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February 2013

Where's the cash?

Failure to achieve sufficient visibility over the company's cash carries significant risk. The question is how best to go about improving visibility of and control over cash? Is technology the only answer?

The Corporate View

Neil King

Group Treasurer

Carphone Warehouse plc

Banking relationships

Creating benefits through heart-to-heart discussions with your bank

Corporate bonds

Still booming in 2013?

Regulation

MMFs: an update

Treasury practice

The power of social media

Back to basics

Balance sheet management

Excellence is rare.
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Adam Smith Awards 2013

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Apprentices
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Switchboard	+44 (0)13 0462 9000
Publisher	+44 (0)13 0462 9012
Subscriptions	+44 (0)13 0462 9002
Advertising	+44 (0)13 0462 9018
Editorial	+44 (0)13 0462 9004
Production	+44 (0)13 0462 9013
Fax	+44 (0)13 0462 9010

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2013: the year of 'muted optimism'

The Year of the Snake came in with more of a whimper than a hiss, with continuing concern over problems in the Eurozone and the US budget deficit. However, despite the International Monetary Fund (IMF) trimming its growth forecast for the world economy in 2013, after predicting a less vigorous recovery in the US, UK and the leading countries of the Eurozone, the general mood at the recent World Economic Forum (WEF) meeting was moderately buoyant.

The 2,500 movers and shakers gathered in Davos seemed fairly convinced that the collapse of the euro, a hard landing in China and a debt crisis in the US all look much less likely. Axel Weber, the former head of Germany's central bank, the Bundesbank, even went as far as to say that the global recovery has passed a turning point. European Central Bank (ECB) president Mario Draghi was equally positive, expecting the Eurozone economy to begin recovering in the second half of this year.

Nevertheless, corporate treasurers still consider the uncertainty of the economic outlook as their top concern, according to a number of industry surveys.

New regulations are also top of mind for corporates – in particular the impending money market fund (MMF) reforms, which are expected to accelerate significantly in 2013. Both the US Financial Stability Oversight Council (FSOC) and International Organisation of Securities Commissioners (IOSCO) are mulling over proposals for further regulation to reduce systemic risk. This month, we take a closer look at the state of play of those proposals and the market in general.

However, in the midst of increasing global regulation, China is bucking the trend and opening up further to corporates. Pilot schemes launched by the State Administration of Foreign Exchange (SAFE), which deals with foreign currency controls, and the People's Bank of China (PBoC), which governs renminbi (RMB) liberalisation, have recently come to fruition. Two foreign currency cross-border sweeping pilots, one by Shell China and Standard Chartered China and the other by Intel and HSBC, and a cross-border RMB intracompany lending pilot by Citibank China and an unnamed European food company, may spell the end of trapped cash headaches for corporates operating in the country.

And finally, a quick reminder that the Treasury Today Adam Smith Awards 2013, sponsored by Bank of America Merrill Lynch, are now open and treasurers have until 30th April to submit entries. Now in their sixth year, these awards recognise leading solutions and best practice. This year we have created three new categories:

1. Best Foreign Exchange Solution.
2. Asia Pacific Regional Award for Best Practice.
3. Treasury Today Woman of the Year.

It is a wonderful opportunity to showcase your and your team's talent and innovation in the face of difficult market conditions. We wish everyone the best of luck.

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For better or worse

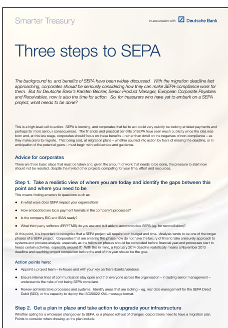
Corporate treasurers work hard trying to get the most out of their banking relationships. Some are waking up to the fact that, just like other relationships, there must be mutual benefit for it to last. Opening up and letting a bank into your 'inner circle' may leave you feeling a little exposed, but in fact can lead to game-changing solutions for your business.

CASH MANAGEMENT 34

The visibility conundrum

According to a study by Ernst & Young in April 2012, a majority of companies are planning to further improve visibility of and control over cash. The question, then, is how best to go about this? What role does electronic bank account management (eBAM) play in this quest?

SMARTER TREASURY 30



Smarter Treasury

in association with Deutsche Bank

Three steps to SEPA

The background to, and benefits of SEPA have been widely discussed. With the migration deadline fast approaching, corporates should be seriously considering how they can make SEPA-compliance work for them. But for Deutsche Bank's Karsten Becker, Senior Product Manager, European Corporate Payables and Receivables, now is also the time for action. So, for treasurers who have yet to embark on a SEPA project, what needs to be done?

This is a high-level call to action. SEPA is looming, and corporates that fail to act could very quickly be looking at failed payments and perhaps far more serious consequences. The financial and practical benefits of SEPA have seen much publicity since the idea was born and, at this late stage, corporates should focus on these benefits – rather than dwell on the negatives of non-compliance – as they make plans to migrate. That being said, all migration plans – whether spurred into action by fears of missing the deadline, or in anticipation of the potential gains – must begin with solid advice and guidance.

Advice for corporates

There are three basic steps that must be taken and, given the amount of work that needs to be done, the pressure to start now should not be resisted, despite the myriad other projects competing for your time, effort and resources.

Step 1. Take a realistic view of where you are today and identify the gaps between this point and where you need to be

This means finding answers to questions such as:

- In what ways does SEPA impact your organisation?
- How embedded are local payment formats in the company's processes?
- Is the company BIC and IBAN ready?
- What third party software (ERP/TMS) do you use and is it able to accommodate SEPA (eg. for reconciliation)?

At this point, it is important to recognise that a SEPA project will require both budget and time. Analysis tends to be one of the longer phases of a SEPA project. Corporates that are entering this phase now do not have the luxury of time to take a leisurely approach to systems and process analysis, especially as the follow-on phases should be completed before financial year-end processes start to freeze certain activities, especially around IT. With this in mind, a February 2014 deadline realistically means a November 2013 deadline and reaching project completion before the end of this year should be the goal.

Action points here:

- Appoint a project team – in-house and with your key partners (banks/vendors).
- Ensure internal lines of communication stay open and that everyone across the organisation – including senior management – understands the risks of not being SEPA compliant.
- Review administrative processes and systems. Identify areas that are lacking – eg. mandate management for the SEPA Direct Debit (SDD), or the capacity to deploy the ISO20022 XML message format.

Step 2. Get a plan in place and take action to upgrade your infrastructure

Whether opting for a wholesale changeover to SEPA, or a phased roll-out of changes, corporations need to have a migration plan. Points to consider when drawing up the plan include:

Three steps to SEPA

With the Single Euro Payments Area (SEPA) deadline for migration quickly approaching, Deutsche Bank's Karsten Becker, Senior Product Manager, European Corporate Payables and Receivables, argues that now is the time for action. What needs to be done if you haven't already started planning your SEPA project?

in association with

CORPORATE FINANCE 15

Tapping the bond market

Corporates need to think outside the box when it comes to funding opportunities. Ford Motor Company was among a number of companies borrowing on the capital markets taking advantage of a post-fiscal cliff rally in early January, using the bulk of the money to fund its pensions. Many are getting in while the going is good, for no one knows how long favourable market conditions will last.

TREASURY PRACTICE 18

Are you connected?

Judging by the growing levels of activity in discussion groups on the LinkedIn website, it appears to be largely the networking function of social media that is currently attracting most interest from the financial community. But to really make an impact on the day-to-day job, social media needs to become an integral part of the treasurer's workflow.

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24 The Corporate View

Neil King
Group Treasurer

Carphone Warehouse

Neil King, Group Treasurer, Carphone Warehouse, steadfastly adheres to the KISS principle – Keep it Simple, Stupid. In a world dominated by complexity and change for change's sake, his approach is refreshingly different.

REGULATION 27

Money market modifications

The road to money market fund (MMF) reform has been politically laborious. The industry is no doubt preparing itself for upheaval and modification with the introduction of inevitable reforms. But the global financial arena is also shaping the structure and various management approaches to funds and certain portfolios.

This page contains an edited version of the Treasury Insight piece written in the last month. The full versions of Treasury Insights are posted on treasurytoday.com as they are ready. The Treasury Insights weekly email summarises the new pieces from that week plus other news relevant to treasury. You can register for this free service at treasurytoday.com

Market reacts as IT2 sells out to Wall Street Systems

When IT2 announced that it was to be bought out by Wall Street Systems (WSS), what was the reaction from industry players and system users?

Treasurers

Mike Verrier, Group Treasurer at Wolseley, said the announcement "has come as a surprise" but added that "it's not something that particularly worries me". Verrier philosophically sees the deal as a natural market development. "The question you've always got as a user of IT systems, particularly ones that are developing all the time, is how stable their ownership is. I've never had any doubts about the ownership if IT2. If it has gone to WSS now, that doesn't strike me as being something to give me cause for concern. If they're going to maintain IT2 and enhance it, then that would not be a bad thing. We'll see how the whole thing develops."

In Ireland, Michael McGovern, Group Treasurer at the Irish Dairy Board, told Treasury Today that this was also news to him, but that he did not expect much to change. "We rely on the IT2 system, and one would think WSS would not just get rid of the system; there's value still in it." But McGovern added "it's a bit disappointing" that it is another private equity company taking over. "I think we're in no better or worse position than when CapMan owned it," he comments, adding that "I would have preferred to have someone other than another private equity company".

Vendors

Bob Stark, Vice President Strategy, at rival vendor, Kyriba, commented: "From an outsider's perspective, it will be interesting to see which products WSS will keep from this acquisition and which ones it will be looking to replace in its existing portfolio." With reference to WSS's acquisition of City Financials in June 2010, Stark says he will be "interested to see if this will spell the end of City Financials' brief run in Wall Street Systems' portfolio".

Jiro Okochi, CEO of Reval (which acquired Germany-based TMS provider, ecofinance, in January 2011), says that if executed well, M&A "can be beneficial for the marketplace". Now, as well as considering the track record of the acquirer, IT2's clients should be contemplating what the long-term strategy might be for their platform. "Is it going to be one of many products; is it going to be a long-term platform for a segment of the market; will it die on the vine? It becomes more concerning the more products you have if the strategy isn't then clearly communicated to the clients," he explains.

Consultants

This is a theme picked up by industry consultant, Ken Lillie, who says that the selection process for buyers of TMS does not concentrate solely on functionality and technical product delivery but looks at many other areas such as service, and the supplier/client partnership. "Without casting any doubt on WSS's ability to deliver in these areas, their purchase of IT2 reduces further the choice of supplier." As with Kyriba's Stark, he too adds that it will be "interesting" to hear WSS's proposed strategy having acquired what was previously a direct competitor of City Financials.

However, Lillie feels that apart from SunGard as the other "major", this acquisition should serve to bring some of the relatively smaller players into shortlists more frequently. "This is no bad thing as there are some very interesting and powerful products available at this level that can deliver to both simple and complex treasuries operations."

With its acquisition of ecofinance and subsequent product integration, he believes that Reval is delivering a "complete" TMS solution. "Salmon Software, Bellin, GTreasury, Visual Risk and several others should step up, and I would recommend any potential buyers carry out some thorough research," he adds.

And then there were two …

The TMS market still offers a number of choices, but on the truly global stage WSS is matched only really by SunGard for sheer size. WSS's acquisitive nature has seen it purchase many different companies over the years. In the treasury space it took on the likes of Thomson Reuters' Treasura in January 2011, Speranza in April 2010, Aleri Global Banking in April 2008 and Trema in October 2006.

In terms of cash and liquidity systems, it now offers the Wall Street Treasury and the less complex Treasura systems. IT2 will presumably now fall into the TMS line, alongside the City Financials solution. In the global enterprise systems space, the firm offers the Wall Street Suite, mostly pitched at large banking institutions and major international corporates.

SunGard, as the main rival to WSS, is not easy to pin down to a particular product for treasurers. Its primary treasury offering falls under the AvantGard liquidity management product set consisting of AvantGard Treasury, AvantGard Receivables, AvantGard Payments and AvantGard Predictive Metrics. But it also lists 68 other different financial technology products (not all of which are treasury-focused).

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Funding growth in the developing markets

Tapping our collective knowledge to get better information

> *What is the best way to fund growth in the emerging markets?*

Gerard Gallagher, Advisory Services Markets Leader, Ernst & Young:

The very first thing is prioritisation of resources. Clients across all sectors are really challenging themselves about where they are spending their money. The level of rigour around investment and return on investment has been at the highest that I have ever seen.

We saw so many business cases in the past, particularly in commodities sectors such as oil and gas, and metals, where commodity prices used to be the saviour. In the last 20 years prices have only gone in one direction, but in the past two years they have begun to move in the other direction. Now, all of a sudden, the operational effectiveness of many of these companies has been drawn out, in a way that is challenging them. So they are now starting to worry about business cases and investments. I would say therefore that the very first thing that people looking to invest in emerging markets, or indeed in new offerings, should do, is to start to rationalise and prioritise their existing resources.

The second point concerns operational efficiency. Organisations are saving money by centralising resources and bringing processes together to fund these new areas.

A third key trend, particularly around the faster growing markets, is that people are increasingly looking to form partnerships. Many organisations are entering into joint ventures where they can add value and get access to that market other than just cash – so they can bring intellectual property, bring skills and resource innovation. In emerging markets it's not just a case of how much money you've got, but what other resources you have available as an organisation to deliver in those markets. You need more than just money to be successful.

And finally, from a treasury perspective, one of the biggest challenges I hear of when I speak to treasurers of companies operating in emerging markets is working capital and cash management. Do not go into an emerging market or a fast-growth market expecting the same working capital management processes and timescales that you may be used to in the more mature and established markets. That is not going to be the case.

My key message is, challenge where you are spending your money at the moment and get on with those good things that you need to be doing around operational efficiency. An average organisation can save up to 10%-12% just by doing that and recycle that money into emerging markets. Think about other resources that you have in your organisation that you can use to fund that expansion – IT and other non-cash resources. And finally, watch out for your working capital and your cash flow.

Dr Murat Ulgen, Chief Economist for Central and Eastern Europe and Sub-Saharan Africa, HSBC:

Emerging markets, led by Asia, in particular China, have become the driving force of global growth as the economic prospects of the developed world are still marred by structural problems. As such, the notion of the 'emerging market' has itself been questioned. While this might be an endless debate, one thing is clear, emerging markets still need a significant amount of investment in infrastructure, both in human and physical capital. It is important to note that the growth potential of a country can be boosted by investments into productivity-enhancing areas, in addition to bringing more people into active economic life. These investments, by definition, should be long term in nature. Hence, the best way to fund growth in emerging markets is to fund such long-term investments that would deliver a highly-skilled labour force in the future.

The source of such funding is also crucial. These investments could be financed by domestic savings and/or external capital. More importantly than the origin, such investments require a stable source of funding. Emerging markets span a very wide range of countries. Some rely heavily on domestic savings, such as those in Asia, others predominantly on foreign funding, like those in Central and Eastern Europe. The latter presents a risk in today's highly-integrated global markets when a sharp decline in investor confidence might lead to a pull-back of external financing, thereby hampering investments in those countries that rely too much on foreign funding. On the other hand, depending excessively on domestic savings poses other problems such as imbalanced growth that relies too much on investments, a decline in the return on capital, excessive reserve build-up and domestic asset bubble, to name a few. Therefore, it is important for an emerging market country to strike a delicate balance between domestic and foreign savings to finance growth, provided that these are long term and stable sources of funding.

Emerging markets should draw a lesson from the past mistakes of the developed world. They should not engage in a swift build-up in debt, even though borrowing terms may look very favourable nowadays thanks to ample global liquidity. That said, access to cheap global capital should be welcome so long as it generates higher productivity, sustainable economic growth and income and wealth that expand at a faster pace than indebtedness.

Mahesh Kini, Regional Head of Cash Management for Corporates – Asia Pacific, Global Transaction Banking at Deutsche Bank:

When companies in Asia are looking to fund growth, they have – generally speaking – three options. These are:

1. Utilising cash to the best extent possible within their company;
2. Optimising cash across the wider organisation – including sister or parent companies, for example; or
3. Tapping into capital markets or bank financing to raise funds. However, when we look at the emerging markets more closely, it becomes clear that the methods of combining and optimising these three options differ from those in the developed markets. This is primarily due to the varying regulatory frameworks that are in place throughout the emerging markets. While most are making significant progress towards easing monetary constraints, issuing changes to transactional policies is not always in their immediate plans.

If choosing the first and second options – utilising cash within an entity and throughout the wider organisation – corporates with operations in emerging markets may face the added complexity of having considerable balances dispersed across various international/local banks and accounts. Companies that find themselves in this situation may wish to consider consolidating these balances, which could prove to be a substantial and relatively inexpensive source of capital. The many liquidity management options available today can be of great benefit to these organisations.

Given that traditional cash sweeping or pooling may not always be possible in emerging markets, banks like Deutsche Bank can help corporates achieve the same goals with alternative solutions, such as standard and advanced group entrustment loan options in China, or nostro collection solutions in Korea, that enable corporates to consolidate bank relationships and reduce the number of bank accounts they hold. In Thailand or Indonesia, corporates may wish to consider multi-bank cash sweeping, which allows them to benefit from a daily cash sweep from their local bank accounts to a single, consolidated master account. Solutions such as this can help corporate treasurers consolidate 'trapped' balances, which in turn can be easily deployed to fund future growth initiatives.

As for the third option, companies may choose to fund emerging market growth by accessing the capital markets either in developed economies, or the emerging markets themselves. However, as some degree of complexity – as well as higher fees and financing costs – is inherent to this choice, it usually comes as part of a company's broader development strategy.

Clearly, one size does not fit all when it comes to funding growth in the emerging markets. The optimal solution will differ from company to company based on corporate profile and strategy. Banks with notable emerging market experience are best-placed to offer advice on the most appropriate cash optimisation solutions, the majority of which are likely to begin with methods of maximising cash internally before reaching out to the wider financial/capital markets as alternative sources of funding. ■

The next question:

"Should corporate treasury be more concerned with managing commodity price risk?"

Please send your comments and responses to **qa@treasurytoday.com**

ecr research

Doomsday inflation?

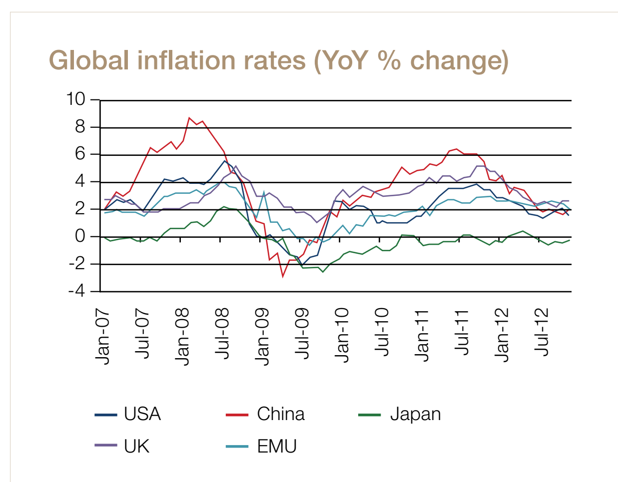
"It took three years of muddling through crisis, near-panics in the financial markets, a million or so jobs lost in the US, social unrest in the developing world to recognise the debt crisis for what it is: a long-term economic and political barrier to development that is slowly strangling world economic growth."

At first glance, this quote from Christine Bogdanowicz-Bindert on the impact of the debt crisis seems very apt. However, the above citation is far from recent. The words were uttered in 1985, when debt crises erupted in Latin America and Africa. Attentive readers may have noticed already that this quote has no bearing on the crisis that started in 2008. So Europe (in particular) has been muddling through for five years already, while the US has lost millions of jobs, instead of a million. That is to say, the present crisis is far worse. In addition, in the 1980s, the major countries (or blocs) – the US, Japan and Europe – could still extend a helping hand to the 'small fry', now they themselves are hit. And, unlike Mexico and the other troubled countries 30 years ago, they face a daunting obstacle: demographic ageing.

Fiat money fatally flawed?

Doom-mongers believe politicians will choose the easy way out and put pressure on central banks to crank up the printing presses. If so, inflation will rise, ie the size of the debt mountain will decrease in real terms. The inflation scaremongers often point to the weakness of the (international) monetary system, because it is based on fiat (soft) money. The pessimists think a monetary system based on fiat money will rarely, if ever, exist for long because hyperinflation is inevitable.

The first use of fiat money was chronicled as early as the 10th Century AD when the Song Dynasty in China issued paper money that remained valid for three years. Subsequently, it could be converted into new money, at a cost of 3%. In the long run, too many notes were issued whereas not enough 'old money' was handed in. Inflation hit and the fiat money lost its appeal.



Source: Orcam Financial Group, LLC

Next, the Yuan Dynasty issued paper money on a large scale in the 13th Century. Eventually, the regime printed far too many notes and hyperinflation reared its ugly head. Still, the Yuan money was used for quite a long time and only abolished in 1455 by the Ming Dynasty.

Horror and success stories

Fiat money made its entry into the western societies in the 17th Century, first in Sweden and the Netherlands, and then later in America in the 18th Century. The so-called Continentals, issued after the start of the American Revolutionary War (1775-1783), are a case in point for those who believe that fiat money is a nightmare. Owing to a lack of co-ordination between Congress and the individual states, not to mention sabotage by the British (who printed heaps of counterfeit money), within a few years the notes were one-fortieth of their nominal value.

Yet such horror stories are but one side of the coin. At the end of the 17th Century in the Netherlands, the Amsterdam Wisselbank (AWB) created a successful fiat money regime that existed for over a century. It slowly bled to death and went under as a result of the Fourth Anglo-Dutch War in 1780.

In 1862, the US notes, also known as greenbacks, were introduced in order to fund the American Civil War. In its original form, the greenback was a fiat currency that was issued until 1971. The greenback hovered between 'hard' and 'soft' until fiat money became the norm. In other words, the idea that in all cases fiat money is doomed to an early failure should be taken with a grain of salt.

Hard money far from perfect

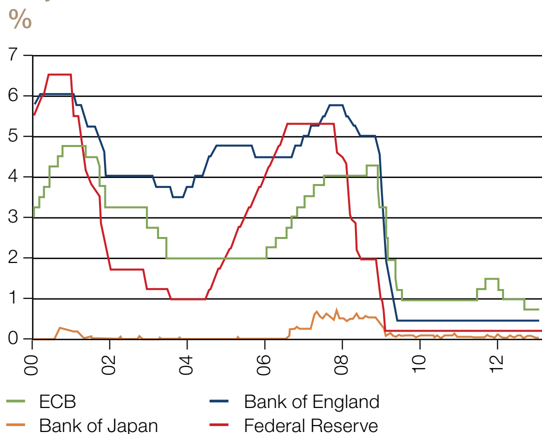
Meanwhile, hard money is also far from plain sailing. Several economists blame the gold standard for both World Wars. The (indirect) gold standard that was introduced after World War II was abolished in 1971, when US President Nixon decided that dollars could no longer be converted into gold.

So monetary systems built around fiat money may not be inherently stable, but gold standards can be fickle too. Whatever the nature of the money, rash political actions and/or waning investors and consumer confidence can prompt a disastrous spiral leading to hyperinflation, recessions and in the worst case, war.

So far, we have not seen such a spiral. However, anxiety is growing that the US, Europe and Japan will crank up the money presses and opt for competitive devaluations. It remains to be seen if holders of dollar debt will continue to believe in the US currency and the creditworthiness of the US government if the

Major central bank interest rates

%



Source: Thomson Reuters Datastream/Fathom Consulting

Federal Reserve conjures money out of thin air in order to reduce the debt. This is the same story for the Eurozone and Japan.

Imagining the unimaginable

Presently, it is still almost inconceivable that the markets would lose all faith in US, European and Japanese government securities. But that does not mean it couldn't happen. In 1961, Robert Mundell – one of the most respected and influential monetary economists the world has known – wrote that "it hardly appears within the realm of political feasibility that national currencies would ever be abandoned in favour of any other agreement." Yet a few decades later the European leaders did precisely that when they decided to introduce the single currency.

So we should think twice before labelling certain developments as "impossible". Take the run-up to World War I. In 1914, markets were convinced that war was out of the question because countries were interconnected economically and therefore mutually dependent. Panic only broke out after the first shots were fired.

Over the past Century, the international financial system has collapsed twice: in the 1930s and the 1970s. The first time, the outcome was catastrophic. The second time, no world war broke out but the rate of inflation soared until it was contained, around the end of the decade, by Federal Reserve chairman Paul Volcker.

Positivism will not last

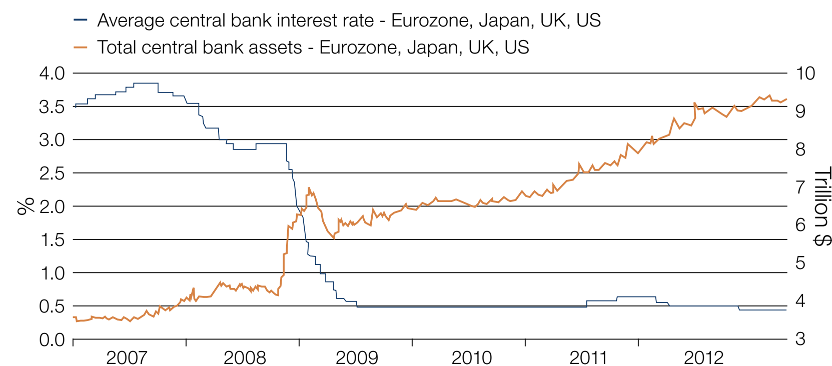
Should politicians decide to drive up inflation in order to tackle the structural problems, and the markets hit the roof, this could result in a long period of high inflation that will eventually be brought under control. This is the more optimistic prognosis. At worst, political tensions will rise quickly as states try to steal a march on each other through devaluations, inflation policies and trade wars. If so, we can only hope that the calamities of the last century are still fresh in the collective memory – otherwise a doom scenario may well occur.

For the moment, the markets are giving the politicians the benefit of the doubt. The US, Japan and the 'strong' EMU countries are borrowing at record low interest rates, inflation is still low and there are no currency wars or large-scale protectionism. The Eurozone crisis has, momentarily, calmed down.

The general sense of optimism may persist for another while but eventually we expect mounting Eurozone tensions, a deepening political struggle in the US, more geopolitical unrest in Asia, and continuous instability in the Middle East. In addition, the major players in the global economy will continue to face gigantic fiscal problems that are more difficult to solve because of the impact of aging populations.

We should monitor closely what happens in Japan as Europe and the US may be forced to go down the same road. Japan's national debt amounts to 230% of GDP; its population is ageing rapidly. Instead of tackling the problems, debts are stacked up to the heavens. It will be increasingly hard to pay these off, as the ratio between the number of workers and the number of retirees (who are living longer than ever) is in decline. Many fear that Prime Minister Shinzō Abe wants to pull Japan from the quicksand through higher inflation and a depreciation of the yen. But how far will he be prepared to go? Are Europe and the US doomed to follow suit? The answers to these questions will determine how the financial markets fare in the medium and long term. ■

Central bank rates and assets



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Carole Berndt, Head of Global Transaction Services for Europe, the Middle East and Africa at Bank of America Merrill Lynch.

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Vice President, Head of Treasury and Finance
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For better or worse

Open communication and an agreed level of honesty are crucial to a harmonious relationship. Many corporates and banks are sitting down for heart-to-heart discussions around what they need to get out of the partnership in order to take it to the next level of mutual benefit.

A banking relationship can be likened to a marriage: it is a long-lasting commitment, built on shared objectives, trust and respect; usually involves an extended selection process, or courtship; and both parties need to benefit in order for it to last. "And in both cases you should have a full prenuptial agreement in place," quips a Senior Treasury Manager from a large consultancy firm, who asked not to be named.

Corporate treasurers normally fall into two categories with regards to how they engage with their banks. There are those who have viewed banks solely as vendors of products and services, a 'marriage of convenience' in essence. Price is the sole driver in the relationship and they commonly play banks against each other in order to get the lowest fees possible. These corporates keep their business operations close to their chests and their banks very much on the outside.

The second type is comprised of those corporate treasurers who have taken a more holistic and forward-looking view of their businesses and relationships. These treasurers want to promote open and honest information sharing with their banks, and bring their relationship banks deep into their organisation. In addition, they are well aware that there needs to be a 'win-win' element to the relationship and that banks need to turn a profit too.

"In good times, those corporates that took a 'vendor approach' to their banks arguably had the upper hand," says Carole Berndt, Head of Global Transaction Services EMEA, Bank of America Merrill Lynch (BofA Merrill). "However, in tough times it's the corporate treasurers who invested in the relationship that have the advantage. Their banking partnerships have brought more to their organisation by providing information, resources and consulting services, such as help with euro crisis planning and Single Euro Payments Area (SEPA) readiness."

Berndt believes that if previously the split was 60/40 in favour of the banks-as-vendors model, since the onset of the economic crisis the relationship model has become the prevailing one.

This conversion has largely been driven because banks are now directly connecting corporate working capital credit facilities to cash management transactional business.

This is a knock-on effect of Basel III and return on capital pressures, which are forcing banks to review certain business areas. They find cash management a particularly attractive business because it is transactional and fee-generating. Therefore it stands to reason that if a bank is providing much-needed credit to a corporate, then they will also want a share of the corporate's cash management business.

And credit is considered 'much-needed' by many corporates. Refinancing/ensuring availability of long-term funding and credit lines is treasurers' top concern, according to the PricewaterhouseCoopers (PwC) Treasury Survey 2012; therefore when a corporate is choosing a new cash management bank, it often picks one that is part of its credit relationship in order to give some business back.

Many corporates are now taking a keen interest in how they can deliver bank relationship information. In order to guide their decisions, today's "savvier" treasurers are pulling together a much more detailed picture of their wallet, believes Steve Dwyre, Managing Director Global Corporates, Lloyds. "The most productive discussions we have happen when we perform account planning with a client, mapping out their entire banking wallet, where they spend their money and where financial institutions make money."

Treasury consultancy Zanders also works with clients to map out their wallets, for example Royal FrieslandCampina, with striking results. The 'wallet sizing' model developed jointly included all the company's worldwide banking partners and helped it to extend its €1 billion general purpose syndicated credit facility in the last quarter of 2011. FrieslandCampina used the model to prepare itself for one-on-one negotiations with its syndicated banking partners and resulted in its facility being extended out to August 2015 at substantially lowered margins.

However, as many are finding out, if the wallet is not proportioned out fairly, then this can lead to a difficult conversation when a corporate comes to renegotiate its credit lines, as the bank may decide to place its credit elsewhere.

The bank/corporate relationship is complex but if both sides can hit the right balance, it can prove to be a powerful stabilising and strengthening force in the current turbulent market.

A how-to manual for a strong relationship

It is worth noting that some banking relationships last longer than many marriages. One Assistant Treasurer from a large global food company reported that its banking relationships have been fairly stable over a number of years. "For example, our cash management providers have been unchanged (except for mergers) for more than 25 years," he says. "Our top lenders have been the same since 2001."

The company has a large banking group of more than 25 banks. "We see value in having a lot of relationships because it reduces the hole to fill if a bank drops out (in the case of a merger) or changes strategy," he explains. "A downside to a large bank group is keeping them all happy from a fee perspective and the time it takes to meet with such a large number of banks."

According to a June 2011 Financial Director Bank Survey, the majority of corporate clients that have maintained a stable relationship for at least five years (73%) are significantly less likely to switch banks. Asked why they did not intend to change banks, 54% explained that their loyalty was a result of general satisfaction with their banks, but there was also a sizeable number (51%) who cited the difficulties of switching as their reason to stay put. Almost one in five (19%) felt that switching banks would complicate transactions, while 13% thought the cost of switching was too high.

If breaking up is hard to do, what steps can treasurers and banks take to get the best out of their relationships? Dr. Mark Goulston, founder of CouplesCompany.com, argues that the foundation of a lasting partnership – although he means marriage, this can be applied in a corporate/bank relationship context – rests on six building blocks that form the acronym CREATE:

1. Chemistry.
2. Respect.
3. Enjoyment.
4. Acceptance.
5. Trust.
6. Empathy.

Chemistry

Chemistry is all about how well suited counterparts are in terms of business goals and approach. "Fit is a key element for a good banking client relationship," explains Lloyds' Dwyre.

In order to truly understand how well they fit together, corporates need to be open about their total wallet, business operating model and where the opportunities are. In return a bank also has to be clear as to what business lines are important to it and where it is operationally committed, as well as what it can and can't do well.

In the turmoil caused by the economic crisis, many banks retrenched to home markets and have focused on just one or two core competencies. Honesty as to where the business is concentrated is much appreciated by corporates. For example, if a corporate is splitting its business between Europe and the US, a bank may decide to only bid for the US cash management business. Most corporates will not see this as a sign of weakness but an acknowledgement of where the bank's strengths lie. Being honest and straightforward fortifies the relationship.

Respect

Respect is demonstrated by how well a party listens to the other. Dwyre agrees that the quality of a relationship directly correlates to the richness of dialogue. "In a marriage, if you are not talking then things aren't going to go well. A good quality relationship allows for the two parties to connect, identify what's really vital and work through it together," he says.

For a treasurer it is essential to have a bank that understands the corporate, its business processes, drivers and operations. Importantly, this includes listening to what it needs. "Corporates say that the best banks are the ones that really make an effort to understand what their business is and to be proactive in offering advice," according to David Kelin, Partner at Zanders UK LLP.

Enjoyment

Enjoyment is all about the people and very often it is key bankers that really cement the relationship – those people that

go the extra mile and show the same level of commitment in a client's business as the corporate itself. Corporates want to have a hotline to one person at the bank that can make things happen when something goes wrong – and most admit that they would pay extra for this immediate responsiveness.

If those key people leave, then that could potentially pose a problem for the relationship. The consultancy's Assistant Treasurer says: "Stability of personnel is important. As they begin to understand your needs, it is crucial that the team remains in place to continue to provide suitable ideas over an extended period."

Acceptance

Acceptance is about feeling welcomed as you are, as opposed to having to prove yourself. It is essential to get to the place where both corporate and bank are able to speak openly and frankly (within the parameters of the business). Sharing information avoids misunderstanding, as things are not left unsaid or implied.

"Through that frank exchange of information, which only happens when you trust each other and this comes back to partnership and relationship, you can then broker an agreement or understanding of where value exists for both parties and what mutual support is needed to make it work," says BofA Merrill's Berndt.

Trust

Trust is a dominant theme in any relationship. It takes seconds to destroy trust and years to rebuild it.

With the current climate in mind, treasurers are placing more emphasis on the reputation and overall positioning of their banking partners. "Corporates want to see a credible strategy, a strong balance sheet and commitment from their banks," says Dwyre. "They need trust in the individuals they're dealing with but also the bank as an institution, particularly in this market environment – corporates want to be sure that their banking partner is here to stay."

It is trust that gets a relationship through the rocky patches. "The true test of a relationship is if one stands by the other when the going gets tough," says Berndt. "There are times when we have to make tough decisions around client selection and support. And without exception when we reached the brink of a critical decision, the tenure, transparency and depth of relationship are the biggest factors as to whether or not we are able to commit to the transaction."

Empathy

Empathy is about understanding, attention and care. When corporates put business out to tender, some ask that a relationship bank be brought into the tender process, even if the bank isn't known for that specific task. In this sense, the bank is not excluded from the process but given the opportunity not to tender.

From a relationship point of view, it is important that a bank is shown what a company is doing in its tender process and also gives it a chance if it has recently expanded its offerings. "For example, if a traditional cash management bank creates a debt capital markets team and wants to lead a bond deal, when normally we wouldn't have seen them in that role," explains the food company's Assistant Treasurer. "Banks may not like to be pigeon-holed for certain services, but our return model is based on banks earning fees in some areas and leaving fees to other banks in other areas."

The spark: innovation

What is omitted from the CREATE model is innovation, which is vital for a lasting and durable relationship. A happy marriage is not just about the boring, everyday routine, but also continual change, development and spontaneity in the relationship.

In the corporate world, treasurers probably look more for proactiveness in their relationship banking partners than spontaneity per se. As treasurers are busy doing their day-to-day work, they would like their relationship banks to think ahead and proffer advice for future challenge, or in the case of a sudden event, to respond swiftly to help them through the crisis. For example, when the Arab Spring uprisings spread to Egypt, Citi reacted by setting up a response team to bridge the gap between in-country teams and overseas parent companies. From a technological perspective, the bank linked all the local systems, so that the team could see any transactions that were delayed or stuck due to infrastructural changes on the ground, which allowed the bank to give informed responses crucial to its clients' business.

A corporate with a strong banking relationship in place can take advantage of such bank-led innovations, as well as working together with the bank to develop new initiatives. For the Assistant Treasurer at the food company, "innovative ideas that reflect our needs and understand our situation" is the single most important factor for him when deciding on core relationships.

Interestingly, the shift to a more relationship-focused model is also driving co-operation between banks. "In response to a major client, we are now working with one of our competitor banks to architect a solution unique to that client," says BofA Merrill's Berndt. "This is only possible when a corporate treasurer is open with its banking partners, by engaging and bringing us into what is happening in his business. He is effectively getting more from the two banks working together to solve the problem, than he would were he to deal with us individually. Plus he will obtain a solution that is game-changing for his business." ■

Corporate Treasurer Survey: Bank Relationship Management 2012

- 44% of corporate treasurers polled believe that both parties profit equally from their primary banking relationships. Only 12% thought that banks were the sole beneficiaries, whereas another 36% thought that the banks gained more out of the relationship.
- 65% believe that there is room for improvement regarding the current fees and earnings credit rate; only 17% are happy with the current arrangement, whereas 18% didn't know.
- When negotiating with banks, 10% said that their banks didn't budge, while 48% said the bank gave them everything they asked for. More than one in five treasurers said that they had never tried negotiating with their bank.
- 41% wished they had more time to proactively manage their banking relationships.

Source: The Montauk Group

Corporate bonds: boom, bubble or bust?

Corporate bonds were last year's must-have asset class – and the market for it seemingly had something to offer everyone. For investors, corporate debt provided higher returns than government debt, but with less volatility than equities. For corporates keen to move away from bank debt, record low-yields presented a great opportunity to lower their borrowing costs. But with a changing macroeconomic backdrop, will the bullish trajectory continue in 2013?

Corporate bonds were one of the most popular asset classes for investors in 2012. The reason is quite straightforward. Yields on corporate debt may have fallen to record lows, but with governments around the globe committed to maintaining artificially low interest rates, the spreads between corporate/gilts have compressed.

This has created the perfect environment for corporate debt. Investors seeking yield are rushing to buy into the asset class, where they can get better returns than with government debt without exposing themselves to volatile equities. Corporates, meanwhile, have had to find alternatives to bank debt, as bank lending is not as buoyant as it used to be. For example, recent data from the Bank of England's (BoE) 'Trends in Lending' survey reveals that the total stock of lending to UK businesses fell by around $4 billion between September and November 2012. As a result, corporates now need to think outside the box much more when it comes to funding opportunities, and the $4 trillion surge in global debt issuance witnessed over the past 12 months is evidence of this developing creativity.

Getting in while the going is good

With record low rates of borrowing available on the capital markets for junk-rated and investment-grade alike, corporates have rushed to take advantage of market conditions. And, as

finance departments start planning further ahead, the "doubling-up" factors of pre-funding and liability management begin to come into play, according to Farouk Ramzan, Head of Corporate Debt, Capital Markets, Lloyds.

"All in all, the cost of debt in 2012 was very low," he says. "Corporates see the current market conditions as a great opportunity to pre-fund and for liability management – to get more cash on the balance sheet and buy back expensive debt." Companies, have been funding not just for the current year, but also further out in the future. "That is one of the main reasons for this quick increase in debt issuance," he says. "Since credit spreads and yields are really low, many treasurers and CFOs are looking beyond the 2012 maturities to 2013, or perhaps 2014."

As Ramzan explains, companies have been using the bullish trajectory of fixed income capital markets to improve their balance sheets. Ford Motor Company was among a number of companies borrowing on the capital markets taking advantage of a post-fiscal cliff rally in early January, issuing $2 billion worth of 4.75% 30-year notes. Neil Schloss, Vice President and Treasurer of Ford, explains that favourable market conditions were a significant factor in the company's decision to enter the capital markets for funding in January. "Interest rates have been lowered again and again," he explains, "and so have credit spreads." Combining the business case and an ideal capital markets environment meant that issuing bonds is a "no-brainer". The ability to issue a BBB-rated bond with a sub 5% yield was an opportunity in the market that Ford couldn't pass up.

"We are using the proceeds partly to call higher cost debt," he adds. "There is about $600m of similar maturity which has a 7.5% coupon, so that represents a significant saving and interest expense. The bulk of the remainder will be used to fund our pension plans."

Corporate debt in emerging markets

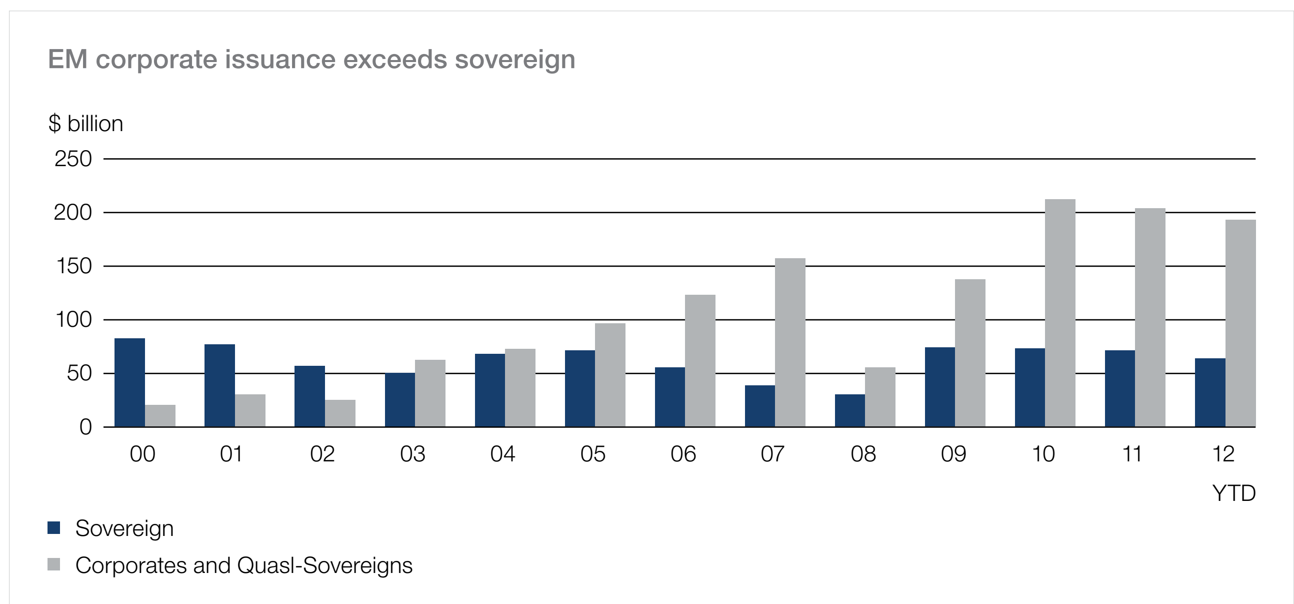
Despite a very different macroeconomic backdrop, the market for emerging corporate debt has been just as positive. Recent data published by J.P. Morgan reveals that $329 billion worth of emerging market corporate debt was issued during 2012, breaking a record of $210 billion set back in 2010.

In the past, interest in emerging market corporate bonds was often tempered by concerns over the credit worthiness of companies in those regions. Instead, sovereign debt was the main focus for investors seeking exposure to global bonds. Not anymore however. As the chart illustrates, corporate issues have far surpassed issuance of sovereign bonds in each of the past six years.

> "Corporates see the current market conditions as a great opportunity to pre-fund and for liability management – to get more cash on the balance sheet and buy back expensive debt."
>
> Farouk Ramzan, Head of Corporate Debt, Capital Markets, Lloyds

There is a similar dynamic at play in the market for emerging corporate debt as elsewhere, says Esther Chan, Emerging Market Debt (EMD) Portfolio Manager at Aberdeen Asset Management. The falling cost of borrowing has led to greater issuance and therefore increased liquidity. Meanwhile tightening credit spreads, together with the improving fundamentals for emerging market companies, have brought about an increase in investor demand for the asset class. "The good thing is that a lot of these companies, because of access to markets, are able to access cheap funding," she says. "And having all that additional liquidity in the market helps alleviate the thing which we fear the most – the inability for companies to get the funding they need."

One of the principal reasons for this positive trend is the greater capacity for growth and development in the emerging markets. But with growth slowing and with various structural challenges now coming to the fore, it may be overly optimistic to expect the same favourable market conditions again this year, Chan argues. "I think that the way companies manage



Source: J.P. Morgan, 10th September 2012

the different growth levels will be important," she says. "Whether a company wins or loses depends on its ability to navigate through the changing environment. It is much easier to hide your mistakes in times of high growth because your buffer is much bigger." This is a factor which will rise in importance more for emerging market corporates in the capital markets over the course of the next few years, if it hasn't begun to already.

Nevertheless, Chan remains optimistic about the prospects for emerging market corporates to meet these new challenges. Companies in developing economies have a considerable experience of operating in difficult conditions, something which she believes will stand them in good stead for the potentially turbulent times ahead.

The market in developing economies is less homogenous than in the US or Europe, comprising of more than 40 different countries, each with a unique political situation and set of dynamics. And this can be an advantage for investors, offering them a level of choice not likely to be found in the capital markets of developed economies.

With that in mind, Chan expects the investor base for emerging market corporate debt to continue to widen in the coming years, despite the changing macroeconomic backdrop.

Will bonds continue to boom in 2013?

In the capital markets of developed nations, the uncertain economic environment ahead in 2013 is dangerous for investors on two fronts: already marginal yields could be further eroded by inflation; and the value of fixed income assets could deteriorate markedly if central banks, particularly the Federal Reserve, begin to move away from their policy of near-zero interest rates.

A rise in interest rates could be particularly damaging to the corporate bond market. At the end of 2012, the ratings agency Fitch warned that while the damage would be limited by a gradual reversion to higher rates, a sudden rise could have dramatic consequences. According to Fitch's projections, a typical investment-grade US corporate bond with a ten-year maturity could lose as much as 15% of its market value were interest rates to return to their 2011 levels. For longer duration bonds, the drop would be even steeper with as much as 26% valuation loss anticipated if that scenario were to play out.

Not everyone is convinced of the likelihood of this happening during 2013, however. "I don't think that corporate bond spread levels are currently in bubble territory," says Euan McNeil, Co-Manager of Kames Investment Grade Bond Fund and the Kames Investment Grade Global Bond Fund. "If you look at it on a three or four year spread history, they are certainly close to the tights. But on a longer-term view they still offer some value, particularly against underlying government bonds."

The macroeconomic backdrop should continue to be supportive of the corporate bonds for the foreseeable future, McNeil argues. "We don't subscribe to the view that government bonds – particularly domestic gilts – will be materially high in 2013, given the relatively moribund economic backdrop and the commitment of central banks to keep rates at exceptionally low levels for the near future. We would be surprised to see any rate hikes before the summer of 2014."

The market for corporate debt could also be affected in the coming year by forthcoming regulatory changes, such as Basel III and Dodd-Frank. New liquidity rules soon to be introduced by the Basel Committee on Banking Supervision were diluted at the beginning of the year and now allow banks to hold some corporate bonds to satisfy their liquidity coverage ratios. Under the previous guidelines, banks were permitted to hold only corporate debt rated AA- and above, but can now include any bond rated BBB- or above as part of the buffer. But with such high levels of liquidity presently in the market for corporate debt, Ramzan is doubtful that the change will make much difference to demand level. The main thing to be watchful for in the coming year, he argues, is a sudden deterioration in the political situation in either the US or Europe.

> "Whether a company wins or loses depends on its ability to navigate through the changing environment."
>
> Esther Chan, Emerging Market Debt (EMD) Portfolio Manager at Aberdeen Asset Management

"Let's be clear, if there was a 'black swan' event and a risk-off period, then the high yield market would certainly suffer," says Ramzan. But excluding an extreme scenario, he predicts demand for high yield to continue for the foreseeable future. "And I think that institutional investors are becoming a little bit more comfortable with this ongoing background volatility. So unless there is a major event, I expect high yield issuance to continue to come to the fore."

No time to lose

With experts agreeing that the favourable market conditions for corporate debt issuers are likely to continue through 2013, should a corporate considering a debt issue move now or wait for the market to move even further in their favour?

Ramzan believes that it would be unwise to delay. With the recent compression in spreads with government gilts, treasurers and CFOs may be tempted to hold out for further tightening that would generate an even lower cost of borrowing. "They are probably right," he says, adding that he expects to see a 50 basis points tightening over the course of 2013 for the indexes. "However, the problem is that while you go fishing for the best level of compression in your credit spread, there is a risk that something will happen that would produce a massive swing in government yields – and the risk of that happening is probably greater than seeing a three or four point compression in your credit spreads."

Ford's Schloss agrees that waiting any longer would not be a gamble worth taking. Corporates should be looking to take advantage of low cost debt while they still can. "I would do it sooner rather than later," he advises. "Ford Credit is constantly in the market. Over the past three or four years we have issued between $6 billion and $10 billion a year in unsecured bonds – and we'll be continuing to do that throughout the year in multiple markets."

"But if I was a one or two time issuer in the market, I would go in early and take the chance while it's still there," he adds. ■

Treasury for the social media age

Social media has profoundly changed the way businesses interact with consumers. Today new platforms are emerging with the aim of integrating social communications into the daily workflow of the treasury and finance professional. Has the time finally come for treasury to join the social media revolution?

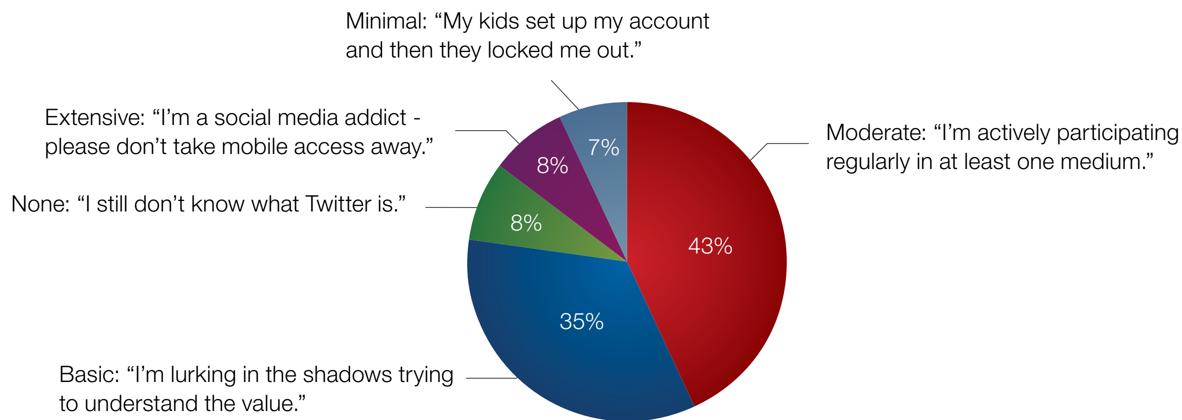
Financial professionals have been slow to foray into the social media realm – a hesitancy which some have speculated stems from concerns regarding reputational and security risk. There are some indications that this may be changing, however. In a 2011 study by American Century Investments (see chart on page 19) half of the financial professionals who participated in the study said that they were either moderate or extensive users of social media. A further 35% claimed to be "lurking in the shadows, trying to understand the value".

While many investment professionals are still 'lurking', most are participating regularly in social media. Half of the financial services professionals participating in the study indicated they have moderate or extensive experience with social media.

"I think that slowly there is going to be a shift," says Nasreen Quibria, an Executive Consultant and Payments Expert for CGI. "There is going to be more uptake as treasurers and financial professionals more broadly, become more comfortable with social media as they realise the value-add of these tools."

Judging by the growing levels of activity in discussion groups on the LinkedIn website, it appears to be largely the networking function of social media that is currently attracting most interest from the financial community. LinkedIn is used principally as a tool for self-promotion and connecting with industry peers. These benefits, Quibria believes, have become increasingly important in recent years. "Treasurers and other financial practitioners are using social media more

How would you characterise your level of experience with social media?



Source: American Century Investments

for personal or career reasons," she says. "In the current uncertain economic environment it has become particularly important, as it is a way for you to establish a positive image and promote yourself online."

But for those treasurers who do put aside their reservations and embrace social communications, there are, she says, a number of potential pitfalls of which they should be aware.

One common mistake that Quibria highlights is typically made before the professional even begins to interact with peers. Sometimes, financial practitioners new to social media will not pay enough attention to building a professional looking profile – the first impression given to a potential interviewer. An unprofessional or clumsily taken photograph is one example of a hazard that should be avoided, Quibria stresses.

Building Treasury 2.0

Social communications are beginning to find some level of acceptance within the financial community – at least from a personal, networking perspective. But whether a site such as LinkedIn has any practical benefits for the corporate treasurer beyond keeping in touch with industry peers and finding out about the latest job opportunities is doubtful, most experts agree. According to Daniel Andres, Business Development at Entarena, the benefits of traditional social media platforms are rather limited. "For the finance professional, Twitter is useful mainly for collecting information, to find out what is going on within the treasury community and keeping up-to-date with new developments," he says. "LinkedIn can be interesting from a networking perspective, for promoting yourself and perhaps finding suitable candidates for open positions in your finance department as well."

But that is where it stops for the traditional social media platforms. Their usefulness from a treasury perspective, he suggests, "is fairly limited, since it never really enters the daily business processes of the treasurer, accountant or cash manager."

But what if the traditional social media platforms could be adapted to better suit the treasurer's requirements?

In the past few years, several platforms have been launched aiming to do just this. One of these is Entarena, a communication platform launched in 2011, which builds upon the two most useful aspects of social media: the collection and communication of information, and integrates this with existing business applications. The system, which was recently adopted by the German airline Lufthansa, allows the corporate treasurer to create customised dashboards around each bank relationship. The dashboards have the capacity to combine internal data from ERP, trading, treasury and banking systems with external data such as market news. Notifications can then be delivered relating to key news or events and the treasurer can additionally use the dashboard to communicate any relevant data either internally or externally.

> "There is going to be more uptake as treasurers, and financial professionals more broadly, become more comfortable with social media as they realise the value add of these tools."
>
> Nasreen Quibria, Executive Consultant and Payments Expert for CGI

"Treasurers still see social media as a marketing tool or a sales-driven initiative within the company," says Andres. "But having a platform and a solution that brings communication in-house and around your daily job, so that it becomes an integral part of the workflow of a treasurer, is when we can see huge benefits."

However, he acknowledges that the industry is still only at the beginning when it comes to applying social technology into business workflows, adding that "there are currently not many solutions out in the market which have been built with the focus on directly building social communication into the work processes."

But Andres isn't the only person to recognise the potential of social communications for use as a business tool. Last year, Daniel Marovitz, former Global Head of Products at Deutsche Bank's Global Transaction Banking division, founded buzzumi, a cloud-based platform that powers professional conversations online. Unlike other products in the online meeting or conferencing space, it enables a company's

employees to have meetings and sales conversations online in a fully branded environment, while giving managers full auditability and control.

Marovitz himself is no stranger to the world of social media having previously spearheaded Drive DB, a successful web-based community site which allowed Deutsche Bank clients to participate in product design and development through online voting, debates and information sharing. With his new project, buzzumi, Marovitz is once again demonstrating that social media can indeed work in a financial professional setting.

> Security concerns are diminishing. IT departments always look into the security aspect and in most cases they come to the conclusion that the technology is as secure, if not more secure, than internal systems."
>
> Daniel Andres, Business Development at Entarena

"Our new platform buzzumi is all about empowering professional conversations," he says. "The issue is that, particularly in well-regulated industries such as finance, there is a lot of difficulty using tools that are intended for the consumer world – they are just not fit for purpose. Online sales meetings need content control and recording that can satisfy the demands of the compliance department."

buzzumi offers several functions which Marovitz says businesses will not find anywhere else. Firstly, the platform is a fully brandable environment. So unlike the market-leading VOIP platform, Skype, only the client's brand is visible. And the interface can be customised to reflect the look and feel of the client's existing web presence. The second unique feature, he explains, is that a company can perform a range of different interactions, removing the need for multiple platforms. In the near future, the platform will also offer integration with leading client relationship management (CRM) platforms, such as Salesforce.com.

The platform also provides dashboards complete with integrated analytics. So if a company was to empower its sales force, for example, with the buzzumi tool set, when they talk to clients over the platform the company can monitor all the details of the meeting – what was talked about, what presentation was shared, how long the meeting lasted, etc. Of course, there is inevitably a degree of intimacy which is lost when face-to-face meetings are exchanged for web-based video conferences, he acknowledges, but what a company gains is more control. "This platform allows you to govern all those interactions. For example, we have built-in content libraries that are controlled, so you can be sure that only presentations that have been approved by legal and marketing are being shared with clients.

This means a company can create a sales force that is much more efficient – firstly, because they are not running around the world, burning time and travel cost; and secondly because the tool set gives the company more control around what each person is doing."

Quibria agrees with Andres and Marovitz that the potential for improved and more efficient communication is where treasurers and the financial profession as a whole will find the real benefits of social media. "I think where they can really leverage the tools of social media is with project-based engagement – where managing projects via email attachments is not necessarily efficient," she says. There are various applications now on the market which can provide more transparent work schemes, which can enable treasurers to share resources, track items, and using the cloud source innovation to effectively collaborate remotely with other colleagues in different locations.

"One of the tools that we use at my company is a platform called Yammer," she says. With approximately 72,000 employees at CGI globally, Yammer, a private social network for enterprises, is an extremely useful engagement system to have, she says. "It is a fantastic tool for identifying and communicating with individuals within the organisation," she says. "Whether the individual is in Europe or Asia, finding the right person and then learning from and leveraging their expertise is a lot faster and more efficient than using traditional communication methods."

But is it safe?

The emergence of enterprise-specific social communications technology, such as Entarena, Buzzumi and Yammer, shows that traditional social media technology is being adapted in some innovative ways for the corporate finance community. And as a result, there seems to be a growing consensus that social media can indeed provide tangible benefits for the treasurer and other professionals. But what might hinder greater acceptance of social media technology in the world of corporate treasury?

Security is one area of concern that continues to be a stumbling block to companies and business professionals in relation to social media. But Andres refutes the suggestion that this unease will persist in the long term. "Obviously all finance departments have concerns around the security of their financial data," he says, "but look at market trends – you now have treasury and payment systems that are software-as-a-service (SaaS). Clearly these security concerns are diminishing. IT departments always look into the security aspect and in most cases they come to the conclusion that the technology is as secure, if not more secure, than internal systems."

Marovitz believes security may still be a concern within risk-adverse financial professions. However, these concerns merely strengthen his argument for enterprise-specific social communications over the traditional, less secure social media platforms, he says.

"I think that security remains a fundamental concern, which is why we built our product with security sensitivity in mind," Marovitz says. "Every single thing we do is encrypted, so you can't even come to buzzumi's marketing website without encountering encryption. Everything runs under SSL (secure sockets layer). We did all that at the beginning as a matter of course to ensure that we are positioned so that CIOs don't have any concerns over our platform," he says, adding that he wants buzzumi to be viewed as "rock solid". ■

You can follow Daniel Marovitz on Twitter: @marovdan

Adam Smith

Alan Greenspan, the American Republican economist and former Chairman of the US Federal Reserve, said that the life of government-controlled economies "ended with the fall of the Berlin Wall in 1989 and the collapse of the Soviet Union" and that the free market was "the sole remaining effective paradigm for economic organisation". If this is true, it places philosopher and political economist, Adam Smith, as the father of all modern economic thought and practice. But what did Smith propose, and do the words of a man writing hundreds of years ago in the Age of Enlightenment really still resonate with today's global economy?

With any great philosophical text, time inevitably draws out myriad readings and interpretations. Adam Smith (1723-1790) was a Scottish philosopher and economist working in the Age of Enlightenment. One of his key works, the 1776 publication 'Inquiry into the Nature and Causes of the Wealth of Nations', was the first in-depth study of how industry and commerce in Europe worked, and as such is taken by many as the basis for all modern readings of free market economics. By all, it is meant that there has been much disagreement as to what Smith meant and that this has been the bedrock of furious debate for a long time: whilst some view it as a genuinely libertarian statement, others have used it as a platform to create their own charter of greed and exploitation.

Smith's analysis of existing commercial practices – in which trading was a very insular and highly controlled affair – put the case for the adoption of a free (as opposed to highly regulated) market and the removal of restrictive tariffs. He proposed ground-breaking practical ideas on the division of labour within the production process (long before Henry Ford) and also explored the profound psychological notion (in that it was contrary to contemporary thought) that human self-interest can (if moderated by the natural inclination to altruism) lead to wider and deeper social benefits through the development of industry and commerce.

The chain of events that followed the publication of the 'Wealth of Nations' were critical in enabling the Industrial Revolution to take a firmer grip of Britain (setting it up as the world's largest ever empire) and eventually most of the rest of the world, cultivating dramatic changes in agriculture, manufacturing, mining, transportation and technology. The effect of this period (between 1750 and 1850) of intense development and rapid progress had an inestimable effect on the social, economic and cultural life of millions.

As well as being the inspiration for Treasury Today's own annual Adam Smith Awards for treasury best practice and innovation, Smith's contribution to economics has seen him commemorated in bronze and stone in various locations around the world. There are various international economic think-tanks established in his name; and he became the first Scot ever to grace an English banknote (he is on the current £20 note, having replaced composer Sir Edward Elgar). He also features on the £50 note issued by the Bank of Scotland, making him the only individual to appear on two British notes concurrently.

Background

Smith was born in Kirkcaldy, Scotland in 1723. He studied at Oxford and Glasgow Universities, and was appointed at the latter as professor of logic in 1751 and then as professor of moral philosophy. Here, in 1759, Smith published his 'Theory of Moral Sentiments' to great acclaim.

In 1764, Smith gave up his position in Glasgow to travel the Continent as a tutor to Henry Scott, a future Duke of Buccleuch, and his brother, spending three years in France. Whilst travelling, he associated with of a number of leading European intellectuals including Voltaire, Rousseau, Quesnay and Turgot.

When Smith returned to Kirkcaldy, he began work on his 'Inquiry into the Nature and Causes of the Wealth of Nations'. This was published in 1776, the same year that he departed for London where he moved in an intellectual circle populated by the likes of Samuel Johnson (with whom he had a tempestuous association), David Garrick and Joshua Reynolds.

In 1778, Smith moved back to Scotland and was duly appointed commissioner of customs in Edinburgh (his father, who died before he was born, was a customs officer in Kirkcaldy). In 1783, he became a founding member of the Royal Society of Edinburgh, Scotland's National Academy of Science and Letters. Smith died in Edinburgh on 17th July 1790.

Commerce before Smith

Before Smith, national wealth was seen purely in physical terms, represented by the amassing of gold and silver. Exporting goods added to the stockpile of precious metals and was encouraged through the use of subsidies.

However, importing goods would deplete the stock of precious metals and was therefore discouraged, principally by imposing stringent taxes on incoming goods. These conditions led to the establishment of fiercely guarded trade routes and frequent trade wars, both of which came at a high cost.

The protectionist mindset pervaded the domestic trade scene as well. Tradespeople were prevented from moving between towns and cities to ply their business because local manufacturers and merchants could petition the king for protective monopolies (again, at a cost).

One for all and all for one … unintentionally

Having laid the groundwork for themes such as rational self-interest in his 'Theory of Moral Sentiments' (in which he also espoused the Enlightened view that humans have a natural sympathy for other humans), Smith expanded the notion and concluded that such a condition, if applied to competitive commerce, could lead to improved economic benefit for society in general. This was counter-intuitive for many (then and now) but he explains it thus: "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages." (The Wealth of Nations, Book I, Chapter II, pp. 26-7, paragraph 12). Because trade benefits both sides of the import and export space (few would trade without personal benefit), Smith argued that it must increase prosperity for all. It followed that protectionism was counter-productive and that only by opening up trade flow could the right conditions for general prosperity be achieved.

> "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest."
>
> The Wealth of Nations, book I, chapter II, pp. 26-7, paragraph 12

He was not advocating a conscious descent into chaos or unbridled greed (as in the 1987 film, Wall Street, where the central character, Gordon Gekko, famously states that "greed … is good"). Instead, Smith argued that a natural order would be imposed on trade, regulating the move towards society's unspoken goal of progressive improvement and fulfilment for all. The manifestation of natural order and harmony, unimpeded in a "well-governed society" (but, notably, without government intervention), is an unintentional by-product of self-interest and Smith likened it to being guided by an "invisible hand".

Every individual, he wrote, "neither intends to promote the public interest, nor knows how much he is promoting it, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention". (The Wealth of Nations, Book IV, Chapter II, pp. 456, paragraph 9).

Smooth operator

The 'Wealth of Nations' also proposes another radical departure from the norm, with Smith turning his attention to contemporary production techniques. The current British £20 note shows a picture of a pin-making factory. Smith had spent some time analysing the handcrafted workings of this manufacturing business. He concluded that far greater efficiencies could be achieved if each major production process (18 in total) was divided into a set of simple tasks which would be performed by specialised workers. His recommendation is reported to have increased production 240-fold.

The kind of savings that could be made in most operations would leave the factory owners with a surplus that they could exchange with others (and thus add to the general health of the economy) or plough back into the business in the form of more efficient machinery. From which could be derived even greater surplus (contrary to Smith's expectations, this gave rise to the Luddite movement – 19th Century English textile artisans who violently protested against the use of machinery to replace them with less-skilled, low-wage labourers, leaving them without work).

The specialisation of labour would extend to all means of production of a society in that (in today's market) we have engineers, artists, administrators and so on, each offering certain skills, using them to create personal wealth in exchange for the output of the skills (and/or the means of production) that they do not have (it also informed the Marxist concept of alienation as many, mostly unskilled workers, lost sight of the purpose of their engagement with their jobs).

As Smith saw it, in a commercial society, each person becomes a trader of their own labour. As with all goods and services, rarity drives up cost because people will pay more for it. As profit from supply increases, so producers will invest more capital into production. If there is a glut, prices and profits will fall and so producers will shift their capital elsewhere. It is the basis of supply and demand, guiding industry to deliver the goods and services that society deems the most important (at a price that those who desire them deem acceptable, ie what the market will bear).

The process of specialisation extends to nations too, said Smith. He offered as an example the folly of trying to make wine in Scotland, when it can be done so much easier and cheaper in France. His point was that countries should stick to what they do best; exporting to countries that need those goods or services and importing what they can't do themselves. A well-worn quote from 'Wealth of Nations' sums it up perfectly: "It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy . . . What is prudence in the conduct of every private family, can scarce be folly in that of a great kingdom." (The Wealth of Nations, Book IV Chapter II, pp. 456-7, paragraphs 11-12).

Automatic for the people

Whether at an individual or national level, Smith saw the process as self-regulating and automatic. But he insisted that it can only work where there is healthy free trade and competition, and where the rules of fair play are observed by each player. As soon as monopolies, tax preferences, tariffs and other such controls and privileges are introduced by the authorities, the whole system becomes distorted or collapses because price and demand fail to reach their natural levels and one party or another will be disadvantaged.

A hundred years earlier, in 1651, English philosopher Thomas Hobbes had written (in 'Leviathan') that "the condition of man is a condition of war of everyone against everyone". Hobbes here refers to a life in the raw, a condition without government. Hobbes was responsible for developing some of the fundamentals of European liberal thought, and notably promoted the idea of social contract theory in which people submit to the rule of law in exchange for the protection of the rest of their rights.

Smith argued that government interference in the free trade process was essential but that it must be limited to upholding the rules by which it could be sustained, in as much that property could be kept secure and contracts would be honoured (what he called "natural liberty"). For him, justice and the rule of law is a key part of the free trade process and so governments should stick to their core functions, which he lists as maintaining defence, keeping order, building infrastructure, promoting education, and of course, keeping the market economy open and free and resisting any action that could distort its natural progress.

> "It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy … What is prudence in the conduct of every private family, can scarce be folly in that of a great kingdom."
>
> The Wealth of Nations, book IV, chapter II, pp. 456-7, paragraphs 11-12

On the matter of taxation, Smith argued strongly that where it has to be raised for the purposes of upholding government function, the rate paid should be in strict proportion to the ability of the individual to pay, with transparent rates for all. He also urged governments not to tax capital, which he saw as a key part of national productivity, and to avoid building up large debts which, he noted, draws capital away from future production.

Smith in the modern world

One of the most prominent modern-day followers of Adam Smith's economic theory is Alan Greenspan, the American Republican economist. Greenspan served as Chairman of the US Federal Reserve from 1987 to 2006 and was similarly convinced that the economy works best with less government regulation. He cited the 'Wealth of Nations' as "one of the great achievements in human intellectual history".

Greenspan commented that although Smith did not introduce the term laissez-faire economics (eg. don't let government interfere), he did "identify the more general set of principles that brought conceptual clarity to the seeming chaos of market transactions".

Greenspan was devoted to the life and works of Russian American philosopher and novelist, Ayn Rand. Rand created a philosophical system, which she called Objectivism, that basically stated reality exists separately from consciousness, and that direct connection to reality comes via sensory perception. Mankind, she wrote, "must live by the independent judgement of his own mind; that his highest moral purpose is the achievement of his own happiness . . . that each man must live as an end in himself and follow his own rational self-interest".

Rand believed that the only social system that afforded respect for individual rights was that embodied in laissez-faire capitalism and that the proper functionaries of a government (police, army etc) existed solely to ensure the system and its players could carry on unhindered. Although some of these ideas resonate with Smith's, a key difference is Rand's insistence that altruism undermines the individual. As Maria Bustillos, writing for 'The Awl', commented: "The possibility that the unfettered egoism of guys like Stalin was the main problem with the Russian government, rather than too much altruism, escaped Rand entirely."

Another torch bearer for Smith was former British Prime Minister, Margaret Thatcher. Apparently, she carried a copy of the 'Wealth of Nations' in her handbag (at 600 or so pages long, presumably there was little room for much else). In 1979, her Conservative government rose to power on a promise of lower taxes, smaller government and freer markets. In 1986, Thatcher's close ally, US Republican President, Ronald Reagan (another Smithian devotee), said: "Our trade policy rests firmly on the foundation of free and open markets". He added that "the freer the flow of world trade, the stronger the tides of human progress and peace among nations." He did, somewhat hypocritically, adopt a harsh protectionist view when it came to imports from Japan and his Treasury Secretary, James Baker, claimed that Reagan had granted "more import relief to US industry than any of his predecessors in more than half a century".

Wrong reading

One outspoken critic of right wing readers (and practitioners) of the 'Wealth of Nations' is American academic, Noam Chomsky who commented in his 1995 book, 'Class Warfare', that "what we would call capitalism, he despised".

His only research on the subject, he stated, was actually reading the whole book. Chomsky believes that most people just read the first paragraph where Smith discusses the benefits of the division of labour, "but not many people get to the point hundreds of pages later, where he says that division of labour will destroy human beings and turn people into creatures as stupid and ignorant as it is possible for a human being to be".

With this in mind, Chomsky detects Smith's opposition to wage labour and corporations and his cutting remarks about how the principal architects of policy are (in Smith's words) the "merchants and manufacturers" who make certain that their own interests are "most peculiarly attended to", no matter what the effect on others. This, says Chomsky, is a truism of class analysis, adding that "you don't have to go to Marx to find it. It's very explicit in Adam Smith."

> "Not many people get to the point hundreds of pages later, where he says that division of labour will destroy human beings and turn people into creatures as stupid and ignorant as it is possible for a human being to be".
>
> Noam Chomsky

Smith was speaking from the perspective of the Enlightenment. "His driving motives were the assumption that people were guided by sympathy and feelings of solidarity and the need for control of their own work, much like other Enlightenment and early Romantic thinkers," said Chomsky. "The version of him that's given today is just ridiculous." ■

The art of simplicity

Neil King
Group Treasurer

Carphone Warehouse

Neil King joined Carphone Warehouse as its first Group Treasurer in 2000. Treasury Today talked to him back in September 2004 about how he established a new treasury department in a rapidly growing company. In this issue we revisit the company and hear just how far his treasury operation has come in the intervening years.

Carphone Warehouse Group (CPW) is the largest independent mobile phone retailer in Europe. The UK-based firm owns and operates about 2,400 retail outlets across the region. Outside the UK and Ireland, it trades as the Phone House. CPW's current treasury operation consists of two teams, each with a treasury manager: one carrying out projects and development and the other covering operations. In total, the whole function is staffed by seven "jacks of all trades", where previously it had accounted for up to 14 staff (immediately pre-demerger from TalkTalk).

There have been a number of significant changes to the structure of CPW since Treasury Today last caught up with Neil King, Group Treasurer at Carphone Warehouse (CPW), at his West London office. Not least of these have been the joint venture established in May 2008 with US firm, Best Buy Inc, and the de-merger of CPW's own Talk Talk business in 2010, the latter leading to the development and eventual departure of a parallel treasury team.

It would be natural to assume that these events impacted heavily on CPW's treasury operation, but Best Buy were "particularly hands-off" as far as treasury was concerned; King still runs the function for all of Europe and funding remains external. However, he has taken a number of practical and far-reaching decisions in the intervening years as to how to best run the treasury operation. All things considered, one aspect has remained remarkably and impressively constant, and that

is the steadfast adherence to the spirit of what is called by others the KISS principle. KISS, for the uninitiated, means keep it simple, stupid. In a world dominated by complexity and change for changes sake, his approach is refreshing.

The principles of treasury for King are about identifying what you have and keeping it simple. "I cannot see any requirement, unless there is a direct cash benefit, to do anything other than in the simplest way," he states. Challenges are issued to businesses within the group from time to time regarding complexities that have become apparent – perhaps around the increasing number of bank accounts or multiple levels of pooling or sweeping. "Sometimes we work with them to simplify things but other times we have to impose it." Most subsidiaries view this process from the perspective of the good of the group as a whole, not just isolated units looking after themselves.

The view of doing what is best for the group is one shared by CPW's board. Since the de-merger, King has enjoyed a treasury-specific power of attorney for every company in the UK group and for some overseas entities. This vote of trust enables him to take significant decisions on many treasury matters (with some, nevertheless, being retained by the board), speeding up the process of decision-making and bringing further simplicity to the function.

The more things change …

CPW reached a peak of complexity in 2007/08, just before the joint venture. "Since then, matters have actually simplified as parts of the business have gone," recalls King. Back in 2000, the plan was to expand into more European countries but CPW has retrenched to a certain extent, having sold off the retail business in Switzerland and pulled out of Belgium altogether. It is still very much a western Europe-focused company. By limiting expansion, for now, it keeps certain funding complexities at bay, although retrenchment in part due to the individual economic and commercial environments in each country. "We are in the markets where we feel there are positive commercial opportunities," he states.

King remains true to his belief that for CPW, centralisation is the only way of running an efficient treasury. It is led by a set of "firm treasury policies": for example, he insists that there can be no unsettled inter-company balances anywhere in the group other than for direct funding, except with his specific approval, which might be given, for example, for a specific tax structure. He admits to being quite a "stern task-master", requiring documentation and adherence to agreed policies, but has concluded that this level of control is essential to ensure the efficiency of the treasure operation.

Currently, all funding is provided automatically across the group through a zero-balancing structure although this is likely to change during 2013 as individual currency pools are established at different banks and the overlay structure dismantled. This management of inter-company funding gives treasury "a lot of comfort", especially as group cash flow is continually scrutinised, King commenting that CPW has "the best knowledge of our cash flow that we've ever had right now".

Flexible friend

Through good times and bad, CPW's treasury priorities have remained much the same: security of the company's cash, funding and liquidity. It is, however, harder to stay true to some policies when times are tough. As such, certain processes may witness a degree of flexibility. In a period of almost zero interest, when trying to explain the time-value of money and the strict policy of centralising liquidity to junior treasury personnel, King acknowledges that he will be challenged (and readily admits that his own view is sometimes split) when it comes to adopting "the correct traditional behaviour" or being more pragmatic about the way in which the firm funds itself.

The effect, over the last six to 12 months, has been that whilst CPW's treasury is fully centralised, the company has started to permit, and even encourage, the uptake of some local bank facilities to assist in managing liquidity at the local level. Some of these facilities have been carved out of the main revolving credit facilities (RCF) as 'ancillary facilities', the accommodation of which led to the RCF being extensively amended last summer.

Translational hedging simplified

Although some local costs may come in a 'foreign' currency, CPW is not an exporting company; it exists to sell in its local markets. In 2004, the plan was to move towards loans made in the local functional currency of each unit; this has now become "absolute policy" with the group running a strictly controlled translational hedging policy. The absolute nature of this policy is extended to ensure that no business unit can hold a bank account in anything other than in its functional currency. "We encourage our businesses to be sensible and protect their margins by hedging if they wish to, but we do it centrally, settling everything through the netting system." The netting system is run every two weeks and covers all external currency payments and all foreign exchange (FX) deals for the subsidiaries, as well as the more traditional settlement of inter-company balances.

Implementation of the policy was "not hugely popular at first" as everyone had to work to a fortnightly cycle rather than being able to pay at will. But most now see the benefit of not having to account for FX contracts, revalue banks account and so on. It's simpler and there are hopefully no surprises from FX coming up through the accounts; the central treasury knowing about currency issues in advance, and monitoring its foreign exchange positions every day. "As far as possible, I think we've taken that area of transactional risk out of the system," states King, adding that "probably to the sadness of many of our banks, FX is now not a large part of what we do."

Finding funding

In terms of funding, it has become almost "second nature" for CPW to be involved in refinancing, having done so more than a dozen times since 2004. CPW remains cash-generative and its gearing is "modest"; its current needs are therefore met by its current core banks and won't now be re-financing until next year. It has never used the bond market, however, in 2009, when times were rather "interesting", CPW used its significant receivables (mainly from the well-rated mobile networks) to structure a secured facility that was used to the early years of the joint venture with Best Buy. "It was the only way we could get the amount of liquidity we required," recalls King, noting that it was "expensive and difficult". By July 2011, he had refinanced that deal back into the more straightforward bank market.

Outsourcing and technology

King's team runs part of the payments function (the disbursement of cash), but the shared services centre (SSC), which was established in Portugal for CPW in the early 2000s,

was fully outsourced around two years ago to operations in India and Romania (the choice of location depending on the countries being covered). This now acts as the payments factory (with internal authorisation) and handles most management accounting, accounts payable (AP), cash reconciliations and so on.

In 2004, most the of investment management of the significant insurance reserves (CPW has an insurance company providing handset insurance for customers) was outsourced to professional fund managers but this has been progressively, and now fully, brought back in-house. The rule of simplicity (in part a response to increasing regulatory pressure in the insurance industry as well as smaller amounts being retained in reserve anyway) has been applied, with much stricter parameters and transparency brought to bear on investments (mainly money market funds (MMFs), via ICD's platform, and bank deposits). This, says King, has served CPW well, "allowing us to retain liquidity and security of our funds during the last few years of uncertainty".

The TMS used by CPW (the old Richmond system, now part of the Wall Street Systems portfolio) is delivered on an ASP basis (and linked closely to CPW's other systems). But this is going to be opened up for tender in the 2013/14 financial year; the system search naturally placing simplicity and cost somewhere near the top of the requirements. By this time, every system the company uses will have been tendered at least once since the de-merger, comments King. "It's useful to look at these things with an eye to saving money."

CPW has also engaged with the SWIFT bureau, Simplex, (it could not justify the cost of its own direct membership). Once live, connectivity will allow the group to submit its own payments files, direct debits, take confirmations and so on. The roll-out will start with bank reporting and by the time the Single Euro Payments Area (SEPA) project has finished (CPW will be SEPA-compliant for direct debits (SDDs) shortly with SEPA credit transfers (SCTs) following later in the year) this too will function via the bureau and not a bank platform. King anticipates "modest savings" here in terms of bank fees, but through automation also expects efficiency savings. Importantly, it also means CPW heads closer towards bank systems' agnosticism.

Some of the new systems being brought in display a degree of complexity. But, as King comments, they will make the operation much more efficient. "And I don't see that the complexity of systems steps away from the idea of a simple treasury; we're just trying to do our simple things in a much more efficient manner."

Since 2004, CPW has been through a lot of changes and King admits that systems development had, for the duration, not been a priority and had possibly fallen back in terms of more recent treasury trends and developments. It is now improving its systems and one of the key aims is to ensure treasury is no longer beholden to bank software. "In talking to other treasurers," says King, "they say the same thing – they would like not to be tied to their banks."

SEPA is coming

SEPA figures hugely in the life of CPW. It has a major IT project (ongoing since November 2011) to become SEPA-compliant "as quickly as possible". "We will have to be compliant anyway by February 2014; we want to be done by summer this year," King states.

The first tranche of the SEPA project covers direct debits, catering to many of CPW's insurance policy holders across Europe and the UK who pay by this means (and amounting to millions of items each year). SCTs will follow: the evidence is that this too will be significantly cheaper, notes King. To expedite matters, CPW has a full-time developer working solely on this project.

The SDD process will be fully automated and managed by a single bank, giving CPW same-day use of the funds, which in itself provides satisfying efficiencies by removing intrabank transfers. By using one bank and arranging a standard tariff, CPW will significantly reduce its costs (close to £700,000 – gross of Simplex and other systems charges – in a full year on bank charges alone, notes King). There is more: "We will become bank agnostic and be able to change banks much more quickly, if we choose to, once we've done all this work."

Banks: all change

Back in 2004, the process of bringing in Deutsche Bank (DB) as an overlay bank was just being completed. The decision to go down the SSC route meant it was also due to become CPW's payment factory provider. In effect, DB scooped up most of CPW's cash management business, except for some local cash collections. Handing so much to one institution was beneficial at the time because it allowed CPW to dispense with multiple banking relationships across multiple countries, bringing discipline to proceedings. With cash being pooled more efficiently it also reduced idle cash and reduced interest costs.

But now, states King, "the lesson that cash is a valuable resource has been fully learnt, right across the group" and over the past few years there has been a change of direction, and, with DB no longer central to the funding of the group, there will no longer be just one bank handling all cash management, with CPW instead splitting its cash management by currency, which may lead to different banks handling different currencies. Optimising cash management remains important but CPW has now found reason to go beyond the "one-size-fits-all" bank. "It was great for the discipline and gave us huge benefits for many years. But it did start to become hardwired into our systems and our brains," explains King.

Breaking out of the routine and becoming more imaginative was "quite hard work", especially on the IT side. In fact, the consolidation of banks in summer 2011 (from 16 to six: three UK-based, one French, one Dutch, one Swedish) was quite an upheaval in itself, he admits. Those banks that remain have worked towards "trust and understanding" and have realised that they now have "a seat much closer to the head of the table": all are equal in terms of distribution of business and all strive to provide an equal service. "We've got closer relationships now with our six banks than we ever did with 16," King says. It would seem logical to expand the core banking group to cover CPW's geographical footprint, and a Spanish and German institution would seem likely as markets recovers.

New challenges

Having a firm grasp of CPW's treasury operation means the next challenge for the team is really just the old challenge – that of "doing it all properly". "I'm sure we'll never get an award for being the most inventive treasury," says King, "but we have done everything we have set out to do and we've done it properly; we're still here, we are solid and well-funded, which is as it should be." ■

An uncertain future for money market funds

The road to money market fund (MMF) reform has been politically laborious. But the fund industry has suffered from a number of other challenges that leave providers struggling to find investible assets and maintain yields. What can market participants expect in 2013?

The coming year will no doubt bring with it some money market fund (MMF) proposals from the US Securities and Exchange Commission (SEC), as well as further reforms in Europe, in particular regarding constant net asset value (CNAV) MMFs.

In addition to these reforms, MMFs are battling myriad other difficulties: the European sovereign debt crisis, concerns about the stability of European banks' credit quality, negative yields in Europe and fiscal cliff remnants in the US. Furthermore, the Federal Deposit Insurance Corporation's (FDIC) unlimited deposit insurance coverage expired on 31st December 2012. If these vulnerable deposits are reallocated into MMFs and money market securities, it may push short-term investment rates down even further.

Managers of MMFs are already struggling to maintain investments that deliver positive returns despite low interest rates. Prime MMF sector gross yields have fallen from more than 0.75% per annum in January 2012 to around 0.13% per annum in December 2012. In an industry where liquidity and stability of investments normally trumps yield, tough market conditions are forcing fund managers to dedicate their efforts to generating yield against all odds. However, with returns on short-term MMFs trending lower and the supply of suitable high quality issuers declining, options are becoming increasingly limited.

The MMF industry is no doubt preparing itself for upheaval and modification with the introduction of inevitable reforms. But the global financial arena is also shaping the structure and various management approaches to funds and certain

portfolios. The MMF environment has become quite a different one to the investment arena it once was.

Reforms and ratings

Ever since the Reserve Primary Fund 'broke the buck' (fell below one dollar a share) in September 2008, financial market regulators have stressed the need for additional MMF regulations. In 2010, the SEC adopted revisions to the regulations to enhance the resilience of MMFs. But when former SEC Chairman Mary Schapiro announced in August 2012 that the majority of SEC commissioners did not support her reform proposals for MMFs and therefore was not proceeding with a vote to solicit public comment, the money fund industry was suitably relieved. However, subsequent public comments indicate that additional reform is almost certain – the date that this is set to happen is rather more unpredictable. But by deciding not to hold a vote, Schapiro effectively handed the issue to the Financial Stability Oversight Council (FSOC).

Alastair Sewell, Director, Fund and Asset Manager Rating Group at Fitch, believes that the pace of MMF reform could accelerate significantly in 2013. "In the US, SEC Commissioner Luis Aguilar recently voiced his support for a floating NAV structure for MMFs, which makes it more likely for this option to be carried out by the SEC," he says.

"This follows the FSOC proposals in November 2012 for MMF reform. These proposals included amendments to the existing MMF structure such as a floating NAV; a stable NAV with NAV buffer and "minimum balance at risk"; and a stable NAV with NAV buffer and other measures." The public commentary period on the FSOC proposals, which was to close on 18th January 2013, has been extended to 15th February "to allow the public more time to review, consider and comment on the proposed recommendations".

MMF regulation is also picking up worldwide. The International Organisation of Securities Commissioners (IOSCO), which the SEC is a member of, has published its policy recommendations for improving oversight and regulation of the 'shadow banking' industry (which includes MMFs). These recommendations are intended to complement existing regulatory frameworks where the IOSCO believes there is still room for further reform – including the US. In addition, the European Commission (EC) under the Undertakings for Collective Investments in Transferable Securities (UCITS) VI report is considering whether CNAV funds should be subject to additional regulations, such as capital buffers.

Sewell adds: "The European Systemic Risk Board (ESRB) is considering the report published by IOSCO in October last year that suggests that the global MMF industry should be further regulated to reduce systemic risk. Specifically, IOSCO recommends additional safeguards for those MMFs using amortised cost accounting and offering CNAV per share. Furthermore, IOSCO recommends a conversion of CNAV MMFs to floating NAV MMFs through limited use of amortised cost accounting only for assets maturing below 60 days."

Fitch's rating criteria is applicable both to floating NAV and CNAV MMFs. Under its Principal Stability Fund Rating methodology, Standard and Poor's (S&P) also currently rates MMFs exhibiting a variable NAV as well as CNAV MMFs, according to Françoise Nichols, Director, Fund Ratings and Evaluations at S&P.

"We will monitor and review what impact further regulation of the MMF sector in the US, Europe and elsewhere may have on S&P rated MMFs. If CNAV MMFs were to become a less attractive investment opportunity (as a result of reforms), some investors may decide to move their investments to less regulated segregated managed accounts, or to directly transact in less diversified and liquid instruments such as bank deposits and/or repurchase agreements," he says.

Recently, major providers have taken steps to provide more transparency in their money funds, disclosing values on a daily basis rather than monthly. Following the announcement by Goldman Sachs of its intention to disclose values of their funds each day, J.P. Morgan, BlackRock and Dreyfus said they will also list NAVs each day. Seen by many as a positive development, daily disclosures may also make investors more likely to pull money out as a result of seeing minor discrepancies.

Alternative approaches

In the past 12 months, euro-denominated funds have faced the brunt of the harsh economic conditions, prime funds and government funds have been withdrawn. There have also been numerous downgrades of European financial institutions and sovereign issuers. As a result, some funds have diversified into issuers outside of Europe, albeit in smaller amounts and for reduced maturities.

Amid this unprofitable environment, numerous MMF providers announced soft closes restricting new accounts and placing varying restrictions on new investment from existing clients. The soft closes were introduced in the summer of last year following the European Central Bank's (ECB) move to lower its deposit rate facility to 0% with an aim to protect MMF investors from dilution risk, according to Nichols, but some have since modified their restrictions. "We see this trend evolving and predict funds reopening to new investors, since dilution risk has reduced, as higher yielding assets held by MMFs have matured.

"More recently fund providers have been looking at ways to handle negative yield for euro denominated MMFs. Certain providers have already announced fund restructuring involving a share cancellation mechanism to compensate negative yield and continue to maintain a CNAV," he says.

In response to the prevailing low yields and a risk of deterioration of MMFs' NAV, J.P. Morgan Asset Management (JPM AM) is one such provider that has elected to employ unconventional measures. The investment firm's board of directors decided to restructure its euro-denominated MMFs, making share class amendments and updating the investment objectives for both the J.P. Morgan Euro Government Liquidity Fund and the J.P. Morgan Euro Liquidity Fund.

Sewell recognises the proactive approach European MMFs have taken to deal with the unfavourable future and offset the potential impact of negative rates on NAV. "Negative MMF yields stemming from the short-term market rate environment would not be a negative rating factor per se for Fitch-rated MMFs, including for those rated at 'AAAmmf'," he insists.

"Some fund complexes have already implemented new share class structures to pass on potential negative yields to fund investors. We expect several others to follow suit in the coming weeks. The essence of the negative yield distribution mechanism is based on keeping the NAV per share stable at the initial subscription price per share. Thus, if a fund suffers a negative overall yield then the fund redeems pro-rata investor shares such that the NAV per share remains stable (ie the

number of units (shares) in the fund can vary, but the value per share remains stable at one)."

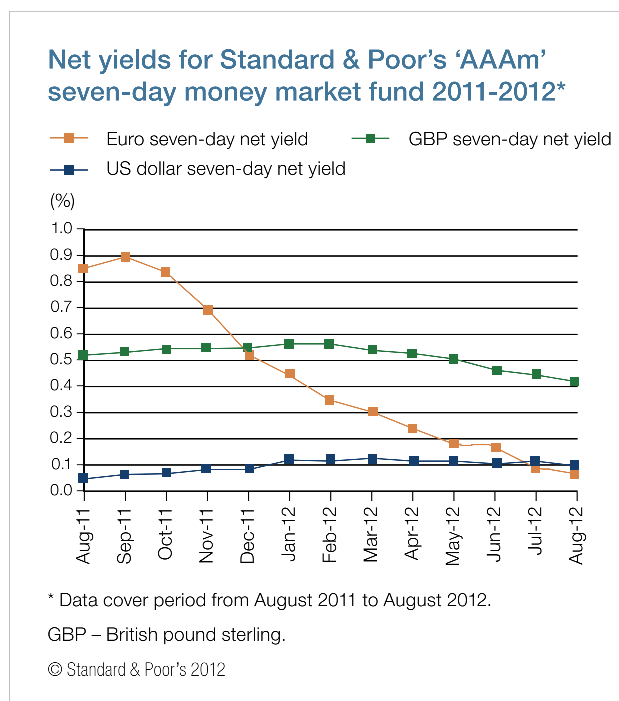
The introduction of flex shares is designed to ease investors' accounting and tax issues through maintenance of share values at par. Yet the net result is that investors lose capital and this, according to some market experts, is at odds with the AAA ratings definition (Moody's cites the ability to meet the objective of preserving capital as one of the key measures). That said, it can be argued that a MMF is a lower risk proposition than direct investment and that yields, although potentially negative, should compare favourably with market returns on similarly high-grade and liquid investments.

According to a Moody's whitepaper, changing the fund's structure is credit positive for JPM AM as it will enable it to operate in both a negative and positive yield environment. "Such flexibility will empower JPM AM to retain current investors and attract new assets under management (AUM), resulting in higher MMF revenues," says the report.

MMF managers feel the strain

Elsewhere, the burden on providers continues to ramp up. With the pressure to achieve yield while remaining risk averse, portfolio managers have placed heavier reliance on barbell strategies. In the US, MMFs are expected to attract new assets as a result of the end of the FDIC's insurance on bank deposits. This may place pressure on yields offered by US MMFs, according to Nichols. Furthermore, some generalist fund providers are focusing on distributing product generating higher fees than MMFs, resulting in further product rationalisation and consolidation in the industry.

Net yields for Standard & Poor's 'AAAm' seven-day money market fund 2011-2012*



* Data cover period from August 2011 to August 2012.

GBP – British pound sterling.

© Standard & Poor's 2012

Source: Standard & Poor's

"The extremely low level of yield for euro-denominated MMFs has led some providers to offer higher yielding alternative products to their investors, which may be less liquid or riskier than 'AAAm' rated short-term MMFs," he explains. The declining yield environment, reduction of eligible supply and tightening rating requirements have each, to varying degrees, impacted and accelerated the level of consolidation in the euro Institutional Money Market Funds Association (IMMFA) space, which represents European AAA rated MMFs, according to Mark Stockley, Managing Director, Head of International Cash Sales at BlackRock. "Consolidation to date has principally occurred with those providers who had smaller sized funds, limited distribution and have found managing their euro funds challenging."

This theme of consolidation is a concept Sewell agrees with, mainly among MMF managers that are sub-scale and do not derive synergistic benefit from MMF offerings. "Niche MMF players are already under material profitability pressures in this prolonged, ultra-low interest rate environment. The impact of low yields on fund manager fees may cause some managers to reconsider their strategic commitment to the cash management industry. "In instances where MMF managers apply management fees, waivers are likely to persist, especially for US dollar-denominated MMFs, to maintain a positive yield to investors. We would question how sustainable these fee waivers are especially for small to mid-size MMF complexes," he says.

And while Mike Hughes, Global Head of Fund Services, Deutsche Bank, doesn't expect the larger players pulling back from the MMF market, he also notes that: "total expense ratios (TERs) are under severe pressure given the interest rate environment. Few MMF managers can really afford to absorb any fees, yet are being forced to subsidise charges from banks, administrators and custodians to protect TERs."

An ongoing battle

The MMF sector would no doubt benefit from the resolution of the European sovereign debt crisis. A likely by-product of the resolution of this issue would be an increase in issuance of MMF-eligible securities due to the potential improvement in economic activities. According to Sewell, Fitch expects the limited supply of high quality short-term assets to continue to be one of the major challenges for the MMF sector in 2013, especially those portfolios denominated in euro and sterling. Nonetheless he remains positive for the future of the MMF industry and Fitch's global outlook for MMF ratings in 2013 is stable.

"We see a few interesting trends: first, towards collateralised exposures (repo, ABCP); and second, to non-traditional geographies – we have seen an uptake in exposure to issuers from Asia in particular, although outside of US dollar denominated funds issuance levels will limit uptake in MMFs. We would expect liquidity levels to remain high in 2013, but weighted average life (WAL – used to measure credit risk)/weighted average maturity (WAM – used to measure interest rate risk) will increase slightly as funds selectively add longer dated exposures to higher quality issuers," he says.

As the regulation debate on MMFs continues, market participants will likely present alternative ideas as they look for common ground on which to operate and aim to maintain a thriving fund industry. However, achieving sustainable yield and currency stability in the volatile financial climate will also play a major part in defining a new, improved fund environment. The question is: will the arduous search prove successful enough to restore investors' confidence in MMFs, and thus stabilise the future of the industry? ■

Three steps to SEPA

The background to and benefits of the Single Euro Payments Area (SEPA) have been widely discussed. With the migration deadline of 1st February 2014 fast approaching, corporates should be seriously considering how they can make SEPA-compliance work for them. But for Deutsche Bank's Karsten Becker, Senior Product Manager, European Corporate Payables and Receivables, now is also the time for action. So, for treasurers who have yet to embark on a SEPA project, what needs to be done?

This is a high-level call to action. SEPA is looming, and corporates that fail to act could very quickly be looking at failed payments and perhaps far more serious consequences. The financial and practical benefits of SEPA have seen much publicity since the idea was born and, at this late stage, corporates should focus on these benefits – rather than dwell on the negatives of non-compliance – as they make plans to migrate. That being said, all migration plans – whether spurred into action by fears of missing the deadline, or in anticipation of the potential gains – must begin with solid advice and guidance.

Advice for corporates

There are three basic steps that must be taken and, given the amount of work that needs to be done, the pressure to start now should not be resisted, despite the myriad other projects competing for your time, effort and resources.

Step 1. Take a realistic view of where you are today and identify the gaps between this point and where you need to be

This means finding answers to questions such as:

- In what ways does SEPA impact your organisation?
- How embedded are local payment formats in the company's processes?
- Is the company BIC and IBAN ready?
- What third party software (ERP/TMS) do you use and is it able to accommodate SEPA (eg. for reconciliation)?

At this point, it is important to recognise that a SEPA project will require both budget and time. Analysis tends to be one of the longer phases of a SEPA project. Corporates that are entering this phase now do not have the luxury of time to take a leisurely approach to systems and process analysis, especially as the follow-on phases should be completed before financial year-end processes start to freeze certain activities, especially around IT. With this in mind, a February 2014 deadline realistically means a November 2013 deadline and reaching project completion before the end of this year should be the goal.

Action points here:

- Appoint a project team – in-house and with your key partners (banks/vendors).
- Ensure internal lines of communication stay open and that everyone across the organisation – including senior management – understands the risks of not being SEPA-compliant.
- Review administrative processes and systems. Identify areas that are lacking – eg mandate management for the SEPA Direct Debit (SDD), or the capacity to deploy the ISO 20022 XML message format.

Step 2. Get a plan in place and take action to upgrade your infrastructure

Whether opting for a wholesale changeover to SEPA, or a phased roll-out of changes, corporations need to have a migration plan. Points to consider when drawing up the plan include:

- Will you roll out SEPA on a country-by-country basis? (Bear in mind the country-specific requirements).
- Will you adopt SDDs or SEPA Credit Transfers (SCT)? Which will you adopt first?
- How will BIC and IBAN be obtained? Is a vendor solution appropriate?
- Will the company do its own mandate management for SDDs? Or is a third party solution preferable?
- Does the company require systems updates in order to be SEPA-ready (eg IBAN, XML)? If so, what specifically is required?
- What documentation changes are required?

Once these questions have been answered, a final plan should be drawn up that outlines deadlines for each part of the project to be in place. When looking at a timescale for the project, remember to allocate sufficient time to roll out the changes and don't forget to incorporate adequate time to test them.

Step 3. Make the change

The third step is to execute the migration plan, while paying attention to accounts information and reconciliation processes, which can often go under the radar. Some final checks will be necessary at this point and these should include answers to the following:

- Are all your payment processes SEPA-ready? (You do not want to be stuck with failed payments or face huge wire bills because you were unable to pay a supplier or an employee, for example).
- Are the company's collections SEPA-compliant?
- Have the reconciliation processes been adjusted?
- And what about all the associated IT processes – can the ERP reconcile with SEPA formats?
- Have all stakeholders – internal and external – been adequately consulted and kept fully up-to-date with the changes?
- Have staff been trained appropriately on SEPA? This could be anything from new software to new procedures.

SCT projects are often tackled before their SDD counterparts, but in reality there is no requirement regarding the order taken. Either way, there will almost certainly at this stage be an overlap between some of the steps and elements of the project. Companies should be looking to complete the analysis phase by the end of Q1; carry out phase two's adjustments and upgrades to the IT infrastructure by the end of Q2; and aim to have account information, migration and testing finished by the end of Q3. This will leave a buffer zone into Q4 for any clean-up activities that may be required (bearing in mind that this may also run up against year-end procedures).

While the project appears daunting, for corporates investing time and resources now, as well as setting aside a window of around two to three months for each step, migration to SEPA can still be accomplished in time and pave the way for a centralisation project. However, while SEPA is a real driver for centralisation, the time remaining to migrate means any centralisation project will need to be conducted separately. SEPA compliance by the deadline must be the absolute priority now.

In the event of non-compliance, the worst case scenario is that it may not be possible for the banks to execute certain payments. This may be the case if, for example a payment file which otherwise carries all the necessary information, is not submitted in the required XML format. Businesses should therefore update their own ERP or treasury systems to support the XML file format, or alternatively consider sending their legacy file formats to a third party vendor for conversion.

While there are a number of important activities that must be tackled right away to meet the SEPA deadline, some of the most important "to-dos" for a successful SEPA-migration are:

- You must obtain all your required IBANs and BICs.
- You must upgrade and update your treasury or ERP systems in order to accommodate these and other SEPA requirements.
- You must ensure your payments messages are XML-formatted.
- If you intend to use SDD, you must start mandate management now.

This is a vital project and should be treated with the urgency and gravity it requires; the consequences of not being able to make your payments do not bear delaying the project.

The end result of SEPA-compliance will be well worth the effort. It is only once the 'get legal' phase is complete that the 'real' benefits of SEPA can be realised.

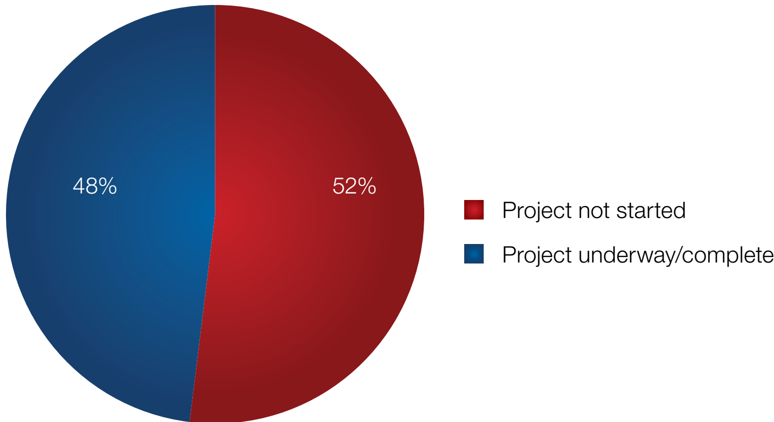
Countdown to SEPA – how ready are corporates for the February 2014 compliance deadline?

What is the current status of your company's SEPA project?

	SEPA zone	Outside SEPA zone
Not started	12%	61%
Evaluating options/planning	29%	15%
Planning, teams and budgets in place	11%	8%
Project under way and behind schedule	4%	1%
Project under way and on schedule	18%	5%
Basic SEPA compliance achieved and no further action planned	12%	6%
Basic SEPA compliance achieved and now seeking further efficiency	15%	4%

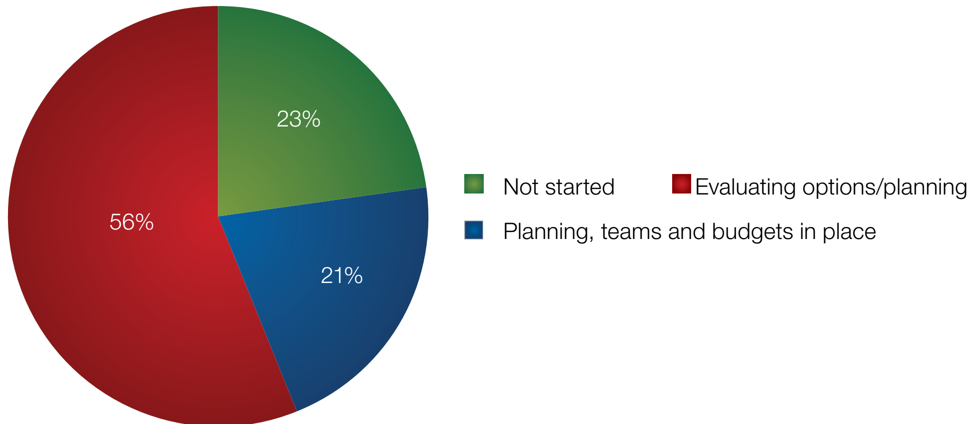
Source: EuroFinance

Analysis of SEPA zone corporates projects

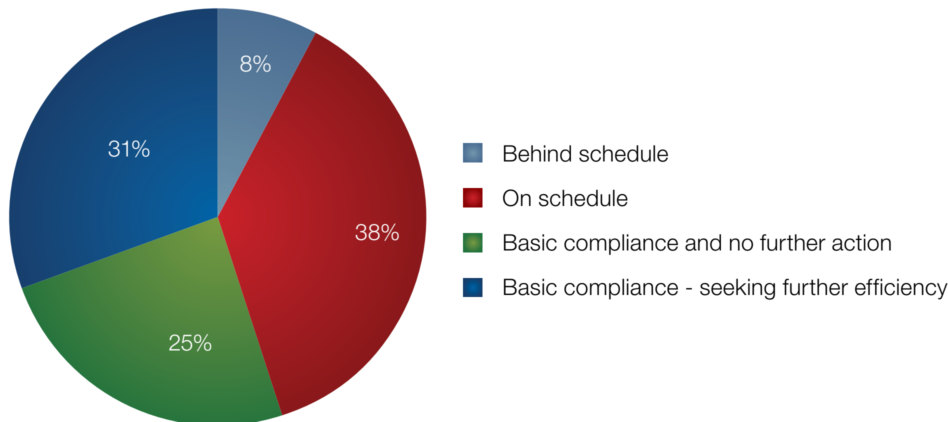


Source: EuroFinance

Project not started



Project underway/complete



- More than half (52%) of corporates in the SEPA zone have not yet started their SEPA project and almost a quarter of these have not even started to investigate the issue. Of those who have already started their SEPA project, 8% are already behind schedule, illustrating the size of the challenge ahead.

Source: EuroFinance

A total of 273 finance and treasury professionals responded to the Countdown to SEPA survey, which was sent out on 27th November 2012.

Respondents by organisation type: 89% of the respondents were from corporate treasury/finance departments. For the purpose of the analysis of the data, the answers were broken down for corporates based inside and outside the SEPA zone.

Karsten Becker is Senior Product Manager for European corporate payables and receivables. In this role, he is responsible for the development, positioning, and growth of corporate payables and receivables products, including legacy and SEPA credit transfers and direct debits. Before joining Deutsche Bank in 2007, Becker spent eight years in the US, where he held positions in product management and risk management for both Citigroup and The Bank of New York Mellon. Becker holds a Master's of Business Administration from The University of Notre Dame in South Bend, Indiana.

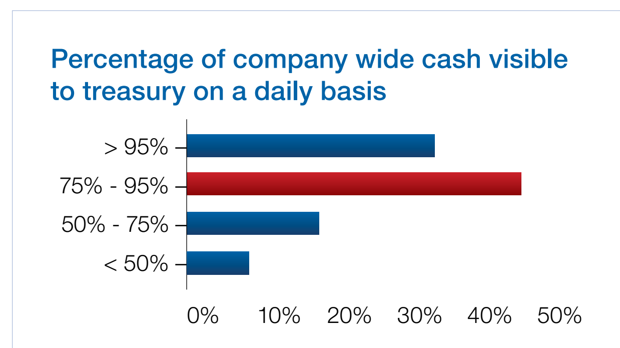
For more information and to download your Ultimate Guide to SEPA Migration go to: **www.db.com/gtb/sepa**

The visibility conundrum

Why are companies still finding it tricky to achieve desired cash visibility levels? Is technology the only answer, or are there more fundamental solutions that should be considered? Treasury Today speaks to leading treasurers from across the globe to find out more.

It may seem like a rather simple task, especially in the day and age of internet banking, but in practice, achieving full visibility across a group's cash position is often harder than it looks. And although some of you will be reading this, happy in the knowledge that you know how much cash you have and where it is, many treasurers will not.

For proof of this, just look at the results of Ernst & Young's April 2012 study entitled 'Reflecting on the future: a study of global corporate treasuries'. Approximately a third of treasury departments have daily visibility of more than 95% of the cash in the company, whereas just under half of respondents claim to have sight of 75% to 95% of the company's cash on a daily basis. Somewhat shockingly, nearly 10% of respondents have less than 50% visibility.



Source: Ernst & Young's, 'Reflecting on the future: a study of global corporate treasuries, April 2012

Failure to achieve sufficient visibility over the company's cash carries significant risk. In fact, without clear visibility, companies cannot adequately control group cash. In turn, this means they cannot use that cash at optimum efficiency, or maximise investment opportunities for it. Reducing borrowing costs and improving foreign exchange risk management will also be extremely challenging without full visibility and control.

"It is hardly surprising, therefore, that the majority of companies (69%) plan to further improve visibility of and control over cash," says the survey. The question, then, is how best to go about this?

Overcoming visibility hurdles

The level of cash visibility that a company can achieve will be heavily influenced by the level of centralisation, with centralised treasuries naturally having an advantage over their decentralised counterparts. In fact, centralisation is one of the key organisational tools that companies use to improve visibility. Elsewhere, the company's size and sector can affect visibility levels, as can the rate of growth of the business and its geographical footprint. Nevertheless, there are some fundamental considerations that all companies can take into account when identifying major challenges to visibility – and investigating how these can be overcome.

Technology

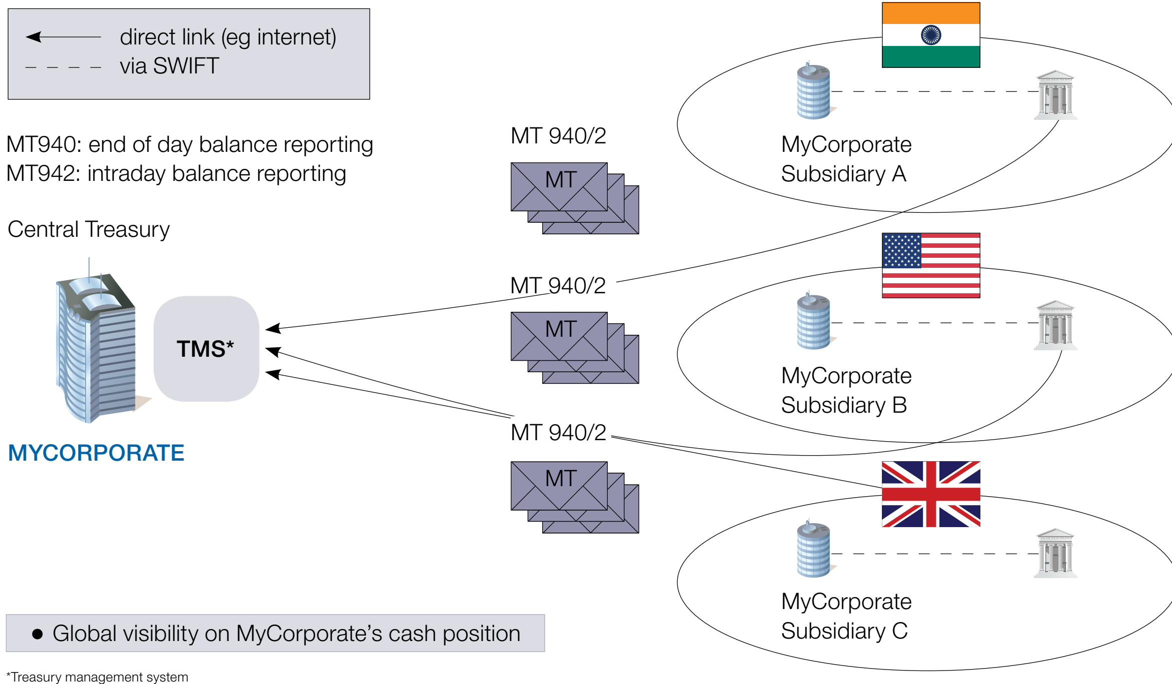
This is the obvious answer to most visibility challenges. In fact, visibility is largely an exercise in deriving cash positions by accessing up-to-date bank account balances – the art is how to make that as simple (and automated) as possible. "We just download the information we need from the relevant online banking systems. The majority of the work is done automatically, with some small amount of manual input," says Stephen Webster, Group Treasurer, QinetiQ. "As a FTSE 250 company, we don't have a particularly complex set-up or extensive international presence, so with the ability to access our entire bank balances online, we really don't find visibility to be a problem."

Many very large corporates, or those with decentralised operations, often do not find this quite so easy – with extended bank networks and myriad reporting solutions in use. This is where SWIFT comes into its own. "It's a great way to standardise reporting and get daily visibility over your global cash positions," says Julia Persson, Former Deputy Head of Treasury at A.P. Moeller Maersk. Similarly, Edward Mundt, Senior Treasury Manager at Asurion, believes that "with SWIFT reporting, any treasury management system (TMS) can give you visibility into the vast majority of your global cash." The diagram on the next page illustrates how this could work.

Many of the world's biggest corporates report vastly improved visibility through the use of SWIFT. In fact, Microsoft, which has in the region of 200 subsidiary businesses, 110 global bank partners and over 1,000 bank accounts, has reportedly achieved 99% visibility over global cash through the use of SWIFT's MT (FIN syntax) and MX (XML syntax) messaging standards.

Nevertheless, this solution isn't foolproof. "Not all banks use SWIFT to the full extent," warns Maciej Müldner, CFO, Skanska Romania. "This is one of the reasons that companies can find Eastern Europe a challenge from a visibility point of view. Take Romania, for example, with such low demand for SWIFT from corporates in the country, the value proposition simply isn't there for many of the local banks to support it." Certain Asian countries, such as Korea, pose similar challenges. "Even if you can get hold of an MT940 from the bank, expect it to be significantly more expensive than you are accustomed to in the US or Europe," says Asurion's Mundt. "Also, don't anticipate that it will necessarily be in English."

End of day and intraday balance reporting



Source: SWIFT

Bank relationships

Let's be clear, this is not an invitation to go and have it out with your bank about your visibility issues; however, your choice of banking partner(s) will inevitably have an impact on the level of visibility that you are able to achieve.

Lenovo, for example, has implemented a single bank model that allows the company to achieve superior levels of visibility. "We have domiciled all our operational accounts with a single bank," says Damian Glendinning, Treasurer of the computer manufacturing giant. "This solution may not be to everyone's taste, but it means that all the data is immediately available in the internet banking system of the bank in question, and can be downloaded easily into spreadsheets, or any TMS."

Putting this kind of structure in place and scaling back existing bank relationships is by no means easy, though. "There are all sorts of issues caused by the relationships, by local issues and by the inevitable teething problems with the new, more concentrated service. We have been in the fortunate position of being able to start with a very concentrated banking structure – even then, it is a challenge resisting all the 'helpful' suggestions emanating from various parts of the business about how we would gain by opening relationships with more local banks," Glendinning observes.

But he also reiterates that "the more banks you have, the harder and more expensive it is to collect the data, and to effectively control the cash, once you know where it is. A tough stance may not win any popularity contests – but it certainly improves efficiency."

Nevertheless, in today's world, the counterparty risk exposure of working with a single bank provider is simply not an option for the majority of multinational companies – or for those with significant borrowing requirements. Running a multi-bank relationship spreads that risk, but also spreads your cash – making visibility more challenging.

"At this point, you really have to think long and hard about the relationships that you choose," says Persson. "If you work with global or regional banks and use the partner banks in their network to cover your needs, this will give you better visibility than choosing individual in-country banks. Not only because there is more integration, but quite often you will find that the local banks who are not in some kind of alliance simply do not have the technology to provide the information that you need – whether that be SWIFT capability or a proprietary system."

Cash management structures

Where some companies are prepared to invest in technology to improve their visibility, others cannot justify the expenditure, or simply see another way. Lenovo, for instance, has taken a largely structural approach to improving cash visibility and control. "We have done everything to keep the cash structure as simple as possible: by having a single account in each country, we have been able to avoid the dispersion of cash which is a major cause of lack of visibility," says Glendinning. "Also, we operate a physical daily sweep of cash to our centre – this avoids having cash balances build up around the world except, of course, in countries with exchange controls."

Moving cash to a single location, often the company's home market, or to a given location that is favourable from a tax or regulatory point of view, is a technique that is commonly employed by companies looking to achieve visibility over their cash position on a per currency basis. This can be achieved by using an electronic banking system to initiate credit transfers, which is highly manual, or through an automated cash pooling solution.

Pooling: visibility and control

Here we stray more into the realm of cash mobility, than visibility, however the two are inevitable bedfellows when it comes to best practice liquidity management. In fact, the term 'visibility' is becoming almost synonymous with the double whammy of 'visibility and control'. After all, as Persson puts it, "if you can't control and mobilise the money, then the value of having visibility over it is vastly reduced."

So how can pooling assist? While both physical and notional pooling can help to support improved real-time visibility and control over global cash positions, there are some important nuances to grasp. According to a recent whitepaper published by the Treasury Alliance Group consultancy: "Many companies are initially attracted to notional pooling because of its conceptual simplicity and the fact that much of the work is done by the bank. As corporate thinking evolves to include regulatory issues and price, physical pooling generally becomes the more preferred choice."

While the whitepaper outlines several drivers for this preference, including the advent of the Single Euro Payments Area (SEPA) and the growth in enterprise-wide ERP adoption, another factor quoted in favour of physical pooling is that "virtually all cash is visible through web-based balance reporting solutions which allow treasurers nearly instant access to all accounts in the pooling arrangement."

But for Mustafa Kiliç, former Head of Regional Treasury and Group Risk and Insurance Manager at a white goods manufacturer, the key to that statement is the word 'virtually'. "We were operating in locations where it was extremely difficult to gain visibility, such as Russia." Adopting one cash and liquidity management approach for all countries the company was operating in was simply not feasible. "Due to different rules and regulations some entities may not be permitted to participate in cash concentration or notional cash pooling agreements. This makes visibility very challenging, especially as the complex markets do not tend to have an advanced technical infrastructure in place," explains Kiliç.

In conjunction with ING/Bank Mendes Gans, the company developed a hybrid cash pooling solution that would allow it a level of visibility and control that was not possible through physical or notional pooling alone. "Before we had the hybrid solution, we would be buying one currency, selling another and making inter-company loans. And if it was a significant amount of money, we would wait for the right time in the market to do the FX deal, perhaps as long as a week, meaning that even if the cash was visible, it was not reachable. The hybrid cash pool gave us instant access to our cash – as well as visibility, even in challenging countries such as Russia and Turkey."

The technical details of this hybrid cash pool can be found on the Treasury Today website, as the solution was Highly Commended in the 2010 Adam Smith Awards in the Global Liquidity Management category. And for more information on physical and notional cash pooling techniques, refer to Treasury Today's European Cash Management Handbook.

http://treasurytoday.com/adamsmith/2010/winners/glm-highly-commended-indesit

Reaching the next level

Beyond the three macro factors outlined above, there are numerous tips and tricks that companies can employ to improve their cash visibility. The relevance of these largely depends on each company's visibility goals – and even definitions, however.

Persson, for example, believes that a useful tool for taking visibility one step further is electronic bank account management (eBAM). "It may not offer account visibility as such, but having control around account management processes, data and signatories makes visibility sustainable." Indeed, some companies implementing eBAM have reportedly discovered bank accounts that they did not even know existed before – so this adds a completely new dimension to the visibility concept.

For others, valuable visibility tools include commercial cards – these are often linked with expense management systems, which help improve visibility as they offer treasurers the functionality to consolidate their indirect costs in one place, allowing for a more accurate review of transactions and overall expenditure. "This greater visibility of outgoings also enables treasurers to track trends, such as potential over-expenditure and spend with suppliers," says Karen Penney, Vice President and General Manager of Global Corporate Payments at American Express. "Companies with a relaxed policy may find that in allowing their employees to select suppliers, they are missing out on the opportunity to negotiate preferential rates for their company. Armed with the data, they can then ensure they establish a sharper policy, and shape conversations with their teams about the use of expenses in their company more effectively."

What is more, says Penney, consolidating expenditure into a centralised system also saves treasurers valuable time cross-checking data. "Hundreds of hours can be spent checking costs, and making and recording payments, whereas a card programme can alleviate this time burden through creating automated and therefore more accurate processes."

Technology holds the answers

These two examples alone highlight that while there are structural and organisational solutions that undeniably help, there is nothing quite like technology and data to improve visibility; but that technology has to be centralised and fit-for-purpose. "Just make sure you've got the right technology and the right data, especially from your operations," warns Skanska's Müldner. Otherwise, it's a case of 'garbage in, garbage out', which defeats the point of the exercise entirely. ■

Striking a balance

The financial crisis means businesses should take a more holistic view of their balance sheets – and must do so in a timely manner. What does this mean and how is it best achieved?

It would seem prudent in any economic environment to understand exactly how much money you have coming in and how much you have going out. This is nothing new: Charles Dickens' fictional character, Wilkins Micawber (from 'David Copperfield'), dispensed the following words of wisdom:

"Annual income twenty pounds; annual expenditure nineteen pounds nineteen and six: result happiness. Annual income twenty pounds; annual expenditure twenty pounds ought and six: result misery."

Back to basics

So what is balance sheet management all about? Starting from the top, a balance sheet is an accounting report designed to give a snapshot of a business' financial health at any point in time. It includes its assets, such as cash and debtor liabilities; liabilities, in the form of creditors such as banks and bond holders; and total or net worth, which is assets minus liabilities. Whilst asset and liability management are typically viewed as separate elements within the financial function, they necessarily come together under the balance sheet management regime.

Finding focus

The process of balance sheet management is equally applicable to private individuals and global corporations and yet, for many corporates, before the current financial crisis, few corporations were giving much thought to the issues that were impacting their balance sheets. "But as the downturn hit and businesses got caught up in bank insolvencies, there was a much greater focus on balance sheet management generally," says Martin Hutchings, Finance Partner in the London-based banking team of international law firm, Freshfields Bruckhaus Deringer. Now many more companies are grasping the nettle "and taking it much more seriously".

In the corporate sector, balance sheet management is closely aligned with working capital management. This focuses on controlling current assets and current liabilities to ensure a

business remains a going concern and can meet its short-term debt obligations and operating expenses.

Daniel Windaus, Head of REL Consultancy in the UK, points out that before 2008, when funding was cheap and readily available, most businesses would question the need for sourcing more cash. But as the crash came and liquidity started to freeze up, the focus of corporates in many regions shifted towards working capital, at least in the short term. This rather changed the face of many operations: "During the slump, many companies realised their revenue line had disappeared and that all the materials to feed their supply chains were now going to have to sit idle as they didn't have the revenue to soak it up. Suboptimal supply chains always get exposed in a downturn."

Spotting problems

One obvious need for a thorough understanding of the balance sheet is that it can help reveal financial issues before they become major problems. In the current climate this is a must, but even when times are good, solid balance sheet management can help companies put their capital to better use. In any case, managing asset and liability mismatch and maximising returns on assets is necessary to be able to keep the business running smoothly.

In addition to monitoring and anticipating actual and potential value differences between a company's assets and liabilities, the process of balance sheet management calls upon company policy and procedure to control, or at least limit, the various financial risks a business's liquidity may be exposed to. As such, it is also closely bound up with risk management. According to PwC, there are four main areas of balance sheet management:

1. Interest rate risk management.
2. Liquidity risk management.
3. Capital management.
4. Discretionary investment portfolios management.

Cash first, ask later?

Of course, from a working capital perspective, Windaus notes that it depends on organisational type as to whether liabilities or assets take precedence, although he argues that both should be managed with equal vigilance. A manufacturing business, for example, will have a heavier demand for assets and thus cash consumption will be higher. A pure service organisation, with very little inventory (if any), will most likely see a higher concentration on liabilities. In terms of building up working capital, he believes that less is better, to the point where negative working capital – when current liabilities exceed current assets – can actually be a good thing. To achieve this, trade-offs need to be well considered and managed so that the overall business is not negatively impacted.

Turning a net asset into a net liability in this way sounds counter-intuitive and in most cases it is a warning that trouble lies ahead. But when a supplier delivers products to a buyer, and it then sells those products to its own customers, cash up-front, before it has to pay the supplier (as with fast food restaurants or supermarkets), its low inventory married to low accounts receivable equates to efficiency. If it can maintain this model it will have no problem raising cash. So, rather than having cash stuck in everyday business processes, it is in-hand and can be used with purpose for activities such as debt reduction, M&A and capex investments.

In Europe, working capital levels did improve post-credit crunch, but in the past couple of years it has deteriorated once more, notes Windaus. "Companies focused on it when they needed to because cash was not readily available, but now there are other priorities, management attention has probably wavered away from maintaining any improvements on a structural basis."

Notwithstanding the discussion around the importance of cash, Hutchings believes that many companies have become much more focused on liability management over the past few years. These businesses may have a profile of debts maturing – such as bank loans or bond facilities – but have found themselves struggling to finance their repayments because the liquidity in the market has tightened. In response, when previously treasurers were rarely invited to board meetings, he says now they have become "quite central to that function" because senior executives are concerned how their business is being financed and what risks exist within that process.

Look to the future

Clearly there is a need to look beyond the immediate financial needs of a business. At a bare minimum, says Hutchings, there should be a view some 15 to 18 months out, simply because a business will need its auditors to give it 'going concern' status when signing off the annual accounts with a buffer that indicates it can continue to pay its debts, at least in the near term. "But any good company will look out longer than that, possibly to the next two to four years, identifying what needs to be refinanced and how best to do it."

There is good reason for this. A notable problem with the market at the moment is that it can take much longer to raise money. Companies cannot automatically assume they can go to the same sources each time, as banks are more reluctant to make funds available.

Asset or liability?

The degree of importance attached to either asset or liability management does depend on the nature of the business. A company favouring debt should naturally err in favour of liabilities management, but whilst a cash-rich operation still needs to keep a watching brief over its liabilities, asset management becomes more pressing.

Despite the downturn, cash-rich corporates are on the increase. In early 2012, FT.com reported that in the US non-financial corporate sector "profit margins are at record levels thanks to savage labour shedding and companies are awash with cash". It added that a similar "accumulation of cash has occurred in Europe", and cited McKinsey's estimate that European and US companies "hold about $2 trillion of surplus cash" (the amount outstanding over and above operating cash, defined as 2% of revenue). With such large surpluses, these companies need to consider the best place to deposit their cash, not just to generate the best return, but also to minimise counterparty risk.

The aim of a company is to assure its own success. Cash-rich is generally a good thing, but if there are liquidity issues because asset management is poor, a business may soon find itself in a position of actual or technical insolvency.

Getting better

Improvements in balance sheet management are founded in improving operational processes, states Windaus. Where most

would see it as a pure finance issue, he sees it firmly embedded in operational matters. Working capital management, for example, is all about how a company procures from its suppliers, how it contracts with its customers, how these processes are run and how the supply chain and demand forecasting are managed. "Very quickly you get out of the realms of finance, where a CFO or treasurer can influence, and into the daily operational processes," he notes. It then becomes a matter of how efficiently the business is running, turning to decisions around inventory and production line downtime.

"The challenge for the treasurer or CFO," says Windaus, "is to try and bring that cash awareness into the overall business, to make people aware of what they can do to influence the balance sheet and what that means for the business." However, he warns, stepping outside of the finance realm to speak with supply chain managers, for example, often requires time and patience to explain the impact that the balance sheet has on the overall business.

But in building that bigger picture, Hutchings advises the need to consider a number of external risks as well. Counterparty risk information, for example, can be sourced from various business units regarding contracts with suppliers and customers. There is also a need, he says, to understand what sort of business is being carried out and with whom. "If there is a breakdown in your supply chain because a supplier has become insolvent, it could have a major impact on your business." It therefore becomes another ongoing task to assess the health of these relationships and the financial wherewithal of the parties involved and the market risks they may be facing.

How it's done

Effective balance sheet management starts with an understanding of what it is that is required of the process; not knowing some of the issues and consequences, and therefore not being sufficiently prepared to take advantage of opportunities at the right time, is a quick route to being caught out, says Hutchings.

Accessing and gathering financial data is a key function too. Whilst a treasury team should know its own debt maturity profile, if those debts are executed on a group-wide basis, it won't necessarily know about some of the supply chain or credit collection issues, for example, making it more difficult to pull in the right data, in the right format, at the right time. In response to this potential issue, Hutchings says a centralised function "can give a full and proper understanding of the business needs".

Clearly then operational processes must be optimised. Windaus suggests one of the duties of the finance professional (treasurer included) is to increase awareness of the power of the balance sheet by establishing clear key performance indicators (KPIs). These must be communicated across the business. And rather than just having a KPI at a corporate or business unit level, it should be cascaded down to the people who can influence processes, where the processes are carried out. All the measurements can then be brought together "to enable the levers to be pulled at an operational level, and at the same time deliver visibility and transparency across the organisation".

Additionally, Windaus believes that CFOs have a key role to play in the introduction of incentives around the management of liquidity at board level. But one other important aspect – one that he feels is often underestimated – is how to communicate and manage the cash flow forecast of the organisation.

Predicting liquidity requirements can be an insular, desktop-based activity for a treasurer, but involving other business and process stakeholders in creating a cash flow forecast can be a means of changing organisational behaviour. If, for example, the cash requirement for a specific unit looks like it may unexpectedly and significantly increase over a short period – based on figures supplied to treasury by that unit – questions can be raised immediately. A solution may then be found to head off this demand by perhaps changing the way the unit's business processes are conducted, for example by revising the collections process or credit terms.

With different operational stakeholders involved, Windaus argues that treasurers have the opportunity to turn a habitual set piece regarding liquidity, into "proactively doing something about the processes that generate cash in the first place".

Preparation, preparation, preparation

Preparing the ground for that coherent view follows Hutchings' belief that reporting systems should be created centrally and pushed out to the local business units, requiring them to report in a standardised format as required. Reporting may be carried out electronically into a central system but this is a rare occurrence. Standardised reporting of the different elements using spreadsheets will suffice as it at least enables treasury to form an overview and open dialogue as necessary with the various stakeholders.

Technology is often cited as the panacea for all process issues, but not in this case Windaus believes. "It can help and might make your job easier, but it will not solve a problem by itself," he states, adding that it is "an illusion" to believe that if a business simply applies technology to a certain set of functions, all will be fine.

Indeed, at the centre of the process, in the treasury department, the need is for experience, professionalism and judgement. "Treasurers will know their business and their own markets better than anyone. Many will have been through similar cycles and will know some of the mitigants to use," comments Hutchings.

At the highest level, balance sheet management requires a firm purchase on what the wider risks to the business are including, for example, the economic, political, geographic and social. Hutchings says: "It's about trying to understand the potential issues. From there you can work back to the risks these present to the business, the exposure you have to these, and then deciding how to mitigate against them, making it less painful if and when those issues arise."

For Windaus, effective balance sheet management centres on transparency, communication and process optimisation. Implementing these concepts in a cohesive way that will work on a day-to-day basis can often overwhelm the finance division "when they realise what it really means to change behaviour in their own company". For financial minds, it may be quite straightforward, but opening up the mysteries of the balance sheet to the rest of the organisation on both a structural and process basis is not a "plug-and-play" exercise. Indeed, he notes, "managing mind-sets and behavioural changes will take some time and hand-holding. Do not underestimate the effort required here." ■

INSIGHT AND ANALYSIS

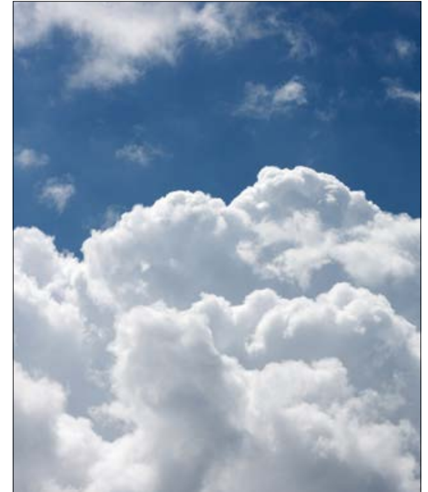
In-house solutions

To build or to buy, that is the question. Some innovative treasurers are taking advantage of in-house talent to create homegrown solutions for their treasury pain points, instead of waiting for technology vendors or banks to come up with the goods. But is this truly the best use of resources?

CORPORATE FINANCE

Demystifying pensions

The world has never seen as aged a population as currently exists, which is fuelling talk of a pension crisis. The basic concept of a pension fund is simple, but there are many pressures applied to the different scheme-types and these make it a far more complex matter than most would care to tackle. What are the issues?



TECHNOLOGY

Cloud computing for treasurers

Cloud computing options are becoming an increasingly popular choice for treasurers seeking greater automation and technological assistance in delivering efficient cash management. With a pay-per-use pricing model, easier maintenance and upgrades, as well as the ability to access the system remotely, what's not to like?

We always speak to a number of industry figures for background research on our articles. Among them this month:

Daniel Andres, Business Development, Entarena; **Carole Berndt**, Head of Global Transaction Services EMEA, Bank of America Merrill Lynch; **Esther Chan**, Emerging Market Debt (EMD) Portfolio Manager, Aberdeen Asset Management; **Steve Dwyre**, Managing Director Global Corporates, Lloyds; **Gerard Gallagher**, Advisory Services Market Leader, Ernst & Young; **Damian Glendinning**, Treasurer, Lenovo; **Mike Hughes**, Global Head of Fund Services, Deutsche Bank; **Martin Hutchings**, Finance Partner, Freshfields Bruckhaus Deringer; **David Kelin**, Partner at Zanders UK LLP; **Mustafa Kiliç**, former Head of Regional Treasury and Group Risk and Insurance Manager; **Neil King**, Group Treasurer, Carphone Warehouse plc; **Mahesh Kini**, Asian Head of Cash Corporates, Deutsche Bank; **Daniel Marovitz**, Founder, buzzumi; **Euan McNeil**, Co-Manager of Kames Investment Grade Bond Fund and Kames Investment Grade Global Bond Fund; **Maciej Müldner**, CFO, Skanska Romania; **Edward Mundt**, Senior Treasury Manager, Asurion; **Françoise Nichols**, Director, Fund Ratings and Evaluations, S&P; **Karen Penney**, Vice President and General Manager of Global Corporate Payments, American Express; **Julia Persson**, Former Deputy Head of Treasury, A.P. Moeller Maersk; **Nasreen Quibria**, an Executive Consultant and Payments Expert, CGI; **Farouk Ramzan**, Head of Corporate Debt, Capital Markets, Lloyds; **Neil Schloss**, Vice President and Treasurer, Ford Motor Company; **Alastair Sewell**, Director, Fund and Asset Manager Rating Group, Fitch; **Mark Stockley**, Managing Director, Head of International Cash Sales, BlackRock; **Murat Ulgen**, Chief Economist for CEEMEA, HSBC; **Stephen Webster**, Group Treasurer, QinetiQ; **Daniel Windaus**, Head of REL Consultancy UK.

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