Over the next three years, finance leaders expect AI tools to become increasingly integral to their risk management decision-making process, with 61% saying it is expected to be very or extremely useful compared to 38% today. Larger companies with more than $10bn in revenues have already implemented some form of AI more widely than their smaller counterparts.

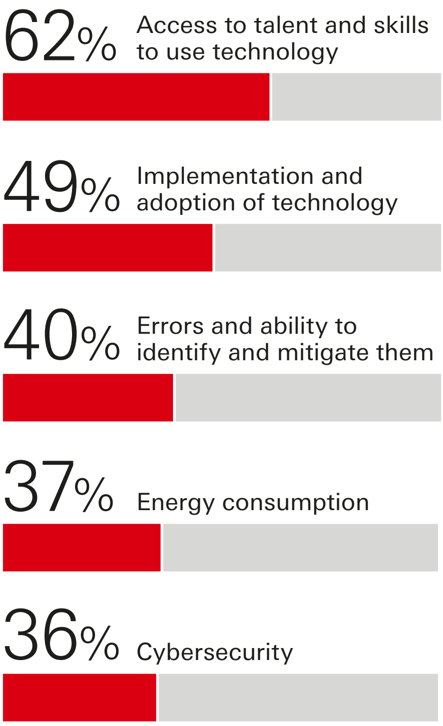
We asked treasury teams to outline three areas where they expect to see the main use cases of AI. Supporting data collection and analysis was picked by 82% of respondents, with another 52% expecting the technology to improve related cash flow forecasting. Fraud detection (38%) is also mentioned frequently. This shows the high expectations treasurers are putting on new technology to strengthen their efficiency in areas where shortcomings have been acknowledged.

While many organisations are using AI and machine learning tools already, the advent of generative AI has the potential to be transformative for treasury departments. Currently, many companies are treating AI adoption in the same way as any large-scale IT project, in part because they are concerned about unknown risks. This approach is potentially restrictive and could limit innovation. Instead, by giving workers access to generative AI tools, companies could stumble upon many use cases that would otherwise remain unidentified, says Mark McDonald, Head of Data Science and Analytics within HSBC's Global Research team.

"Rather than having one monolithic AI project that's going to completely transform your business, there will probably be at least as big and maybe even a bigger aggregate impact from the thousands and thousands of little improvements that people are able to achieve. It's only really by letting your workforce have access to these tools that you realise those benefits," he says.

Fig. 14

The top five challenges and risks around adopting newer technologies in the finance department*



** Respondents could select up to three choices*

However, organisations face a number of challenges on this journey. Respondents said the main perceived risk when adopting new technologies such as AI is access to talent and skills to use the technology (62%), followed by implementation and adoption of technology (49%), the risk of errors and the ability to identify and mitigate them (40%), as well as energy consumption (37%) and cybersecurity (36%). Somewhat surprisingly, senior finance leaders were rarely concerned about funding (5%) and subsequent return-on-investment (ROI) measures for AI projects (3%).

However, concerns about a lack of talent might well be overstated.

“This might be more of a perception than reality because while it’s unambiguously true that there is intense demand for AI talent at companies that are building new cutting-edge AI models, when it comes to applying existing generative AI models, this technology is already ready to use,” says McDonald. “You hear about a war for talent, but that’s probably not a war that most people are involved in.”

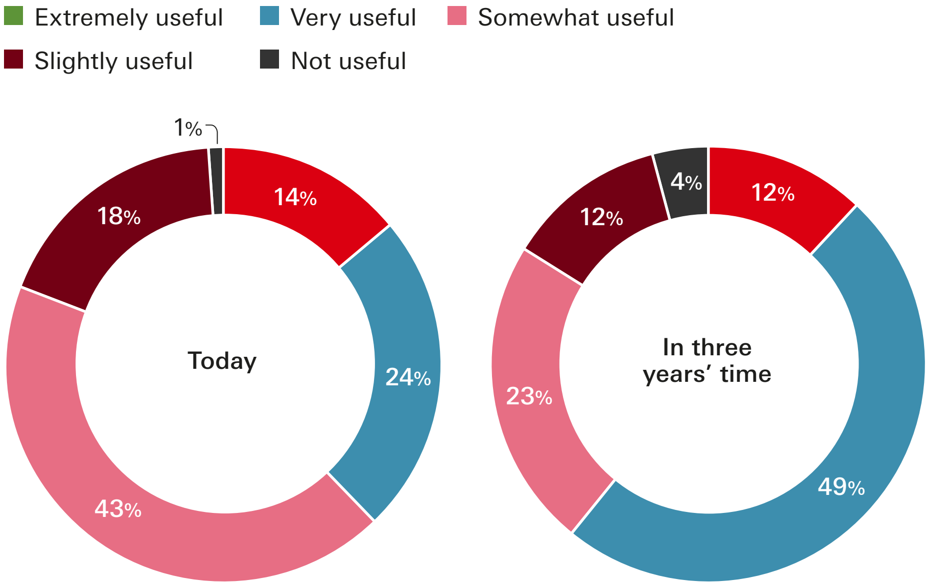
While ‘hallucination’ risks from unidentified and uncontrolled model errors are a legitimate concern, companies can mitigate this by using AI as part of a process rather than relying on it for a definitive final answer.

“My analogy for how people should think about these models is like a clever, hardworking intern,” says McDonald. “If you ask an intern to find something out for you, you wouldn’t just take what they gave you at face value, you would sanity check it. People need to be in the same mindset when interacting with these AI tools.”

Treasury teams also shouldn’t view AI as a threat: it is unlikely that you could automate someone’s entire job unless that person had a very narrow role, says McDonald. The more likely outcome is that AI will help automate some specific tasks that effectively free up time to focus on areas where AI can’t help, which tend to be the higher value work that can have more of an impact for a company, he says.

Fig. 15

Finance leaders are already finding uses for AI but expect it to become even more useful for risk management decisions in the coming years



The survey data backs this up. Most respondents expect the integration of AI into their treasury job to be supplementary rather than disruptive: 81% feel AI can only replace less than 25% of their work over the next five years.

What areas are treasury departments considering for tech and automation investment? There are different priorities depending on the region. In EMEA, group-wide cash flow forecasting is most frequently picked (47%), followed by loan processing (43%). For APAC, 62% plan to look into their credit risk management and 57% each into treasury reporting and analytics as well as cash pooling and intra-group funding. For respondents based in the Americas, reporting and analytics support is identified most frequently as a priority (57%).

Of course, companies may decline to invest in this technology. This decision very likely won't prevent treasurers from doing their jobs, but could increasingly create frustration for team members.

"If you don't invest in this, then eventually all your systems are going to be archaic. Staff are going to be annoyed because the tools that they're using at work are going to be worse than the things that they can use at home," says McDonald. "It would be like a company not having computers that were connected to the internet – people would just think that was absurd."

It is unknown how AI will develop. But even if AI models don't improve, the impact of AI on the treasury function is likely to be significant.

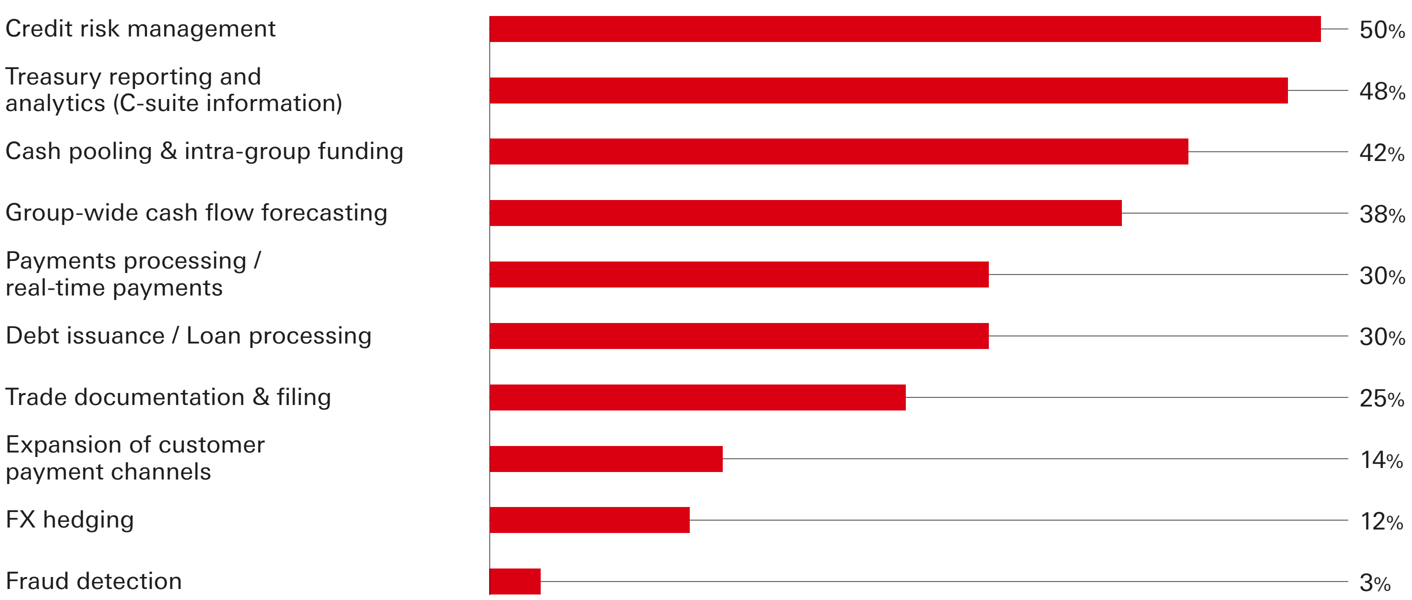
"There are still conservatively about five or ten years of productivity improvements just from people working out the most effective use of this technology," says McDonald. "We saw a similar thing with the internet – people are experimenting and eventually they will coalesce on what works."

If treasury teams give team members the tools – and the time – they need to experiment and unlock new ways of working, it could transform how they manage risk and what the treasury of tomorrow will look like.

> "Even if AI models don't improve, the impact of AI on the treasury function is likely to be significant"

Fig. 16

The priority areas for technology investment / automation in the treasury department*



** Respondents were asked to select their top three areas for investment*

Conclusion

The risk management landscape is more turbulent than ever. Treasury teams must balance multiple threats and challenges and find ways to thrive in times of persistent and overlapping crises. Traditional approaches to mitigating risk in this environment are no longer sufficient. Treasury teams must continue the journey laid out in our 2018 and 2021 survey editions. They should adopt and implement a strategic approach to financial risk management that aligns with the company's risk appetite and ultimately contributes further value to the wider business.

Here are six key takeaways to help finance leaders navigate the risk landscape and build a treasury function that is seen as best in class by stakeholders and peers.

Flexibility is key
Risk events are not only becoming more frequent, but they are often hard to predict, which can make it challenging for treasury teams to manage FX and other finance-related issues. By adopting a more agile stance, treasury teams will have more elasticity to react to unexpected events, not only helping them to minimise losses but also giving them more strategic room to manoeuvre and emerge quicker and stronger from a storm.

Find the right debt mix
Many finance leaders expect higher financing costs to persist for the foreseeable future. With the interest rate environment as uncertain as ever, the path to lower financing costs is unlikely to be a straight line. Ensuring companies have set the right long-term target balance between fixed and floating and being agile to react in either direction is a vital area where treasury teams can add value.

Build and keep strong feedback loops
Communication between treasury and the rest of the business is fundamental for a best-in-class treasury function. Instead of merely reacting to events after the fact, maintaining open communication lines with different business units can help treasurers anticipate potential risks and plan accordingly to avoid or minimise any disruption.

Supply chains and sustainability
Evolving ESG regulations globally are putting greater focus on supply chains and increasing potential financial risks for companies. Treasury teams need to take active steps to improve visibility into those supply chains. Together with banks, they need to introduce incentives to positively influence supplier sustainability and behaviour.

Optimise working capital
With many treasurers recognising a need to improve working capital utilisation – in part because it is now higher up the CFO agenda – adopting a more holistic approach to working capital management is vital. This means viewing payables, receivables and inventory together and building a strategy around that.

Embracing AI and innovation
The rapid advance of generative AI is opening up new opportunities for innovation and changing the way treasury teams work. By integrating AI tools into workflows, companies can find new use cases and streamline previously manual processes, freeing up treasury teams' time to focus on higher-value activities that deliver on the goal of becoming a more strategic partner to the business.

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