The right connections

At the beginning of 2000, Carphone Warehouse was a private company which had been growing organically and rapidly for a decade without the need for dedicated internal audit or tax functions – or a treasury department. It has now been listed on the London Stock Exchange for five years, requiring the introduction of all the above, and diversified both geographically and into new sectors. In tandem with this public growth story, the company has implemented an integrated treasury operation, along with mature banking and lending relationships.

With more than 1,500 retail outlets across Europe, a rapidly expanding UK fixed-line offering with two million customers, a service provision business in Germany, and growing turnover from insurance and average revenue per unit agreements with the telecoms networks, the treasury department has had to learn fast. Keeping it simple has been the key to success – this is, after all, primarily a retailer and telecoms company. Most purchasing is in local currency, and without the buying demands of a diversified retailer there is no great demand for hedging complexity. So the focus remains on working capital and risk management.

Yet simplicity has its limits, especially when the business model is unique. Are we mainly a retailer? Or a telecoms company? With multiple revenue streams, the answer is far from obvious – as testified by different banks parking us in different sector portfolios. Yet even those that opt for retail coverage many find us to be a square peg. We pay for stock some weeks in advance and receive revenues some weeks after sales, so our supply chain is the opposite of many retailers'. Try fitting that into a traditional retail cash structure and you won't get far. Yet some of our banks still express surprise we are not awash with cash at Christmas.

Furthermore, with the fixed-line telecom markets changing rapidly, there are challenges in trying to increase market share at the expense of former monopolies such as BT.

GATHERING THE THREADS The financing requirements of overseas operations originally came under the responsibility of the finance director of the subsidiary, who was given a high degree of autonomy. The result was a large network of local overdrafts and banking relationships, and an extensive and complex inter-company loan network. In places, these had developed in line with local banking practices – such as in Spain, where having a large number of overdrafts is not uncommon. But this imposed a limit on the group's borrowing capacity when it needed to grow and created inefficiencies in bank charges and cash management.

Lending relationships were reduced to a manageable number, with the plc providing a single consolidated front to the bank loan market. Accordingly, Carphone Warehouse's debut syndicated loan transaction took place in 2000. Originally intended to provide a backstop for the IPO in July 2000, the transaction became the first in a series of refinancings to capitalise on an improving credit profile.

For cash management, it was necessary to emphasise the idea of a centralised treasury responsible for decision making and funding structure – without treading too much on the relationships between local FDs and their banks. We have always tried to involve local FDs in the decision-making process. But without the greater central control that has been achieved, something in the region of £20m would have remained unconsolidated in different bank accounts – inaccessible and not earning interest.

To improve reporting, we implemented the ISR version of the Richmond Treasury System – one of the first UK corporates to do so. In terms of liquidity, the dbdirect online banking system from Deutsche Bank was the only system in its class, allowing real-time reporting and full access to account details held with local banks in each market. During each trading day, treasury can now survey group-wide liquidity and sweep it into the central Deutsche Bank-held treasury accounts.

But with a rapidly growing presence in markets across Europe, the need for local banking partners cannot be avoided. Although much revenue is derived from direct debits and network commissions, it is still surprising how much cash is passed over the counter. To avoid the use of cash carriers – hard to justify with many stores, which have

NEIL KING, GROUP DIRECTOR OF TREASURY AT CARPHONE WAREHOUSE GROUP, TELLS HOW IN THE PAST FIVE YEARS HE HAS BALANCED CASH AND FUNDING SOLUTIONS FROM CONTINENTAL BANKS – AS WELL AS BUILDING A ROBUST TREASURY FROM THE BOTTOM UP.

Executive summary

- Carphone Warehouse has grown dramatically over the last decade and in the process implemented an integrated treasury department.
- Treasury systems have been implemented to improve reporting and online banking systems installed to improve liquidity.
- The need for a centralised treasury has to be balanced with maintaining the relationship between local FDs and their banks.
- With a growing presence across Europe, the need for local banking partners cannot be avoided. One key lesson is you can't be a European company without European banks.

relatively low amounts of cash – we need a local bank in each market with a very strong branch network. And with each of these banks providing other ancillary services, they also form the core of our lending syndicates, formed between 2000 and 2004.

FINDING A FRENCH PARTNER France delivers a good example of how our expansion and integration has taken place in Europe.

The first Phone House European franchises opened in Paris and Dublin during 1996. A 1999 acquisition of FNAC Telecom was the major French expansion, numbering 45 stores and making Phone House the leading independent retailer in France. By 2004, total store numbers had climbed to 185, with a further 15 opened in the first half of 2005 and growth set to continue in 2006. With this kind of reach, it was essential to build a stable local banking system, preferably combining branch reach and flexibility in a single bank.

The bank we work with today, Natexis Banques Populaires, is the corporate and investment bank owned by the mutual Banques Populaires network. It has access to the clearing facilities of 22 regional Banques Populaires and also delivers flexibility and increased capital commitment via a maturing corporate relationship with the Natexis side. And for all our centralising ambitions, it is also a good example of a relationship growing alongside our own business.

The Natexis Banques Populaires relationship originally came about because the Banques Populaires de Rives de Paris was providing clearing services to our local branches of Phone House. It was one of four French banks providing small overdraft lines in 2000 when such financing was replaced by a new £150m revolving credit facility. All the French banks were invited to join the subsequent syndication but only Natexis chose to do so. From 2000 onwards, balance sheet lending and ancillary business have built up layer on layer – with the bank's willingness to address local and group-wide requirements being a key driver of the relationship.

With each successive refinancing, the bank stayed in our core bank group, increasing its participation each time. It agreed to new covenants and applied more creative thought to solving the problems standing in our way. A good example of this has been looking at ways to improve our reporting information. With daily cashflows coming in from branches across France, we were missing a key piece of management and business development information – from which store the money was coming. To address this, Natexis was willing to adjust the architecture of the incoming reporting statement so that it included a numeric field identifying which branch had made the deposit. With this now functioning to a high degree of accuracy, it has proved an invaluable resource in managing growth.

As with all core banks, we are willing to reward this loyalty and service with more ancillary business. In 2003, for instance, we transferred the handling of our customers' insurance direct debits to Natexis Banques Populaires – not the most exciting work but good recurring business for the bank. We now set up each new branch in France to bank at Natexis and are close to completing the transfer of our existing branch network.

Natexis has even provided broad-minded advice to tighten our funding costs in line with the increasingly liquid bank market of the last few years. In 2005, we found ourselves in need of greater headroom in our funding to allow for further acquisitions and store expansions. At the same time, our 2003 term loan had begun amortising. It was Nicholas Hill at Natexis who suggested that we ask to suspend amortisations and convert the repayment schedule into a bullet at maturity. This may sound counterintuitive coming from a bank, but it was relatively painless for the banking group and is saving us a £15m repayment every six months until final repayment in 2008.

So what are the lessons of the last five years from a European perspective? That the support of a good bank is needed in each of your chosen growth markets and the best option is to allow your banking group to mirror the geographical spread of your markets. Banks are looking for increased return on capital and so consolidating ancillary business with those banks remains the most effective route to maintaining or reducing your core cost of capital.

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