Ask the experts:

How to pull the right levers

AT THE ***TALKINGTREASURY*** CONFERENCE IN LONDON IN FEBRUARY TREASURERS MET TO DISCUSS THE IMPACT OF THE CREDIT CRISIS, LIQUIDITY RISK MANAGEMENT, STRATEGIC RISK MANAGEMENT AND THE CHANGING ROLE OF THE TREASURY. HERE THREE TREASURERS WHO WERE PANELLISTS THAT DAY OFFER THEIR JUDGEMENT ON THE ISSUES INVOLVED.

Alex Hall, group treasurer, ABB

The role of the treasurer is down to the individual organisation and the individual treasurer, but all treasurers need to communicate and articulate what they are trying to achieve. At ABB the treasury function aims to be the strategic partner of the board and the executive committee in executing the financial strategy. It should be an aspiration of all treasurers to be part of the strategy formulating process. Within this context the treasury has three distinct roles.

First, the treasury function has to proactively manage the financial assets and exposures of the group. This means not just the cash in treasury but the financial assets in other parts of the business such as the assets in the pension fund or the cash in the group's captive insurance companies. And the proactive element is vital. The treasurer needs to look holistically across the group to see where financial risks may arise in the future, and not just react to existing risks.

Second, the treasury function is also there to develop financial solutions to support the profitable long-term growth of the group. This can mean finding ways to support customers and suppliers as they look to work with the company, finding the right capital funding for the businesses, and working with the banks to find suitable financial solutions.

The final element of the treasury function is to put in place and manage the company's financial infrastructure. Put simply, without us no one in the organisation could pay a bill. The infrastructure also encompasses areas such as the hedging activity and the relationships with key banks.

So we have an overall strategic input and then we work in three areas to support the business. In the modern world the organisation needs to understand the function of the treasurer. It is not enough for others to think that we are a bunch of clever people who spend all their time working on models.

The ABB treasury function developed its remit following a crisis in the group in 2001-03 which provided a catalyst for looking at how the group operates and organises itself from a financial perspective. Before 2002 we were very decentralised and managed risk on a decentralised basis. That has now changed and where legally and logistically possible we try to centrally manage risk, cash derivatives, insurance, pensions and even real estate to ensure we are moving in the right direction. By centralising risk management, we now have the right levers to pull to execute our strategy. As a result of the actions we took back then, we are now in a good position to cope with the present financial and economic crisis.

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Lucy Fuller, group treasurer, Smith & Nephew

With sales of $3.4bn Smith & Nephew is in a good market segment, with an ageing population driving demand for our advanced medical devices. Most of our major markets are in the developed world outside the UK and so one of the major decisions we took in 2006 was to move to dollar reporting in order to take out translation exposures. We do have to deal with a high volume of foreign exchange (FX) exposure.

We have always been fairly conservative in our capital market strategy and we don't have high debt levels. Over the years we have relied on bank debt. Currently the group has a $2.5bn facility that runs until 2012, and our current debt level stands around $1.2-$1.3bn. Given the current conditions in the credit markets, we think our facilities go far enough. However, in terms of liquidity management, Smith & Nephew decided to terminate its share buyback programme.

Smith & Nephew has a policy of hedging in order to provide the business with certainty in reporting results. We have a high focus on our margins and we are keen to meet forecasts and budgets, so we tend to be relatively short term from that perspective. We look 12 months ahead on transaction hedging.

One point to note is that FX can be a source of competitive advantage or disadvantage depending on the functional currency and location of sources of production of your competitors. It is an advantage that many of our major competitors actually have a similar FX profile, manufacturing in the US and selling in Europe.

In common with most treasury departments these days, we are not a profit centre, so we are not looking to make FX gains. In terms of internal

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reporting it is important for the treasury department to be consistent and to explain what it is doing and what it is trying to achieve. If as a treasurer you change your policy because you had a hunch that the market was going to move in a certain way and you turn out to be wrong, then you would face criticism and rightly so.

Stephen Pugh, finance director, Adnams

At Adnams we divide our business into brewing and associated brands, and retail, which is pubs, shops and hotels. At £50m turnover we are in the mid-cap bracket and like many businesses we have felt the effect of the downturn, issuing two profit warnings in the last 12 months.

Our debt falls into three categories: bank debt, pension debt (we have a long-established pension scheme) and lease debt. We closed the pension scheme to all accrual in 2005. After having been the major part of our debt, the FRS 17 deficit had almost disappeared by 2007.

We have tried to keep our financings very simple in keeping with our size. Our facilities are short term and they are all through one bank. The bank facilities are due to be negotiated soon and it is clear from early discussions that the world has changed in terms of fees, margin and security. Adnams has had a relationship with the same bank for more than 20 years and has stayed loyal despite interest from other banks.

We have given no security and we have no financial covenants. I am a bit of a sceptic when it comes to the advantages of longer-term debt. It tends to come with financial covenants that tie you in reasonably tightly and if breached you have to renegotiate, so you end up with a short-term facility anyway. Had we given covenants, we would probably have breached them last year.

When we issued the profit warnings we ensured that we kept the bank informed by speaking to it the moment we made the announcement. We are an asset-backed business so maybe the bank has more reason to be comfortable.

The last year has been an interesting test of relationship banking. So far our bank has been very supportive, but it is my impression that power has shifted away from the relationship managers and towards central committees, which are making the decisions. And as far as those committees are concerned it is a question of whether they want to be lending to the pub sector in general, rather than us specifically. Is that anti-pub policy fair? Of course not. But businesses like ours have nowhere else to go for finance, and are not of a size to justify rating or a commercial paper programme.

We have noticed that our bankers are asking more probing questions and that the nature of the questions has changed, which suggests the need to justify lending decisions to those central committees. We are happy with how we are placed, but there are concerns in the pub sector more generally.

See Finding The Funding on page 36 for more on *talkingtreasury*.

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