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## **The CFOs Are Coming**

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Among the torrent of discoveries thrown up by the near-death experience of so many Asian banks at the end of the 1990s was the realization that bankers were not very good financial managers. Banks were full of professionals with claimed expertise in banking products and services, including collecting information, reporting systems and disclosure. And while their focus was theoretically on the client, the reality was often different.

More significantly, many Asian banks were not focused on profits. They were in the business of making money. But they enjoyed cartel protection, as in Hong Kong, or “nation-building” roles, as was the case across most of Southeast Asia. Some serviced only “preferred customers,” financing pet projects of owners’ friends and relatives. Power, connections and influence were as important as the bottom line.

No longer. Both internally and externally, banks operate in a new landscape. With it has come a notion of creating the post of chief finance officer or CFO. The CFO’s task is to ask the questions of the bank that the bank asks of its shareholders and customers. The CFO focuses on the real bottom line.

Getting a grip on financial management of a bank means a CFO’s purview can extend over half a dozen areas: treasury; credit policy; financial operations; external audiences; financial reporting; and risk management. Some banks already have personnel responsible for these areas, but normally such responsibilities are scattered, especially in Japanese institutions. And some areas are not covered at all.

In most Asian banks, a treasurer is typically appointed to take care of short-term liquidity management – the day-to-day cash management process. Cash management has typically meant maintaining high-liquidity positions through investing in short-term, low-risk assets. International liquidity, including funding by raising bonds, has been the job

of an international banking department where the foreign currency is used and staff have the best foreign-language skills.

Asian banks often have someone whose job it is to consider credit-risk policy, which includes financial reporting for either internal purposes or to meet the demands of external regulators. The banking authorities have tended to see their role as making sure that banks under their jurisdiction have sufficient capital reserves. To satisfy regulators, there is normally someone responsible for financial operations – general ledgers, accounts payables, and profit and loss statements.

A person to address the needs of shareholders, someone truly responsible for assessing the overall risks faced by the bank, is what is really needed. Without a person responsible for managing capital and return-on-equity, it’s easy to see why, in the past, banks have not been run for the benefit of shareholders.

Enter the CFO. At the heart of the CFO’s job is management of shareholders’ funds, the bank’s equity. A CFO, therefore, must be aware of the full range of risks – credit, economic, social, moral and so on – to which the institution is exposing its capital. After all, the proper business of banks is not to avoid risks, but to properly identify and manage them in a rational way, and to earn proper returns for shareholders and depositors that are commensurate with those various levels of risk.

This overarching risk-management role requires the structures, systems and tools to assess and measure what a bank is actually doing in each of its businesses and with each of its customers. In short, one is back to the much-discussed issues of transparency, information and disclosure – the lack of which undermined so many banks during the financial turmoil that washed across Asia in 1997.

Creating CFO positions is therefore intimately related to the general restructuring and recapitalization of Asia’s banking sector. The driving force is survival. Liberalization, new competitors in the form of foreign banks and new players such as insurance companies, plus the advent of the Internet, all threaten unwary local banks. Pressure for change is

also coming from other forces. Shareholders and stock markets want more information from their banks – not just more data, but also more about the processes banks are using. The more complex relationships common between banks and banking authorities in the West are appearing in Asia.

A CFO is the logical nexus to drive the internal changes a bank needs to make. What does this mean in practice? First and foremost, this means spearheading the building of the complex system and processes needed in a modern bank. This involves using the large-scale enterprise resource planning technology packages common in the industry. With ERP and proper reporting systems, bankers can acquire the data they need, and “slice and dice” the information to tease out meaningful numbers, for example, by customer, product, business line or branch. This is phase one of a CFO’s job description.

Phase two is turning accurate numbers into the basis for knowledge-based decision. Techniques are available to measure, assess and manage profit and risk. One technique known as risk-adjusted performance translates risk into capital allocation. The greater the risk, the more capital that has to be set aside to cushion possible losses due to that risk.

A good CFO needs top management skills and the ability to create and implement the changes Asian banks need. The pool for such talent will be found in industry and commerce and among younger Asian bankers trained in cutting-edge banks and financial institutions in Europe and America.

The West took two decades to recognize the need for CFOs. Asia’s banks don’t have the luxury for such a long learning curve. We estimate that within three years, three-quarters of the region’s banks will have a CFO in place, driving the financial management processes that Asia’s banks need to prosper and compete.