KEYNOTE INTERVIEW

Optimizing treasury management

All managers should be thinking about their treasury set-up and anticipate future needs to manage risks while maximizing use of scarce resources, says Alpha Alternatives' partner, treasury practice, Danny Olds

Q What problems are fund managers experiencing?

We see two different types of problems impacting fund managers to varying degrees based on size, complexity and overall maturity of the treasury operations in place. Some have implemented treasury management systems (TMS) with common controls but have not focused on evolving the platform. Others have little or no system support, with key activities handled manually with e-mail and spreadsheets. This creates vulnerabilities that place cumulative strain on staff and lead to recurring errors and/or increased risk.

Common symptoms include overly burdensome processes for initiating and approving wires, LP distribution errors, challenges matching capital calls, mistakes in funding highly visible investment activity, overdrafts, inefficient use of debt and misuse of idle cash. Without concentrated data to forecast cash and systems that surface it effectively, it can be impossible to analyze and optimize liquidity at higher volumes. There are solutions to these problems, and together they can increase scale materially while eliminating traditional risks.

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Q What is the difference between corporate treasury and treasury operations for private funds, fund administrators and asset managers?

All corporations of size feature a treasury department. For managers focused on alternatives, that function rarely appears on the organization chart in private equity, but usually exists in some form in private credit and at larger, diversified investment managers, where managing liquidity is core to its strategy and more operationally burdensome. Nearly all fund structures in this space roll up to a stand-alone entity, with operational considerations for investment activity that crosses funds.

Management company, or corporate treasury, typically focuses on a more traditional, balance sheet-oriented set of objectives. Needs, pressure points, connected systems and language differ, but the underlying idea is largely the same. Firms lacking a dedicated treasury function often push these responsibilities to fund accountants, who may not be best suited to evolving the operational function as volumes and complexity rise. Tasks like downloading

bank statements for cash analysis, initiating and chasing wires and cobbling together forecasts might not be the best use of their time or talents.

Q For newly formed and growing firms, how should they manage treasury processes to anticipate future needs?

Dedicating resources and focusing on systems and processes from the start would be ideal, but it is rarely is it practical. The best approach is to maintain an early focus on controls and best practices to mitigate risk, positioning the firm for a more formal structure over time, and monitor KPIs around time spent on treasury-related activities and volumes. Firms should not wait until mistakes become disruptive or costly before addressing issues. Periodic health checks from an experienced third party are not costly and are an easy way of staying ahead of the curve.

Q How can treasury management technology help?

Without the right systems and streamlined processes, there is escalating room for error, fraud and inefficiencies, which worsen as size and complexity increase. It is one thing to miss a $7,500 expense; it is another for a bad actor to hijack a funds flow and redirect a sizable allocation in a fund investment. Operating this way creates a lot of pressure and risk. Practically speaking, if the time being spent on movement of cash is consuming 10 minutes per wire and it can be reduced to one to two minutes, by itself, resolving that will really move the needle.

"Cash forecasting is typically the area most impacted by data"

Managers experiencing growth or increased complexity without a TMS can benefit significantly from adopting one to streamline and de-risk business processes that are common to all fund managers. For fund administrators, where scale is king, a TMS is an absolute must.

Q Why is scrutiny of managers' treasury operations important to LPs?

Treasury as a function, and its related processes, are now commonplace in LP due diligence exercises. Investor interest is typically driven by the need for strong controls to combat financial fraud, which can pose a significant threat to a firm's ability to operate. Sophisticated platforms automate and strengthen payment and approval controls, making it far easier to combat fraud and reduce risk while incorporating best practices across the board, which typically check the box.

A firm's treasury function health is most visible to its LPs via its seamless processing of distributions. Mistakes in the distribution process can be highly detrimental to LP relationships and overall firm reputation. And LPs are concerned with headline risk and black swan events that can disrupt fund operations, such as the 2023 Silicon Valley Bank failure.

Q What kind of data do managers need to effectively execute treasury operations?

Cash forecasting is typically the area most impacted by data. Managing liquidity is as much art as science, and cash planning and forecasting are core responsibilities of any treasury function. The data required to produce a trustworthy forecast comes from many sources and must be accessible in a central location for analysis to be accurate. As funds grow in complexity, nuance often increases, requiring continuous focus on data strategy. Once data is consolidated, reporting and follow-on analysis becomes far easier.

Much of the data resides in multiple systems, and sometimes spreadsheets serve as the system of record. From deal pipelines and allocations to legal entity attributes, debt levels, upcoming expenses, fund commitments, accounting data, other investment-related activity, static data for funds, investors, and unfunded commitments, all must be aggregated for on-demand cash forecasting.

At most firms, data is the issue. A TMS can be an aggregator of this data, or TMS data can be combined with other data in a data lake, with reporting handled by tools appropriate to the required level of sophistication. As a rule of thumb, a TMS will natively produce serviceable cash forecasts with interactive capabilities to act on modeling decisions. This works well for private equity-style funds, related SPVs and funds with conventional asset classes. For origination and more complex structures such as a BDCs, additional tools can be leveraged to produce a highly customized liquidity analysis.

Q What's the role of artificial intelligence in upgrading treasury processes?

TMS vendors are investing heavily in AI strategy, but it's only useful if the underlying data is sufficient and accurate for the desired interaction. For activity initiated by a TMS, or where TMS is the system of record, AI can spot anomalies, and opportunities for optimization, creating efficiencies and adding another layer of risk mitigation.

As AI capabilities evolve, a TMS will be able to identify the most attractive yield on idle cash and position it accordingly, highlight surplus cash or shortfalls across a fund structure and support other forward-looking business needs, for example. Imagine simply asking: "When will Project X close, and is all cash properly positioned?" Most TMS vendors have already incorporated first-generation AI into platforms and it is at the top of their strategic roadmap. ■