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Global Treasury Briefing

PERSPECTIVES GUIDING GLOBAL TREASURY AND FINANCE

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THIS ISSUE

Credit Crunch 2.0
Learning the Treasury Lessons of the Last Downturn

European Treasurers Council Report: SEPA

Interview:
Indesit's Treasurer Discusses Risk

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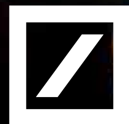

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Credit Crunch 2.0

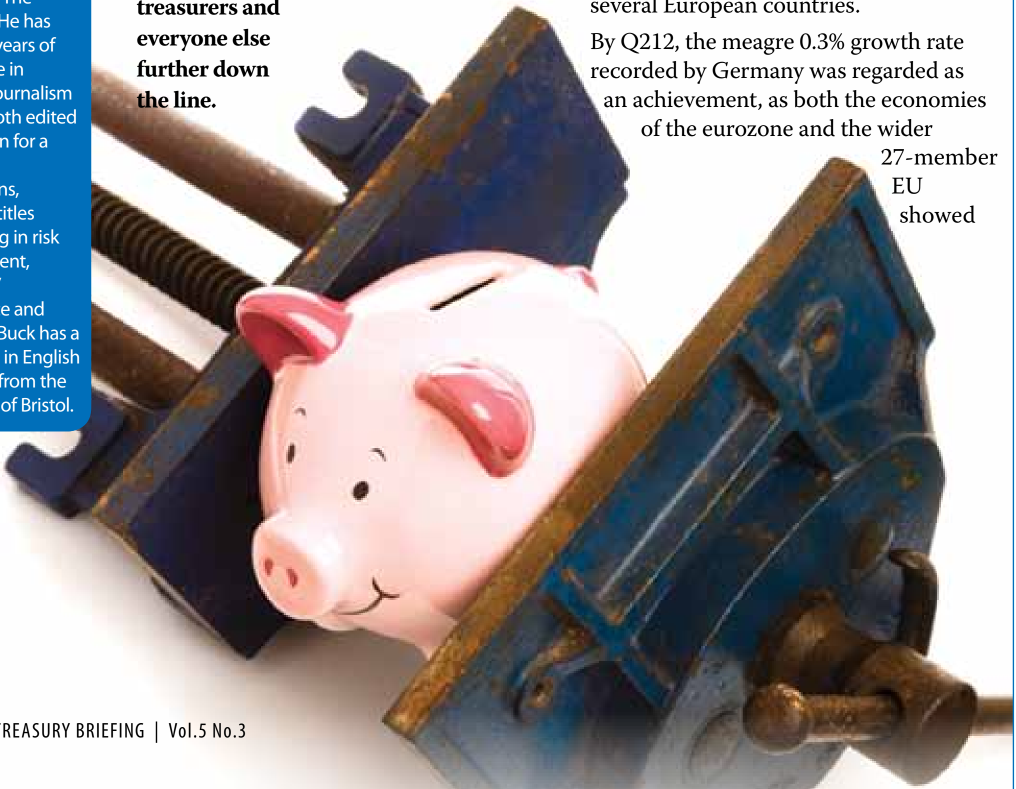
The repercussions of the credit crunch that struck five years ago are still not fully played out, even as another crunch beckons due to the worsening global economic situation, new capital adequacy regulations and other factors restricting bank lending. Graham Buck examines the drivers and opportunities of the present volatile business environment and asks what lessons have been learnt since the first crunch to guard corporate treasurers against the second coming?

Graham Buck is deputy editor at *gtnews*, having joined the title in June 2012 from the Association of Corporate Treasurers' magazine, The Treasurer. He has nearly 20 years of experience in financial journalism and has both edited and written for a range of publications, including titles specialising in risk management, insurance/ reinsurance and pensions. Buck has a BA degree in English Literature from the University of Bristol.

August 2012 marked a melancholy anniversary. While opinion varies as to when the gravity of the credit crunch first became evident, 9 August 2007 was the day when BNP Paribas announced a "complete evaporation of liquidity" in the bank market, prompting a US$90bn capital injection into the financial markets by the European Central Bank (ECB) and US Federal Reserve. The action was still not enough to prevent banks being frozen out of the markets they relied on for funding, and the cost of credit rose sharply for corporate treasurers and everyone else further down the line.

Five years on, for corporate treasurers any return to so-called 'normal conditions' remains as distant as ever. Indeed the pre-2007 period of easy credit increasingly appears to have been a temporary aberration. Concerted action by governments in 2009 and 2010 to revive economic growth through measures such as quantitative easing (QE) briefly raised hopes that the global economic downturn would prove short-lived. However this same period also saw concerns take hold among investors of a potential sovereign debt crisis, with the downgrading of government debt in several European countries.

By Q212, the meagre 0.3% growth rate recorded by Germany was regarded as an achievement, as both the economies of the eurozone and the wider 27-member EU showed



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a 0.2% contraction. As the biggest single casualty, Greece's economy recorded a 6.2% decline against a year earlier and was back at 2005 levels, while the larger economies of Portugal, Spain, Italy and the UK are also contracting this year.

"Before 2007 it was widely believed that once a resolution was found, normality would return but few appreciated how bad things were about to get," says Selwyn Blair-Ford, head of global regulatory policy at the technology vendor, Wolters Kluwer Financial Services' FRSGlobal. "There was no great concern over liquidity, even among the regulators.

"Today, people have become painfully aware that a good credit rating is not necessarily a guarantee of strong liquidity. Government securities have, in a number of cases, turned out not to be liquid. Firms have had to become accustomed to new standards and methods of operating."

Anita Patterson, director of treasury services at Cox Enterprises, adds that other changes in perception since 2007 include less reliance on credit ratings, a new appreciation that 'liquidity is king' and an increased focus on free cash flow.

Ron Chakravarti, managing director of Citi's institutional clients group, agrees the main lesson of the crisis is the increased awareness of liquidity risk both by corporates and banks. "Treasurers need to be keenly aware of the various risk triggers, including those that are less prominent and lurk in the background," he says. "They include regulatory risk, supply chain, customer credit, commodity price and political risk. To this list, sovereign risk has been added in the past couple of years as the debt crisis has had an impact on practically every business. The need for due diligence has been heightened as a result, so corporate treasury departments are working to a broader risk remit and their role is increasingly that of internal consultant."

Volatility as the New Normal: Eurozone Crisis

Five years on, corporate treasurers have adapted to a business environment where uncertainty and volatility have become the norm and there is little prospect of improvement over the near term. The so-called eurozone crisis, marked by several EU countries finding it impossible to refinance government debt without outside assistance, first became a major concern in late 2009. Despite the recent insistence of the ECB president, Mario Draghi, that the central bank would do "whatever it takes" to support the eurozone, the lack of any immediate concrete action effectively undermined his assurance. Ditto the much heralded 'fiscal compact'.

The crisis will continue to weigh heavily on treasury departments, "especially how companies react and act," says Ellen Cornelissen, treasury director for Europe at Swiss aluminium manufacturer Aleris, who has set up a contingency project across all departments to prepare for the worst case scenario of a euro break-up. "Related to this is the topic of cash pooling – for example, will you continue to keep your pools with one bank, do you distribute funds among banks and what benchmarks do you set?" she adds.

"Credit and collection get more important as the crisis continues. Do you remain with your credit insurer, who could pull out of some countries as a number have already done, or do you set up an internal team and start acquiring knowledge in-house?"

The general consensus appears to be that although one or two of its weakest members could eventually stage a phased withdrawal, the eurozone will survive largely intact.

"The sovereign debt crisis has to be [left to run] and will ultimately be resolved. Germany, as a major player in the eurozone, will not allow a break-up to happen and there is a buffer of capital that

people have become painfully aware that a good credit rating is not necessarily a guarantee of strong liquidity

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Analysts forecast that an already modest recovery will be choked off with 3.5% to 5% of potential US economic growth lost

the ECB has in reserves to bail countries out," says a UK-based treasury member of the *gtnews* editorial advisory board, who wished to remain anonymous.

"Were there to be a break-up, the entire financial world and business world would collapse and I don't think anyone wants that. Nor do its major players want to be seen as failures, so every effort will be put in to save the eurozone."

US Fiscal Cliff

By Europe's meagre standards the US's recent economic record has been enviable, with the country pulling out of recession by mid-2009. Nonetheless, its recovery rate over the past three years has been the weakest since the 1930s and the country lost its coveted triple-A credit rating in August 2011 when it was downgraded by Standard & Poor's (S&P).

In addition, the US now faces what has been dubbed as an imminent 'fiscal cliff', as tax cuts introduced by the Bush administration in 2001 and 2003 are due to be withdrawn at the end of this year after being granted a two-year extension in 2010. The result will be an increase of US$3-3.7 trillion in the tax burden. At the same time, an austerity programme that aims to cut US$1.2 trillion phased over a period of 10 years is about to kick in.

Analysts forecast that an already modest recovery will be choked off as a result, with 3.5% to 5% of potential US economic growth lost. The US Federal Reserve has openly indicated that it will aim to preserve its policy of maintaining low long-term interest rates to the end of 2014.

Changing Strategies

How are treasurers' strategies changing as the repercussions of the credit crunch 2.0 continue? In Europe, companies appear to be refining their approach through policies to address possible future volatility. For example, Irish building materials group CRH recently revealed that it no longer holds large cash balances in euros over weekends due to the single currency's uncertain prospects, but instead converts to either US dollars or sterling. Some companies move cash out of euros and into other currencies on a nightly basis to reduce their foreign exchange (FX) exposure. Others are making contingency arrangements for the eventuality that customers pull out of the euro or run out of cash; in some cases putting 'early warning systems' in place to identify emerging risks.

The UK's Association of Corporate Treasurers (ACT) and Barclays collaborated in Q112 on a survey of more than 100 multinational corporations, of which 79% were from the Europe, Middle East and Africa (EMEA) region, focusing on how their corporate risk management was responding to events.

The survey, which follows a similar canvassing of opinion in 2010, found that over the past two years corporate treasurers have become focused on a broader range of risks, with strategic and macroeconomic issues heading their list of concerns whereas transactional and operational issues previously dominated alone. The findings mirror the Association for Financial Professionals (AFP) recent global liquidity risk survey which found all manner of threats to corporations' profitability and a tendency to hold on to cash balances.

The 2012 ACT survey indicated that, in response to an economic outlook that remains uncertain and volatile, EMEA treasurers are increasingly aware of counterparty risk and demand "a better quality of relationship" from their banking partners. Among the findings of the survey were the following:

- Reduced earnings volatility is more clearly than ever the top risk management objective for corporate treasurers.
- FX transaction risk remains the highest ranked concern followed by liquidity risk, while counterparty risk has become the third highest ranked concern.

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- Sixty per cent of companies cited market volatility as the biggest risk management challenge facing treasurers.
- Banking relationships have been simplified, with treasurers tending to ask their core banks for risk management support.

The survey also suggests that corporates' risk management activity is increasingly driven by concerns over market volatility, which is the main driver of changes in FX risk management. Around half of the companies surveyed use FX options where FX risk is actively hedged - a similar finding to the 2010 survey - while hedging of emerging market FX risks has increased to more than 40% of companies and nearly two in three use some form of e-commerce for FX transactions.

Questions to corporates on interest rate risk management reveal a shift towards more fixed debt over the past year. Vanilla swaps have become an increasingly important hedging tool, while inflation swaps are also more widely used.

This summer also saw the ACT reissue its briefing note from 2008 entitled 'Contingency Planning for a Downturn in the Economy: A Treasurer's Checklist,' outlining the financial fundamentals in a period of weak growth or recession. Martin O'Donovan, the ACT's deputy policy and technical director, says that while the document was first written when a meltdown of the whole financial system seemed a distinct possibility, it remains relevant four years on by focusing on the basics of good housekeeping for any corporate treasurer from looking after cash to keeping all potential lines of funding open.

"Assumptions that the downturn would be of relatively limited duration have been confounded as a succession of different crises have prolonged and intensified the adverse conditions," he adds. "Consequently, the general mood has remained fairly pessimistic for the duration of the past five years although bigger companies continue to have reasonably easy access to credit. Diversification, both geographically and in their product lines, enables them to respond to changing circumstances."

Short-lived Stimulus

There were, nonetheless, signs that government action on both sides of the Atlantic to jolt economies back into growth through the QE programme might be achieving some success in H209 and during 2010. But as Kevin Lester, director of risk management and treasury services at Validus Risk Management, comments, subsequent rounds of QE have proved less sustainable and produced diminishing returns.

"The remaining options left are not monetary policy options and what we're seeing is not positive," he says. "In France, the new regime has already pushed up the minimum wage and lowered the retirement age, while in the UK overall debt is still growing despite the talk of austerity. So the fundamentals are not being addressed, mainly because the measures needed are simply too painful. As a result, corporates continue to accumulate cash and are either putting off or cancelling any major capital investment plans. The focus is simply on preserving what you have."

Monie Lindsey and Mike Gallanis of the Treasury Strategies consultancy suggest that most companies have adjusted well to the challenging conditions of the post-2007 period as liquidity management, risk management and the tools used for both functions have been modified. "We are now in a different environment marked by much greater volatility. There is a much greater focus on counterparty risk, which extends to include other vendors and trading partners," they observe. "For larger corporations, the drama of the 2007-08 credit crunch has diminished. Provided that it has decent credit ratings, funding is readily available and, in many cases, at very low rates. Smaller companies face much more of a challenge [from a second crunch], although for UK

For larger corporations, the drama of the 2007-08 credit crunch has diminished. Provided that it has decent credit ratings, funding is readily available. Smaller companies face much more of a challenge

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non-financial companies now find themselves able to borrow from the markets more advantageously than their traditional lenders. The world has turned upside down.

treasurers' credit is in place for the foreseeable future."

Lester adds that European corporates have traditionally relied more heavily than their US counterparts on bank funding, which reflects Europe's smaller corporate funding market. However, in the first half of 2012 bond issuance by European companies surged to around the same levels as syndicated loans from banks. This is not unprecedented; in early 2009 bond issuance outpaced bank borrowing when, in the aftermath of Lehman Brothers' demise, companies paid high yields in their efforts to secure finance. However, this time the phenomenon appears to be a more permanent shift in the way companies finance themselves. Increasingly stringent regulatory requirements, coupled with the pressure to boost margins that the Basel III capital adequacy rules impose on Europe's banks, means that non-financial companies now find themselves able to borrow from the markets more advantageously than their traditional lenders. The world has turned upside down.

European companies are also becoming increasingly creative as they explore alternative forms of fund raising. Among various options that have been explored are going to the US private placement market, long-term non-bank institutional financing, asset-based lending (ABL), commodity finance, equipment finance and retail bonds. On both sides of the Atlantic, smaller businesses have been helped by crowd sourced funding circle initiatives, in which funding from a pool of individual investors is divided up between several businesses.

One recent example of non-bank funding is provided by UK water and waste management services group Severn Trent, which made its debut in the retail bond market in June 2012 with a £75m issue. Group treasurer Gerard Tyler and treasury manager Nick Corker explain that the company was seeking to diversify its sources of funding and access a new class of investor.

"The company has taken a very cautious approach to its finances throughout the credit crisis," says Tyler. "Severn Trent has raised money ahead of its requirements and held several hundred million pound in cash balances for the past four years.

"It is fair to say that the treasury team has concerns about the bank sector and its long-term ability to provide cost-effective funds for large businesses. Equally, the company sees the sterling bond markets as dominated by a small number of large institutions."

Severn Trent also deliberately limited the size of the transaction as "the objective was to open the market and establish Severn Trent's name and, as this market grows, the company intends to become a regular issuer."

Bonds Versus Bank Loans

Similarly, in North America 2012 has seen US corporate treasurers able to take advantage of record low borrowing costs and sell longer-term investment-grade bonds at rates that would have seemed impossibly low just three years ago. For the first time in more than 10 years, investment-grade bonds are once more being sold that have a maturity date of 30 years or more. At the same time, corporations themselves are mostly shunning long-term investments in favour of short-term debt, while a global liquidity survey issued in July by the AFP indicated that many have continued to beef up their cash balances over the past year in order to have a greater safety buffer.

"I see businesses spending where it makes sense to spend to grow their business," says Cox Enterprises' Patterson. "It's not so much 'conserving cash' as being more cautious and judicious about their spending."

The AFP also recently held a webinar examining asset management and alternative investments, explains Craig Martin, executive director of AFP's Corporate Treasurers Council (CTC). "Based on that, it is now clear that it is time for corporate treasurers to start

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taking a look at extending out both the yield and risk curves for their short-term investments. If investing in the business is going to remain somewhat limited because of the volatility in the markets and uncertain global growth, then it almost becomes imperative to begin to move out of investments that yield practically zero."

US corporate funding has recently been threatened by the attempts of the Securities and Exchange Commission (SEC), spearheaded by chairwoman Mary Schapiro, to impose further regulatory controls on the money market funds (MMF) industry. Although the industry has shrunk since the onset of the financial crisis, MMFs are still at the heart of corporate financing as major investors in commercial paper issued for working capital by US corporations.

A recent AFP survey of corporate treasurers on the MMF issue found that a majority would be less willing to invest in MMFs and would either reduce or eliminate existing holdings if further regulation was to be added to that already imposed in 2010. These misgivings were shared by some SEC commissioners as days ahead of a vote on the issue scheduled for late August, Schapiro announced that she had been unable to attract sufficient support to proceed with the vote.

Crumbs of Comfort

Although the credit outlook remains less than promising, Validus' Lester believes that the past five years have offered several positive features for corporate treasurers. "The crisis has resulted in companies paying greater attention to counterparty risk," he says. "We were too complacent before 2007, but post-Lehmans it's evident that nothing is 'too big to fail'. The corporate treasurer's role

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The lessons learnt after the first crunch – to self-fund, deepen supply chain relationships, monitor risk and not just solely rely on credit rating agencies – will all stand treasurers' in good stead

has expanded as a result, particularly in areas such as liquidity risk and counterparty risk.

"We're also noticing, on the commodities side, a growth in treasurers' involvement in commodity risk, which was previously managed elsewhere and lay outside the scope of treasury. Treasury is increasingly regarded as adept at managing risk, so has been brought in to manage the supply chain component. This role connects treasury to the business, its suppliers and general day-to-day activity far more than, say, FX management."

Citi's Chakravarti also notes changed attitudes within traditional procurement organisations, which used to focus mainly on the cost of goods sold. "Treasury and procurement are now looking at overall risk, on the basis that a stressed supply chain is bad news for their company," he explains. "Treasury is working in tandem with the business as they jointly explore opportunities for self-funding and releasing trapped cash."

The unanswered question is whether the lending role of the banks will be severely diminished forever. Christos Baltoumas, treasurer for private equity real estate investment management firm Bluehouse Capital, believes that, unlike five years ago, the simple bank current account is no longer regarded as secure. "We all used to consider it as the means to have your cash safe and protected, available for use without prior notice or penalties. Now we all know that banks in the nations hit worst by the euro crisis are not safe," he says.

"Moreover everyone is reluctant to tie up money for long durations. We all look for short-term investments, one month at the most. Special care is taken for bank loan repayments and for the covenants tied to every loan agreement. In the past a breach of covenant would not cause a major problem if it was reversed after a short period, now the slightest breach can lead the bank to ask for all the money back."

Baltoumas adds that many European treasurers are attempting to transfer cash to banks in northern Europe. "This has led to a series of problems regarding tariffs and fees, communication with the new bank, payments processes and so on.

"Apart from the fact that a lot of new documents must be signed to start your relationship with the new bank, you have to consider the different pricing policy, the new electronic banking [e-banking] platforms, the fact that you must get to know and communicate with many new people who speak a different language, and so on. All these add extra cost and stress to our work."

Conclusion

FRSGlobal's Blair-Ford believes that banks will continue to be used, provided that they are competitive. "They are recipients of a vast flow of data, so people continue to look to them in their advisory capacity. Their expertise will help treasurers determine the best course of action for corporate customers.

"However, over the past 30 years banks have adopted a factory-type model and have wanted to sell financial products. This has been an off-putting development for their corporate clients, many of whom have decided that if banks are now selling products, pricing is the basis they will use when selecting them. But the servicing and advisory role is crucial, and banks are just starting to understand this."

Not before time either as another recession looms on the horizon even in northern Europe and other parts of the world face an economic slowdown. The lessons learnt after the first crunch – to self-fund, deepen supply chain relationships, monitor risk and not just solely rely on credit rating agencies – will all stand treasurers' in good stead for the second coming and the changed business environment that looks like becoming permanent.

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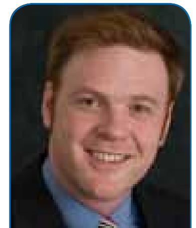
EUROPEAN TREASURERS COUNCIL

The Single Euro Payments Area (SEPA) is Fast Approaching

The European Treasurers Council (ETC) met at the Hotel D'Angleterre in Geneva, Switzerland, on 11 June, to discuss the importance of the single euro payments area (SEPA) and what treasurers should do to achieve best practice ahead of the compliance deadline in 2014 for euro members and 2016 for non-euro members. The ETC also discussed the interaction with other treasury pain points, such as the on-going eurozone crisis and the primacy of liquidity and stability concerns as the global economy worsens.



Neil Ainger is editor-in-chief at gtnews, having joined the title in January 2012. He maintains a keen interest in technology and banking, especially in the payments and mobile fields, having previously been the deputy editor at Banking Technology and editor of FSTech. Ainger has a BA (Hons) in English Literature from Leeds University and has also worked at Reed Elsevier and on internal publications for BT Global, PwC and Lucent Communications (in NYC), having been employed as a journalist since graduating in 1995.

The possibility of further SEPA end date slippage due to the eurozone crisis and countries such as Greece potentially exiting the single currency was discussed in Geneva, alongside practical SEPA considerations such as the role of SWIFT, the mandatory ISO 20022 XML messaging format, and the SEPA Credit Transfer (SCT) and Direct Debit (SDD) instruments, particularly getting mandate approvals for the latter. The participants also discussed the role of payment factories and shared service centres (SSCs) in any SEPA technology upgrade projects and the scope for differing legal frameworks in each individual country, versus the harmonised goal of a single payments infrastructure across Europe.

The long-running nature of SEPA and its various permutations ensured that all these subsets proved to be hot topics, alongside a lively discussion of the more general 'pain points' facing the corporate treasurers gathered around the ETC discussion table, such as liquidity and counterparty concerns due to the worsening global economic situation. The parlous situation in Greece and its possible exit from the euroland and how this might perhaps impact the end date timetable for SEPA was a recurring theme, alongside the best ways to deal with such volatility. One treasurer in the room admitted that he had spoken to someone who had put US dollars into a vault in Greece in order to cover the payroll in the event of a return to the drachma.

"SEPA and the euro go hand-in-hand," said one treasurer who went on to say that she worried about the stability of the eurozone and its potential to impact the timelines and plans for SEPA. The single, harmonised payment methodologies, charges and practices across the 32

Just concentrate on SEPA compliance and be aware that a couple of countries might exit [the euro] as you go along. It shouldn't affect your wider compliance project

countries participating in the project could be adversely impacted by any instability. 17 countries are part of the eurozone; 15 are outside the single currency, including Switzerland and the UK.

Remember that the non-EU European Economic Area (EEA) countries are involved in this project too, advised another treasurer, who went on to warn that nevertheless he was "quite sure that the SEPA end dates would be delayed yet again." Not officially perhaps, as too much political capital has gone into ensuring the 2014 and 2016 SEPA compliance deadlines are met, but the rules could be fudged a little bit and some delays perhaps introduced for small firms only. In France, the early internal changeover slated for autumn 2013 may also slip, it was noted.

Meanwhile, another treasury colleague said that it didn't matter if one or two countries exited the euro in terms of SEPA compliance because the same procedures and structure would be needed for the remaining participants and he was confident that the timelines would not significantly falter. Any euro refugees could still join the non-euro 2016 SEPA compliance deadline. "We've all got euro exit contingency plans no doubt, but this should be treated as a totally separate subject," he said. "Just concentrate on SEPA compliance and be aware that a couple of countries might exit [the euro] as you go along. It shouldn't affect your wider compliance project."

"It's not the 'business-as-usual' aspects that interest me about SEPA compliance," said a fellow treasurer. "I'm intrigued by how the present currency crisis plus SEPA might play out, and how the technical aspects of how any old/new currencies that arise out of the crisis might be handled in the event of a Greek exit, or the departure of any other country for that matter." An exit might not impact continent-wide SEPA structures but plans would still have to be in place for any individual countries leaving. This, and general foreign exchange (FX) volatility and risk, was what was truly worrying and it was the most prominent treasury 'pain point' for some in the room.

The Long Road to SEPA

The moderator for the Geneva ETC on 11 June was Laurens Tijdhof, a partner at the Zanders consultancy, who admitted that he had first talked about SEPA way back at the turn of the millennium, a timeframe that raised a laugh from the corporate treasurers gathered in the Hotel D'Angleterre for a lunch and subsequent roundtable discussion. The project has been going on for that long and been delayed that often, many of the treasurers present said they had ignored it for some time, turning their attention instead to more pressing treasury matters such as the rise of risk burdens and assessments since the 2008 financial crisis.

"In 2001 I was project managing a multinational client with an US$8bn turnover that was implementing SAP worldwide, plus an in-house banking [IHB] concept and examining a payment factory and payment-on-behalf-of [POBO] options," explained Tijdhof, returning the conversation to SEPA. "I remember thinking way back then that if only SEPA was already in existence – rather than just a vague twinkling in some regulators eye – that the project would be so much simpler."

The point being that SEPA should not just be seen as a compliance project, but rather as a broader opportunity to improve efficiency at corporate treasuries and across supply chains and payrolls. It is also a way to advance the adoption of standardised ISO 20022 XML messaging; the mandatory format that has been adopted for SEPA.

The importance and timeliness of the topic, with SEPA due to come into force on 1 February 2014 for euro members and in October 2016 for non-euro members, was affirmed by a treasurer in the room who explained that he was there to listen, to learn, and to see what could be optimised in his corporation's procedures and technology infrastructure. "International Bank Account Numbers [IBANs], Bank Identifier Codes [BICs] and ensuring suppliers are lined up against these is important. It's relatively easy, but it does need to be done and is time-consuming. Mass payments is also an issue for us, as is SWIFT and its role in

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the mix," he said. "We use a SWIFT service bureau (SSB) for payments at present, so integration and the mandatory XML format are important considerations for us." Many SSBs, and indeed banks, will offer white-label services and technological conversion services to try to ease the migration of corporation's payments over to a SEPA-compliant procedure. If SWIFT is involved in the swap-over then a multibank capability can be built into treasury operations at the same time.

Best Practice

Another treasurer said they too were at the ETC to learn about SEPA best practice and discuss any examples with peers, as his corporation was "just beginning to look seriously at the subject". As had already been mentioned, the establishment of the SEPA end dates should be taken as a wake-up call to start the planning process of devising a compliance and benefits plan. "If companies had not already done so, they should start now," urged a fellow treasurer. First movers are likely to gain the most advantages from clear sighted planning and technology and procedural overhauls; while those that leave it too late could even struggle to find partners as vendors, consultants and other players expect the typical 'Y2K-like' rush to hit as the compliance deadline nears.

"I've worked in treasury for more than 20 years," commented one treasurer, "and I am now in the exciting process of creating a treasury structure pretty much from scratch at my new firm, which is growing rapidly. I've only got a very small treasury team, but we have a lot to do – not least introducing some modern cash management platforms and an over-arching treasury management system [TMS]. Making the link to SEPA is crucial as the projects should overlap. There is no point overhauling cash management internally if we do not simultaneously deliver something that adds value to the business and ensures compliance with SEPA, giving us all of its advantages in terms of standardisation, a single centralised system and location independence across the European continent in terms of your accounts payable [A/P] and accounts receivable [A/R]."

The 'benefits' of SEPA were hard for another treasurer to see as he explained how in his home country, "it would be received pretty negatively domestically because the Netherlands has such a modern and efficient payments infrastructure already." SEPA won't necessarily improve this; in fact its minimum requirements will not be as good as the existing system so if everyone standardises on it this will be a regression. With systems like iDEAL and modern technology already in place in the country, SEPA will certainly not act as a spur for further large investments in the payments architecture of the country. The existing non-compliant Dutch domestic chip and PIN system will have to go as well it seems.

It is a similar situation in the UK, where legacy systems do not need overhauling as VocaLink invested in the near real-time Faster Payment Service (FPS), just as Equens – the automated clearing house (ACH) in the Netherlands – invested in its solution and banks rolled out services off the back of it, alongside their own initiatives. France too has invested in overhauling its ACH system with the STET Core product coming into force in 2008 to process SCTs. In some other European countries, however, the harmonisation project should improve the technology infrastructure, speed, reporting and reliability of payments as money is spent to upgrade national solutions in time for SEPA. Some may decide to outsource the function to a more modern cross-border ACH that can afford the outlay and want volume. Ultimately, this should assist corporate treasurers as new functionality is added to national schemes and cross-border abilities are added at no extra cost, as is required under the regulation, alongside a market driver for consolidation. Many larger banks can expect to benefit from white-label services too, as smaller banks exit the market in the face of onerous compliance costs at a time when budgets are tight.

the SEPA end dates should be taken as a wake-up call to start the planning process of devising a compliance and benefits plan

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SEPA will be beneficial in processing cross-border payments more easily and cheaply, against harmonised rules and fees

"On the positive side for us," added the Dutch treasurer, "we also have operations in Belgium, Germany and other European countries, so SEPA will be beneficial for us here in processing cross-border payments more easily and cheaply, against harmonised rules and fees. Additionally, the technical standardisation that SEPA is bringing in – in terms of XML and so forth – should also mean it is easier in future to change your cash management bank if so desired, or in the event of a bank failure."

SDD Mandate Management and SCTs

The moderator Tijdhof from the Zanders consultancy reminded everyone that basically SEPA boils down to three key instruments for corporate treasurers – namely, making a simple SCT work efficiently; collecting money by SDDs and overseeing the associated mandate management; plus ensuring that the card payments stipulations are in force and working efficiently. "Remember that at present direct debits vary from country to country in Europe. In some nations mandates are managed by the debtor; but under the new SEPA arrangements the SDD must be managed by the creditor and its banks, hence why mandate management is such a big issue for some."

At this point the challenge facing a corporate treasurer at a large petrol station retailer in the low countries in getting tens of thousands of mandates updated and SDD-compliant so that express approval is proven was shared around the table. The tale caused many a rueful grin and shake of the head at the magnitude of the SDD mandate challenge facing some corporate treasurers.

The old debate about a pan-European automated clearing house (PE-ACH) was also raised by the moderator Tijdhof, and whether it would replace the old model where every European country had its own individual (and not necessarily efficient) account clearing system. Obviously a mixture of a PE-ACH type operator for certain regions and interoperability between a few large and technologically advanced ACHs, such as the one in Holland, creating continent-wide reach is likely to be the end result of SEPA. Existing investments will not simply be discarded and early predictions at the start of the harmonised project of a single NACHA-type equivalent across the Atlantic in Europe have proved to be unfounded, at least for now. ACH consolidated has happened but not on the scale necessary to force a single entity.

"I am worried about the collections function because my corporation use some instruments in France or in Italy, such as the Ricevuta Bancaria [RIBA] electronic bank receipt, which while nominally they should disappear under the SEPA scheme seem set for some extra life yet," said one of the ETC members. "How can I plan for the migration towards SDDs if RIBA continues to exist?" she asked, while also raising the issue of whether IDoc, SAP's format for business transaction data transfers, would continue to be supported?

This prompted sympathy from a fellow treasurer who agreed that as long as RIBA is in existence in Italy, it is likely that customers will be reluctant to migrate to SDDs. On the IDoc issue he offered some reassurance by saying it wouldn't disappear overnight but that, "ultimately, XML is the file format of the future and any technology upgrade project, whether linked to SEPA or not, should take this into account".

In regard to SCTs the consensus here was that this is less of an issue because in the end it is not that dissimilar from any other credit transfer. "You have different cut-off times and value date rules, but it remains a transfer," commented a treasurer. "The SDD is totally different, however, from what some countries are currently using as their direct debit mechanism. That is why this is the bigger concern."

Local Anomalies Versus Cross-border Standardisation

Concern was voiced by some treasurers at the ETC about the potential conflict between national interpretations of the

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SEPA regulation versus the harmonised ideal across every European nation. The legal frameworks for introducing the regulation into each and every country would have to be solid, standardised and consistent to ensure maximum compliance and benefits, but as was pointed out this worry about differing interpretations is common with every EU-administered project so there was nothing especially new to worry about here. It should be introduced on a consistent enough basis to make it relevant and for the reduced cross-border fees to benefit treasurers.

"Local instruments will disappear because local banks will charge much more for them, in comparison to the cost of a cross-border SCT or SDD payment," pointed out one treasurer, making the argument that the changed market itself will also force harmonisation, regardless of the legal strictures.

There is a whole lot of legal paperwork to do as well, however, countered one treasurer. "In France, for example, if a payment is not made on the sale between the same counterparties then that sale is not valid. Therefore, you've got to have all the right legal documentation, company documentation and so forth. The bank may not care, nothing to do with the bank, but as the treasurer you have got to have all the right documentation whether it's a factoring procedure, an agency payment, or whatever. We could end up with a totally different situation in a different country if these country-specific anomalies persist and that is my major worry."

Standardised XML Format

The official standpoint in regard to SEPA-compliant file formats, explained the moderator Tijdhof, is that when the legacy payment instruments are phased out everyone is going to use the mandatory ISO 20022 XML format. Large corporates will be keen to do so because it is the format of the future, but it is doubtful that it will be used by everyone in the short term. It is much more likely that some corporations, particularly smaller players, will use external vendors or banks offering a conversion service to achieve compliance.

Agreement was almost universal with this viewpoint, with one treasurer stressing that: "XML is a global format that can be used for SEPA and non-SEPA payments alike. The SEPA project has just piggy-backed on the global standard, which actually offers far greater scope for wide international benefits that aren't just confined to the European region. It is also better to think about XML rather than SCT technical compliance when we are speaking about payments because of the global reach XML offers multinational corporations and international treasury architectures."

There are different types of XML variances. "Are you talking about version 2 or version 3 XML?" queried one treasurer. "Some countries may oblige you to introduce version 3. Also be aware some banks may not accept your XML file if it is too antiquated." Yes, the XML standard will ultimately become the de facto financial services messaging standard but it is not there yet, and coping with small variations across borders may throw up some technical problems over the next couple of years. In Europe introducing the ISO 20022 XML standard makes sense, but other regions may see this as too SEPA-specific. How the standard fits in with SWIFT's old high-value FIN transactions and lower-value FileAct services for global multibank payments and the updated SWIFTNet infrastructure is also a key consideration. Essentially, for best practice purposes a global treasury should be able to use SWIFTNet SEPA-compliant messages wherever it wants around the world effectively creating a global payments area, not just a European one. But wishful theories and on the ground practice are often hard to align.

The key topic from a treasury technology point of view is whether your TMS can integrate with your version 2 or version 3 XML files. It should also be able to convert IDoc, Oracle or other enterprise resource planning (ERP) system data formats. If it can, pointed out an ETC member, then the connectivity options available should mean

Concern was voiced by some treasurers at the ETC about the potential conflict between national interpretations of the SEPA regulation versus the harmonised ideal

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XML is a global format that can be used for SEPA and non-SEPA payments alike

that you can take advantage of a more harmonised world where payment factories and SSCs become more and more possible as standardisation grows. "The key issues to examine are the internal corporate impacts of SEPA, the changed banking/payments environment and the connectivity options in between."

Centralisation and Payment Factories

SEPA means that theoretically you can manage all your payments from one bank account, but most members of the ETC did not see that as a realistic target just yet. "The payments harmonisation project could be used to move towards a SSC and as an impetus towards increased treasury centralisation and perhaps, ultimately, a payments factory," said one treasurer, "but it takes time."

If you are going to change your account structure it will also have an impact on your pooling structure and cash flows, cautioned another treasurer. "Less bank accounts may mean you want to consider a different, more centralised cash pooling infrastructure," he added. "Ask yourself how are you going to send payments, receive statements and collections, what electronic banking solution or SWIFTNet solution are you going to use, and how this can all be used to achieve SEPA compliance and provide other more interesting centralised efficiency benefits. That is what we did when looking at SEPA as an opportunity, not just a compliance burden."

The possibility of using an IHB and POBO structure as an alternative to a full blown tech savvy payment factory, or as a way towards reaching this nirvana, was also discussed at the Geneva ETC, although it was noted by a treasurer that the legal implications of this methodology would be considerable and fall upon the treasury. "I worked in Asia on some projects like this in the past and remember thick legal files proving we had inter-company and bank agreements, and countless documents covering the pooling, netting, offsets and so forth. It's not an easy thing to do and you will need very very good IT systems if you decide to pursue either approach."

SEPA can act as a spur towards centralising a treasury operation and gaining more efficiency. But achieving basic compliance can take anything from six to nine months, typically using the assistance of an SSB or banking partner. With this is mind trying to introduce centralisation while the SEPA end dates approach may not be such a good idea at this late stage.

"Never let the bank IT people just talk to your treasury IT people or external vendor consultants as you'll have months of conversations but won't necessarily get a useable business solution at the end of it – you'll get an IT solution unless clear direction is provided," cautioned an ETC member. "Also remember there is no 'one size fits all' approach."

SEPA compliance and treasury efficiency can be achieved via many different methodologies and practical steps. The key thing is to assess your treasury's needs, size, capabilities and future desires. "One of the reasons why I like coming to these events is because you can compare and contrast, as well as network which I believe is quite important in sharing knowledge," added another treasurer. "It's healthy to exchange business cards and ideas."

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SABMiller's European Treasury Centre Implementation

Giles Newell has been the deputy treasurer at the multinational brewer and FTSE50 corporation, SABMiller, for the past six years. He has lead the transformation of the treasury department into a centralised group-wide service centre and will relocate to Johannesburg in South Africa in summer 2012 to head-up the transformational treasury project team there, which is working to establish an African regional treasury centre (RTC). Prior to SABMiller, Newell was a treasury consultant for Price Waterhouse for a number of years, before becoming group treasurer at the electrical retailer, Dixons, in 1997. He worked there for nine years before departing for SABMiller.

This case study, which won the Foreign Exchange (FX) Project of the Year category at the *gtnews* Awards 2012, explains how Project Griffin at SABMiller built a European treasury centre in the UK to improve efficiencies and standardisation. The project has enhanced control and reduced risk across the board at the brewer, in addition to generating substantial savings and transparent workflow optimisation in FX pricing, cash and exposure forecasting. The case study is shared here to provide an overview of effective FX operations and in order to encourage best practice among treasuries.

The strategic objective of Project Griffin, the name given to the implementation of a new European treasury centre at the multinational brewers SABMiller, was to leverage the scale of the corporation to deliver improved control and cut costs and risk exposures, including on its foreign exchange (FX) activities. The project was started in 1 November 2010 and completed on time and on budget in April 2012.

The aim was to establish best practice treasury operations throughout the region, centralised on the UK offices. The key requirements in the project plan were to:

- Transition from decentralised to centralised treasury management at SABMiller by establishing a European treasury centre in the UK.
- Introduce an IT2 treasury management system (TMS) to the European business units, providing dependable FX exposure and cash forecast management capabilities.
- Ensure risk management centralisation.
- Introduce European bank rationalisation, reducing the number of local banking partners, and make Citi SABMiller's European regional bank.
- A simplified banking landscape was also targeted, allowing for an easier rollout of SWIFT FileAct/XML capabilities for operational banking purposes, covering accounts payable (A/P) and accounts receivable (A/R).

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Michael Connolly (left), vice president and treasurer of Tiffany & Co., and compere of the gtnews Awards 2012, with Jennifer Boussuge, head of global treasury sales at the sponsors BofA Merrill, (on the right), present the trophy for the Foreign Exchange (FX) Project of the Year to Alan Chitty, treasury controller at SABMiller.

12 countries are now completely migrated to the new system, meaning that in excess of US$1bn in FX exposure is now under central treasury management

- The project aims, described above, were delivered over an 18 month deployment, across 12 countries and 14 businesses.

The Griffin team's approach to project management was central to achieving a superior result in terms of completeness, quality and timeliness. All 12 countries are now completely migrated to the new system, meaning that in excess of US$1bn in FX exposure is now under central treasury management at SABMiller.

The on-time execution of the project plan was thanks to the hands-on approach taken by SABMiller senior treasury executives and staff, allied to strong central management and scope discipline. A transparent project methodology, clear management lines of responsibility and escalation paths were also important.

No extra resource was needed beyond the original plan. The successful implementation of the new TMS and centralised European treasury centre involved diplomatic negotiations with the existing European business units' finance management structure, while enforcing SABMiller's standardised treasury operations model.

Obstacles and Difficulties

The hands-on nature of the SABMiller treasury team's project management activities minimised the obstacles and difficulties encountered when implementing Project Griffin. The team worked collaboratively with a diverse group of finance executives, from countries including the Czech Republic, Poland, Hungary, Switzerland, Slovakia and Romania. The education, planning and rollout processes were needed to achieve the local business units' buy-in, in

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The successful implementation of the new TMS and centralised European treasury centre involved diplomatic negotiations with the existing European business units

order to ensure that the project benefits were worthwhile, realistic and deliverable.

The centre might enjoy the benefits of cost savings, banking efficiencies and improved controls, but the local business units needed to understand and accept the real overall corporate value of making cuts to their budgets. This required creativity and flexibility. Working collaboratively with banking and technology partners was also a key requirement.

In addition, SABMiller treasury successfully managed the substantial workload of financing the simultaneous Foster's beer acquisition, worth AUD$10bn (USD$10.1bn), without disrupting Project Griffin – a major achievement considering the amount of work involved in both initiatives.

Benefits

The precision of Project Griffin's planning left little room for achieving benefits beyond the original project scope. There was one such benefit, however, relating to accommodating a much more granular approach to hedge accounting than was originally envisaged. This takes advantage of IT2's in-house bank (IHB) facilities to allocate external hedges to more specific accounting categories, such as inventory, capital expenditure and operational expenditure. As a result, the actual deal volume is approximately double what was originally planned, and has been managed without cost or timetable slippage.

Project Griffin has already yielded a number of other, expected benefits. The advantages of the new TMS, harmonised banking infrastructure and new centralised European treasury operation are quantifiable against the previous situation at SABMiller, delivering:

- On-going FX and full time equivalent (FTE) benefits estimated to be worth US$1m per annum.
- Pooling and central funding benefits far exceed the original business case estimate of US$1m.
- There has been a reduction from 25 banks to one regional European bank, namely Citi.
- Bank fees have been reduced by approximately US$0.5m per annum.
- A simplified banking landscape allows for an estimated one-off deployment cost saving to be achieved for the installation of SWIFT FileAct/XML capabilities (this is presently being rolled out).

Regional cash visibility via SWIFT messaging into the IT2 solution and concentration procedures had already been optimised through an earlier phase of the Citi multi-currency cash pool implementation.

Technology and Centralised FX Dealing

Technically, the results have been achieved using the web-based IT2 .NET module to intercommunicate between the business unit network and the new centralised European treasury facility in the UK, producing the required robust, cost effective 24x7 service needed for proactive treasury management. There are about 40 IT2 .NET users supporting this part of the business.

FX pricing performance has been optimised through leveraging the efficiencies and added value of centralisation via a straight-through processing (STP) link between IT2 and 360T, compared with the business units' pre-project performance with their local banks.

In Europe, SABMiller can now concentrate FX exposures in the IHB, and execute securely with the most competitive counterparty. The centralisation of FX dealing brings the additional benefit of broadening the scope of counterparty risk management; this enables the treasury team to manage this kind of risk more effectively, with the efficient use of dealing lines and transparent exposure management.

The estimated deployment cost savings are based on the completion of a standard SWIFT FileAct/XML interface between Citi and SAP, meaning it is no longer necessary to build and support a series of

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one-off interfaces, enhancing the control quality and efficiency of A/P workflow on a continuous basis.

The SABMiller brewery now enjoys the dual benefits of SAP-based enterprise resource planning (ERP) and management, plus IT2's value-adding cash, treasury and financial risk management facilities.

Centralisation

Centralisation has generated many benefits through the concentration of front and back office professional resources and expertise, versus the preceding localised arrangement.

The highly automated IT2 workflow integrates the information flows for SWIFT (for statement and payment management and deal confirmation), SAP (for G/L), 360T (for dealing) and the subsidiary network via IT2 .NET (for FX exposure and cash flow forecasting), reducing manual effort and error potential, and significantly enhancing transparency and control. The critical mass of headcount now allows best practice segregation of duties.

Forecasting frequency has now been upgraded to weekly for cash flows, on a 12-week rolling basis, and quarterly for FX exposures, on a rolling 18-month basis. The new environment now allows material forecast changes to be made on an ad hoc basis, at the business units' discretion. The centralised organisation also provides a future platform for the development and deployment of forecasting performance measurement and management tools at SABMiller.

- This case study is based upon an entry into the *gtnews* Awards for Global Corporate Treasury 2012, sponsored by Bank of America Merrill Lynch (BofA Merrill). The winners of this year's annual awards, now in its third staging, were first revealed at a gala dinner on 24 May at the Sofitel Grand Hotel in Amsterdam, the Netherlands, after the opening of the two-day *gtnews* Forum for Global Corporate Treasury conference. This winning SABMiller entry is shared here from the FX Project of the Year category as a best practice guideline and commentary. To see a full report on all the Awards winners and the gala dinner on 24 May please visit www.gtnews.com.

SABMiller

SABMiller is one of the world's leading brewers with more than 200 beer brands and 70,000 employees in more than 70 countries. The group's portfolio includes global brands such as Pilsner Urquell, Peroni Nastro Azzurro, Miller Genuine Draft and Grolsch, as well as leading local brands such as Aguila (Colombia), Castle (South Africa), Miller Lite (North America), Snow (China), Victoria Bitter (Australia) and Tyskie (Poland). SABMiller also has a growing soft drink business and is one of the world's largest bottlers of Coca-Cola products. In the year ending 31 March 2012, the group reported earnings before interest, tax and amortisation (EBITA) of US$5.63bn and group revenue of US$31.39m. SABMiller is listed on the London and Johannesburg stock exchanges.

In Europe, SABMiller can now concentrate FX exposures in the IHB, and execute securely with the most competitive counterparty

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Microsoft Takes its Liquidity Structure to a Whole New Level

This case study, which won the Working Capital Project of the Year at the *gtnews* Awards 2012, explains how Microsoft introduced a completely automated international zero balance account (ZBA) structure into its global liquidity management function. The initiative has streamlined the cash concentration for hundreds of bank accounts and created a just-in-time funding model for subsidiary operating accounts. It is shared here as an overview of effective working capital management procedures and in order to encourage best practice among treasuries.

Jim Scurlock is a senior manager for global cash planning at Microsoft's treasury. He manages the treasury activities for Microsoft's European subsidiaries and the in-house treasury venture integration team. Scurlock has over nine years of cash management experience across Asia, Europe, Middle East and North America.

Sunnie Ho is a cash planning manager at Microsoft. For the last five years, she has been responsible for the treasury's cash management function in support of cash concentration and positioning. Prior to joining Microsoft, Ho worked at ABN Amro and managed foreign exchange (FX) settlements. She holds an MBA degree from the University of Washington, US.

Microsoft runs a centralised treasury for more than 350 legal entities in 118 countries. The software giant has more than 1,100 bank accounts with 100 plus banking relationships worldwide. At the height of the global economic crisis in 2008 and 2009, each US dollar held in local subsidiary managed accounts faced increased counterparty risk, sovereign risk, foreign exchange (FX) fluctuations, and fraud considerations, so the process began to find a long-term solution post-crash.

Many of these former concerns are once again key considerations as the eurozone crisis and economic uncertainty once more raises its ugly head, making Microsoft's recent introduction of a fully automated international zero balance account (ZBA) structure even more timely. During such volatile times few things are more important than having effective working capital management and oversight. "Now, Microsoft has a ZBA structure that sweeps each account to zero every day and creates journal entries with no manual involvement. And the solution has no negative impact on the operations of finance staffs in the subsidiaries," explains project overseer, George Zinn, corporate vice president and treasurer at Microsoft, who relied on the day-to-day project efforts of Jim Scurlock, senior manager for global cash planning, and Sunnie Ho, cash planning manager.

As one of the non-aligned corporate treasurers on the judging panel of the

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strategy [was] to reduce average daily balances by automating the collec- tion sweeps and imple- menting a just-in-time funding model

gtnews Awards for Global Corporate Treasury 2012 pointed out, "the fact that Microsoft has developed a scalable, cost-effective platform that allows it to reduce counterparty exposure and gain [cash] visibility is very impressive".

Project Background

The global cash management (GCM) and the global cash operations (GCO) teams within Microsoft's large centralised treasury department in the US are responsible for ensuring that hundreds of worldwide legal entities only have enough cash for operations, and that all collected cash balances are concentrated efficiently.

Microsoft has 175 actively funded subsidiaries and the process to fund them for payroll, accounts payable (A/P), taxes, and so forth is an exceedingly time-consuming and manual process. Additionally, the cash planning manager, whether it is Scurlock or Ho, works with each subsidiary to repatriate any cash balances not needed for operating expenses. For the GCO team, the ultimate goal is to promptly transfer available balances to the parent account in order to maximise the investment return. However, it is time-consuming to manually sweep hundreds of worldwide bank accounts and Microsoft were unable to perform same-day funds transfer for European and Asian accounts due to the time zone differences.

With these challenges in mind, the treasury department at the software giant realised the need to develop a cost-effective strategy to reduce average daily balances by automating the collection sweeps and implementing a just-in-time funding model for subsidiary disbursements.

The GCM and GCO teams in the treasury, which lead the initiative overall, conducted kick-off meetings one year prior to the 'go live', with the project getting underway in August 2010 with a planned completion date of Q311. The goal was to develop a cost-effective strategy to reduce Microsoft's average daily balances. Many joint working sessions were scheduled internally with IT resources and externally with project partners, Citi, to outline the existing challenges and brainstorm a solution. During this initial planning stage it was quickly determined that the establishment of inter-company ZBA structures would be the optimal solution.

The Project

The project required close coordination and collaboration between numerous key stakeholders. The initial scoping meetings were held with the aim of developing a strategy to reduce Microsoft's average daily balances by increasing the frequency of collection sweeps and implementing a just-in-time funding model for subsidiary disbursements. The GCM and GCO treasury teams soon realised that while introducing a new cross-border inter-company ZBA structure could meet both goals, the current IT infrastructure was not up to the job. It could not handle ZBA transactions within the SAP in-house cash centre (IHCC), meaning that key changes needed to be made to SAP.

Numerous conference calls over a 10-month period were held with Citi and SAP developers to outline and test new configurations. Meanwhile, the treasury controllers group at Microsoft completed six months of comprehensive accounting testing to ensure that the planned new solution would impose no operational challenges. Once all this testing was completed, the GCM team held conference calls with all subsidiary stakeholders to advise them of the changes. The success of this project is largely due to the hard work and co-ordination of all these various stakeholders involved in the improvement drive, and their early engagement eased the process along.

Microsoft faced two significant obstacles in the execution of the plan:

1. *The need for a ZBA with customised text capability:* Although many multinational banks have a ZBA product, no single bank offered a

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(L to R) Michael Connolly, vice president and treasurer of Tiffany & Co., and compere of the gtnews Awards 2012, with Jennifer Boussuge, head of global treasury sales at BofA Merrill, (in middle), present the trophy for the Working Capital Project of the Year to Mark Tweedie, head of technology, media and telecoms, EMEA, at Citi, accepting on behalf of Microsoft.

solution to contain customised texts in the transaction details. However, this is critical to the subsidiary identification function of the Microsoft IHCC. In fact, a ZBA transaction without this specific text will not be recorded automatically by the treasury's SAP enterprise resource planning (ERP) system, causing inter-company imbalances. Microsoft, therefore, partnered with Citi to develop and implement a new global cash concentration product called the Global Concentration Engine, which allows the required customised text to be included.

2. *The need for automated accounting:* Despite ZBAs years' of history, there has not been an inter-company ZBA solution that allows automated accounting within an IHCC. If Microsoft were to automate the collection of sweeps and enable just-in-time disbursements for hundreds of accounts, the resources required to manually post accounting entries would be overwhelming. Therefore, the treasury had to make a series of developmental changes to SAP to enable automated accounting. It did this by triggering the general ledger entries, based on the customised text, which is included in every ZBA transaction.

Challenges Along the Way

In response to the European debt crisis in 2011 and more recent events, Microsoft worked to re-prioritise the ZBA implementation schedule, bringing forward the original start date to Q311, to get the project up and running as soon as possible. According to Microsoft, the company was able to promptly put its Ireland, Italy, and Spain accounts into the ZBA structure. This greatly reduced Microsoft's cash exposure to high risk European countries, which have been suffering due to sovereign risk concerns amid the trials and tribulations of the eurozone.

Within the past year Microsoft has been able to reduce its balances in Ireland, its largest regional operating centre, by more than 99%. The successful completion of the project late last year has allowed the treasury to create a proactive offensive strategy that mitigates risk instead of playing defensively.

The key benefits of the project have been:

- A reduction of time. It no longer takes so long to monitor cash balances and cash sweeps at subsidiaries.
- A significant reduction in unreconciled balances, which is due to the automation of the accounting entries.

the company was able to promptly put its Ireland, Italy, and Spain accounts into the ZBA structure. This greatly reduced Microsoft's cash exposure to high risk European countries

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Microsoft has seen improvements in operational efficiency, with hundreds of work hours saved that were previously spent reviewing subsidiary cash balances

Benefits

The new inter-company ZBA structure at Microsoft's treasury has not cost a penny extra in terms of IT costs, with much repositioning and programming of existing equipment undertaken, and it maintains a zero balance in more than 150 accounts. It also:

- Automates cash concentration for hundreds of bank accounts.
- Creates a just-in-time funding model for operating accounts.
- Enables 100% accounting automation.

The associated new global cash concentration product went live with Citi in nine countries, with more being added all the time. The following results have flowed from the rollout:

- Reduction of more than US$250m in worldwide average daily balances.
- Increase in monetary gain: More than 250,000 interest gains due to collections are now promptly transferred to interest-bearing concentration accounts.
- Reduced risks as subsidiary accounts are maintained at zero balance, which lowers sovereign risk, particularly in vulnerable countries such as Greece.
- Decrease in bank fees: wire volumes have been significantly decreased by more than 40%.

In addition, the treasury team at Microsoft has seen improvements in operational efficiency, with hundreds of work hours saved that were previously spent reviewing subsidiary cash balances to ensure that cash was effectively used. The new automated system also means that excess cash is transferred to the centralised portfolio account as a matter of course.

The accounting team has also saved countless hours that were previously wasted manually posting general entries. Subsidiaries can now devote more time to selling Microsoft products, instead of managing cash which should also have long-term benefits.

- This case study is based upon an entry into the *gtnews* Awards for Global Corporate Treasury 2012, sponsored by Bank of America Merrill Lynch (BofA Merrill). The winners of this year's annual awards, now in its third staging, were first revealed at a gala dinner on 24 May at the Sofitel Grand Hotel in Amsterdam, the Netherlands, after the opening of the two-day *gtnews* Forum for Global Corporate Treasury conference. This winning Microsoft entry is shared here from the Working Capital Project of the Year category as a best practice guideline and commentary. To see a full report on all the Awards winners and the gala dinner on 24 May please visit www.gtnews.com.

Microsoft

Microsoft is a leading, globally recognised software corporation. It has established a strong position in the finance sector by providing best-of-breed enabling technology that helps financial services solution providers of all sizes build reliable and cost-effective business solutions. Microsoft offers a comprehensive Internet/intranet-enabled client-server platform that embraces industry standards. It works with hundreds of software developers, industry consultants, system integrators, and hardware vendors to ensure a critical mass of financial services solutions and capabilities.

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Expert Opinion

Joerg Bermueller, Head of Cash and Risk Management, Merck KGaA

1. Ahead of this autumn's conferences with EuroFinance, the AFP Conference in Miami and many other shows around the world imminent, what are you hoping to get out of the traditional conference season?

It is the intensive exchange of ideas and discussions with all financial participants concerning the latest market trends which make these events so valuable. Talking to the top treasury peers of the industry and sharing their views for the upcoming challenges is a key way to evaluate future strategies and find out about best practice. There is no better way to do it.

2. What topics are you most interested in exploring during the upcoming conference season?

At present it is the issue of counterparty risk that is most concerning me and which I most want to investigate during the upcoming conference season, in conjunction with the problem of where best to invest the cash at a reasonable interest rate, which should not be negative. These are key issues for treasurers at the moment.

3. What impending regulations are you most interested in learning more about and why?

In particular it is the single euro payments area (SEPA), which is due to come into force in 2014 for eurozone members, and I'm especially interested in the direct debit regulations, the impact on mandates, etc. Longer term, the Basel III capital adequacy rules are of interest to me, especially the restrictive impact they could have on bank funding and trade finance, so I want to look into that more during the conference season as well. Additionally, the on-going deregulation process in emerging markets – whether that is renminbi (RMB) liberalisation in China or whatever – is always of interest.

4. Does the current gloomy economic situation worry you and what are you doing about it? For example, are you diversifying into emerging markets seeking growth, looking at commercial paper issues new credit lines with banks, focusing tightly on liquidity and short-term only investments, etc?

For the time being, it is very relieving that our business is doing well. Due to this fact we do not have to worry overly about the worsening general economic situation, although we are of course constantly monitoring it. For the moment, however, we can stick to our current treasury strategy, concerning markets, products, timings and financial partners without having to make any major alterations.

5. If there is one thing that you could change in your treasury what would it be?

If it comes to my 'favourite wishes', I am always dreaming of a fully integrated and IT connected treasury system which covers the whole process from evaluating exposures until posting. In between the system should be capable of handling deals, market evaluations, exercising cash transfers, doing intercompany clearing, cash flow forecasting, scenario analyses, electronic bank account management (eBAM), Twist assessments, etc. For the time being I am happy if the existing interfaces are all running smoothly but in my dream scenario I'd like absolutely everything to be integrated in the future.

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Keara Killian, Director, Treasury and Risk Management, Getty Images

I'm looking forward to seeing how other corporates are thinking about capital structure and debt financing, and learning more about the investor relations function during the upcoming conference season. Bharti Airtel, for instance, promises to put the spotlight on investor relations at the forthcoming EuroFinance conference in Monaco at the end of September.

In addition to the areas I've already mentioned, I'm going to be focused on funding. Getty Images grew in large part through acquisitions, and the resulting integrations of acquired entities in emerging markets into our global banking structures presents a myriad of challenges. I will be plugging into modules on treasury centralisation, minimising local cash and migration to shared services, with a view to learning how to better manage our emerging market liquidity.

NOTE: Getty Images has itself just been acquired for US$3.3bn by the private equity firm Carlyle Group from Hellman & Friedman. The Getty family, which founded the agency in 1995 with Jonathan Klein, will increase their stake in the firm to just under 50%, as part of the deal.

I am more interested in discovering how regulation is *not* going to affect us. The recent onslaught of regulation, including the single euro payment area (SEPA), Dodd- Frank and the Basel III capital adequacy rules, have all certainly got treasurers talking. Hearing from the early adopters as they describe the trials of their experiences so far will be interesting for me.

At Getty Images, we are not exempt from the concerns that are associated with an uncertain economic climate. Growth is, after all, dependent on consumer trends. We have been fortunate to be a leader in our industry and we continue to focus on international expansions including recent acquisitions in the Middle East and Asia, while simultaneously expanding our diversified product offering such as video and music. From a treasury perspective, we are focused on major risk factors, key among them at the moment is the euro crisis and we continue to refine our contingency plan.

We ultimately aim to position treasury as a value-adding function, by optimising our key capabilities and providing the business tools to optimise transaction flows, enabling customers to pay for our products and for us to pay our content providers easily. Access to technology is crucial to our delivery and like all organisations there is intense competition for limited resources. Of course we'd like more [tech budget] but we nonetheless strive to provide benefits to the business through optimising the resources we have and leveraging our relationships with the best providers.

Patricia Hui, Senior Corporate Treasury Manager, Mentor Graphics Corporation

I always look forward to attending the annual Association for Financial Professionals (AFP) conference in particular because I'm US-based and it offers an excellent opportunity for corporate practitioners to network and discuss best practice with their peers and service providers. Spending a few days in a group learning environment, I usually find myself getting inspired from listening to the knowledgeable experts. With the upcoming conference season, I am hoping to bounce off a few new ideas, as well as to validate some current business processes with my peers. In addition, I would like to investigate all of the latest service and product developments in the financial market with the objective of perhaps implementing a few of them.

There are so many interesting and relevant topics that are worth exploring during the upcoming conference season. However, I am particularly interested in electronic bank account management (eBAM) implementations and learning more about this. I have had casual conversations previously with my banking business partners to explore the eBAM initiative, since my company has hundreds of bank accounts worldwide and authorised account signers spread across multiple continents. It's absolutely a pain to work through tons of paperwork usually required by the banks whenever there is a need to open a new account or to update account signing authorities. It would be more efficient to manage those global bank accounts and authorised signatories electronically as opposed to manually via an Excel worksheet.

There are two impending regulations that are generating a lot of discussion among corporate treasurers. One of them is Basel III which will have an impact on corporates that rely on bank funding. Basel III not only raises the costs of doing business with banks but may also contribute towards banks focusing more and more on a narrowing customer base. Another impending regulation that is being talked about frequently in recent months is the Securities and Exchange Commission's (SEC) proposed money-market fund (MMF) reforms. I agree with my peers that the proposed MMF reforms such as floating net asset values (NAVs) and holdback provisions would significantly reduce investors' interest in utilising MMFs as an investment tool.

I am not overly concerned with the current economic situation. I do see signs of improvement in my industry even though the US market recovery has been taking baby steps. Given the current global market condition, I believe it is even more important for corporates to stay focused and properly execute its business strategies than ever before, but for my corporate things aren't looking too bad.

As mentioned in answer to Question 2, I would love to work with my banking partners to implement eBAM as soon as possible in order to manage our global bank accounts and signatories more effectively. Due to the number of bank accounts maintained in various geographies and authorised signatories that spread across multiple continents I would love to co-ordinate with my banking partners to implement an eBAM solution. It is labour-intensive and cumbersome for treasury to keep track of global bank accounts and signatories using Excel. Automating this manual workflow with the objective of achieving better visibility and more up-to-date information for internal reporting, as well as auditing purposes, is definitely a process improvement my department is seeking.

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Scanning the Horizon for Risk

Mustafa Kilic, head of regional treasury, and group risk and insurance manager at the home appliances manufacturer Indesit, spoke to Neil Ainger at *gtnews* about why he is constantly scanning the horizon for risk, the need for better, more comprehensive risk assessments, how' black swans' can be spotted, and the lessons he has learned during his 20-year career.

Mustafa Kilic, head of regional treasury, and group risk and insurance manager at Indesit, is responsible for assessing risk across the home appliances manufacturer and running the treasury operations in eastern and southern Europe including Russia, Turkey and Ukraine, plus he looks after Argentina and China. He joined the corporation early in 2004 after 13 years in the finance and risk management fields at Siemens, Nestle, Motorola and Vodafone Group. He has a BSc degree from the Business Administration School of Istanbul University in Turkey.

"You have to see risk before it arrives, that is the point of the function. It's no good seeing it after the fact," says Mustafa Kilic, head of regional treasury, and group risk and insurance manager, discussing one of the key elements of his job, alongside the traditional cash management duties of a treasurer.

His company Indesit, a white goods manufacturer headquartered in Italy that makes and sells home appliances in 105 countries around the world, understands risk well. The company instituted a wide-ranging and comprehensive business continuity risk programme in 2009 that identified a sole Asian supplier of a refrigerated cooling part as an unacceptable supply chain risk. Action was taken to mitigate this risk by diversifying production to a second Latin American-based supplier in 2009, before the devastating Japanese earthquake hit in 2011 temporarily knocking out the original supplier. Good planning averted disaster before it happened.

Indesit, which has revenues of €2.8bn and employs 16,000 people worldwide, seeks to identify all the elements that could impact the health of the firm in its on-going business continuity risk programme. The idea is that by broadening the treasury-controlled global risk function away from its traditional specific concerns around interest rates, currency fluctuations and the like, the corporation can be 'future-proofed' as much as is humanly possible and gain a better oversight of all the risks facing the corporation.

Kilic was the driving force behind the start of this philosophy at Indesit in 2009 when the on-going yearly business continuity risk programme was started, partly as a result of seeing what the earthquake earlier that year in Italy had done to some other manufacturers' supply chains and operations. Kilic has been with the corporation since early 2004, slowly building towards the establishment of this comprehensive risk assessment procedure. He previously spent 13 years in the finance and risk management field at Siemens, Nestle, Motorola and Vodafone, before moving fully into treasury.

He is an advocate of the holistic risk approach for many reasons but admits it is partly from his experience of working at Motorola in the early 1990s and seeing it displaced by Nokia, who have themselves now been supplanted by Apple as the world's premier mobile phone manufacturer.

"The point is that so-called 'black swans' can be identified if you are looking for them and constantly assessing threats, weaknesses, future income streams and planning, planning , planning," says Kilic. "I believe the traditional approach to risk needs to change and it needs to become much more dynamic. As corporate treasurers we must focus on the future more and build up systems and structures that predict problems, and identify possible solutions, before they occur."

Strong business continuity risk plans should not just rely on good IT people and human resources staff, believes Kilic. Indeed these departments are not related to the entirety of a corporation because they do not necessarily talk to all employees

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or understand precisely who the partners in a supply chain are. "Treasury can do comprehensive financial and other risk assessments because we touch all parts of the business internally and externally."

Interdependency

There is a need to classify and categorise risk and to understand the interdependencies of how different risk factors overlap and impact each other, believes Kilic. "I look after risk at Indesit group-wide and examine everything from counterparty risk, to foreign exchange [FX] risk, supply chain, credit risk and so forth. Before 2009 we were focused too much on financial risk at Indesit, which is of course vital, but it is not an isolated risk. Risk is interdependent and we didn't previously understand that well enough. A liquidity crunch is really the end of a chain of unmitigated or unrecognised risks. Conversely, effective foresight and business continuity risk planning – and I don't just mean the technical aspects of keeping a business running here – pay off in the long term."

Indesit has 14 production facilities in Italy, Poland, the UK, Russia and Turkey and 16,000 employees to pay, as well as revenues from around the world to accumulate, so of course traditional cash management, FX risk and so forth are key concerns and a part of Kilic's job. "Liquidity risk is an especial concern at the moment for obvious reasons with the eurozone crisis and the economic downturn," he admits, "but being aware of the domino effect of different risk factors and the interplay between them, allows you to be better prepared to deal with particular challenges as they arise."

Each and every corporation has different risks, which is why Kilic thinks that drawing up an interdependency map, as Indesit did in 2009 and now does every year, is a good idea. "It allows you to see potential problems well into the future and to plan effectively," he says. "You then need to develop a business continuity risk plan from this base, as we do, and to test this plan as much as possible. You may need to diversify so you are not reliant on a single supplier [as Indesit did for its refrigerated cooling part before the Japanese earthquake struck]. In our map one natural disaster could have triggered 16 other risks. As this single component fell away our manufacturing plants in and around Europe would have been negatively impacted, hitting our distribution, retailing partners and so forth.

"Insurance doesn't cover everything, in all instances, but effective planning can mean that it doesn't have to," he adds. "It is time that everyone started doing interdependency maps and business continuity risk planning."

Teamwork and Key Risk Indicators

Of course, treasurers with risk responsibilities such as Kilic – and risk is increasingly part of the job these days – need to convince others in their corporation, the board, and partners in the supply chain to join in with any comprehensive risk mapping and testing structures that are put in place. Kilic had the help of two other people at Indesit when establishing the procedure that the corporation now regularly uses, plus the assistance of some external consultants. Teamwork is a vital component in business continuity risk planning.

One crucial element that Kilic found very helpful in the early stages of development was what he calls 'key risk indicators' (KRIs), as opposed to traditional key performance indicators. "These triggering items are often under the radar but if they are activated – by a natural disaster, a currency collapse or whatever – then they quickly come to the surface. Identifying KRIs and working out possible solutions before the problems arise, helps to nullify the risk."

In terms of the immediate risks that Kilic sees on the horizon now it is economic and financial risks that are worrying him at the moment, due to the present downturn and the volatility of markets and currencies. Other future risks are simultaneously being assessed at Indesit, however, to try to 'future proof' and protect the corporation. Nothing lasts forever they say, but as much as it is possible effective risk planning can extend the life and health of corporations.

Risk is interdependent and we didn't previously understand that well enough. A liquidity crunch is really the end of a chain of unmitigated or unrecognised risks.

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