

Focus on the nuts and bolts

The treasury function in large FTSE 100 companies is a well-defined and thoroughly understood part of the business. Processes are structured and treasury policies dealing with issues such as interest rate and foreign exchange risk management are typically understood and adhered to.

In large organisations, teams are divided into front, back and sometimes middle offices, splitting the execution of deals, reporting and other processes between a group of highly trained treasury professionals.

This sophistication is commonplace and can be found in most large treasury departments. But not every company is a multinational with a dedicated treasury function, so how do small and medium-sized enterprises (SMEs) deal efficiently with core treasury functions?

SMEs are a key part of the UK economy. Figures from the Department of Trade & Industry show that 95% of businesses in all industries in the UK are SMEs. An SME is defined as a business with up to 250 employees and a turnover no greater than £30m; this is on a completely different scale to the typical multinational, which will have operations all over the world and a large treasury team to deal with the demands this brings.

DIFFERENT APPROACH TO TREASURY Tony Chitty, Treasury Consultant at TC Treasury Services, sees a big difference in the way in which large corporates and SMEs fulfil a treasury function.

Chitty says: "Listed corporates will have a department of people with a segregation of duties. In these companies everyone understands exactly what treasury should be. For SMEs, it's different. You may have a company run by two operational directors plus a finance director. Quite often, they will not understand the implications of treasury and everything it involves."

Chitty says that although SMEs have treasury requirements, there is often insufficient activity to warrant a full-time treasurer. The responsibility is therefore shifted to the FD, who is not always in possession of all the necessary skills.

He says: "To a large extent, financial control and risk management all revolve around the treasurer's role. If he is in any way out of his depth, it becomes very difficult to maintain control of this responsibility. If the FD is commercially switched on, he will realise that he doesn't know enough to realise how treasury works and will need help in this area."

A MOVING SPEC So what exactly is needed for treasury in an SME? All companies – whether they are SMEs or large listed corporates – differ in their requirements, so the specifics of the treasury function will differ as well. However, while these nuances will shape how treasury is performed, the basics remain crucial.

Ruth Cooke, Group Director of Resources at Weston-super-Mare-

Executive summary

- Small and medium-sized enterprises are vital to the success of any economy, but few SMEs can afford to have large treasury teams on their books. However, they still have to cope with treasury transactions which can be as demanding, complex and important as those undertaken by large companies. So how can smaller companies effectively and efficiently deal with treasury?

based housing association Arcadia Housing Group, sees core treasury values as vitally important.

Cooke says: "You have to focus on the nuts and bolts. You have to get your cashflow right and your business performance right. You have to understand your key financial risks and how to manage them. For small treasury departments, your absolute main task is liquidity management."

Arcadia employs a treasury manager and two part-time treasury officers, who attend to the group's cash management needs. As a housing association it has a very active development programme, which makes cash management very important. For Cooke and her treasury team, cash management is about day-to-day large-volume, low-value tasks and a very large capital spend.

Cooke says: "We are managing a development programme which is about payment to contractors. Because we build properties for outright or partial sale, we are managing a sales programme, as well as managing interest rate risk on our debt portfolio. All of this is on top of the day-to-day operational functions. It's quite a challenge."

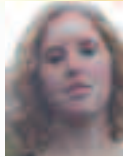
Although Arcadia fits the definition of an SME, it has large borrowing facilities amounting to £140m, making bank relationships a key for the treasurer.

Cooke says: "Bank relationship building and maintaining is critical for us. We have significant borrowing and it is cheap compared with commercial organisations because we are working in a regulated industry. We have to keep the regulators happy and keep the funders informed. It is complicated."

Maintaining strong bank relationships is a focal point for SMEs as well as large companies.

Chitty says: "It's all about managing bank relationships. This is what it boils down to. From a cash point of view, if you haven't got the right overdraft facilities, you will run out of money. If you

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someone with treasury experience. An SME can’t afford a specialist treasury function.”

Chitty agrees that a full-time treasurer would probably not have enough to do in this kind of environment. And with modern working practices evolving, it is possible that a more flexible option could be available.

Chitty says: “A full-time treasurer would get bored very quickly. What they could afford is a part-time treasurer to provide support.”

SMEs benefit from a commercially aware all-rounder to act as FD, including taking on treasury as part of the job. Williams says that while treasury is a secondary function for his company, SMEs in general need to be aware of the implications of treasury management and how effective risk management can be a big deal.

Chitty says that many SMEs do not realise the importance of sound treasury management until it is too late. “Many small companies are not going to recognise that they need this kind of support. Then a problem climbs out the woodwork and all of a sudden they become aware of the gaps in their knowledge.

“This is when you realise the importance of good cash forecasting and cash management. It’s only when you fully understand the drivers of cash in your business, that you can start to pick up where the risks to your company are.”

Keeping up to speed with cashflows, foreign exchange risks and interest rate risks is a hard job for any treasury team. But for SMEs, which typically do not have extensive resources available to them, it is even more demanding.

A WORLD IN MINIATURE Cooke argues that you cannot be afraid to muck in and get your hands dirty if you work for an SME. Cooke says: “It’s very hands-on. We are a small business but we have a huge loan portfolio. We have derivatives and there is a lot of cash management work. It’s all there, a world in miniature.

“It is a much more immediate way of working and you have to be the right kind of person. There’s no point being precious and saying you don’t deal with particular areas. You have to be a generalist and be ready to get stuck in.”

Treasurers are always being told to focus on the basics of treasury, making sure that cash management is carried out to an excellent standard and that the team is connected to the wider company rather than being isolated.

It seems that those working in treasury in an SME have to take this approach. Cooke says: “There is a danger that you could be lured by some of the more sexy transactions. In an SME you have to be realistic about what is important and what will benefit your business and not what you find fascinating.”

haven’t got the right foreign exchange facilities you may lose money on your foreign trading. You must make sure you know what you need from the bank and that your bank is doing for you what you need it to do.”

Managing bank relationships is what helps the treasury function achieve effective risk management. Any company dealing with more than one jurisdiction has to deal with foreign exchange risk management, which inevitably is more of a challenge for the smaller organisation.

TREASURY PROBLEMS Hugh Morgan Williams, Managing Director of broadcast equipment company Canford Group, says: “SMEs that have complicated operations, like Canford Group, which has a range of buying and selling in foreign currencies, can have problems with treasury. We generally invoice for very small amounts, so buying currency from a bank is really not an option.”

The finance function at Canford attempts to offset the risk by balancing purchases against sales. The company has import and export activity within Europe so it attempts to assess the value of exports, which will be in euros, sets a target for purchasing in euros and roughly matches the two.

Williams says: “It’s not an exact science and it does depend on the availability of products. In many ways the treasury function is very much secondary to the product mix.”

Williams says that FX risk management is important to Canford because of its import and export activity. In his view, this does not require a full-time treasurer because the treasury processes are not the most important elements of the business’s day-to-day running.

He says: “It’s a secondary function and therefore when you are recruiting your FD you are not recruiting a treasury specialist, you are recruiting a good FD. It’s a stroke of luck if you get

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