Hot stuff

GRAHAM BUCK DISCOVERS HOW THERMAL PROCESSING SPECIALIST BODYCOTE KEEPS CASH MANAGEMENT CONTROL OVER ITS HIGHLY GLOBAL OPERATIONS.

Macclesfield-based engineering services group Bodycote derives around 90% of its turnover from outside the UK, but is neither an exporter nor an importer. With more than 170 facilities in 27 countries, it is principally a service provider to the manufacturing sector. It is the world's largest specialist in thermal processing services, providing cutting-edge materials technology to improve the strength, durability and corrosive resistance of manufactured metal components.

Two years ago the group undertook significant restructuring to remove cost, close facilities and to move out of low value offerings in favour of more profitable business activities. The strategy has paid off so far; for 2010 Bodycote reported a headline pretax profit from continuing operations of £46.1m, against a profit of £3.7m the previous year. In late April, the group issued a bullish profits forecast for the current year as the positive trends seen in the second half of 2010 broadly continued into 2011. Following a steady rise in its share price over the past year the group's current market valuation is over £725m.

Group treasurer Andrew Hughes reports that almost all the company's sales and costs are in local currency, so there are no trade finance requirements; nor is any supply chain financing needed. "Instead, the manufacturer brings the parts to our facilities for processing and that means we don't have any significant transactional foreign exchange exposures."

Although it does have translation exposures, the group opts not to hedge its profit and loss exposure. More recently it has reduced its hedging of the balance sheet translation exposure. "As with many other UK firms, the sharp depreciation of the pound in late 2008 left us with higher net debt levels in sterling terms than we would have liked, so we have scaled back our active balance sheet hedging and no longer hedge using derivatives," says Hughes. "So the main international treasury role at Bodycote is cash management in territory and arranging funding and defunding of operating companies in 26 overseas countries back to central treasury in the UK."

Territorially, the group's global operations are divided into four main areas: Europe, the Americas (the US, Canada, Mexico and Brazil), Asia (China, India and Japan) and the Middle East (currently limited to an operation in Dubai).

Bodycote's declared long-term strategy is to move into new markets through acquisitions and strategic partnerships. At the same time it does not seek to enter markets "which are not sustainable on a long-term basis". Hughes adds that this policy effectively means focusing on the key emerging markets of China and Brazil, where the group is already established, rather than seeking to move into new territories.

CASH CONCENTRATION AND OTHER ARRANGEMENTS

Bodycote has a centralised treasury department in the UK, which, says Hughes, basically consists of himself and the group's cash manager. Following a period of international growth, the department was set up five years ago and was

established as the group's in-house bank through Bodycote Finance, which directly controls cash management for territories covering around 75-80% of the group's total turnover. In countries where it is not possible or not tax-efficient to use Bodycote Finance, a trading company is utilised as the point of access instead. "We endeavour to get every last bit of cash back to the centre," says Hughes.

This effectively sees treasury operate a cash pool at home in the UK, a zero balance structure in the US and Germany, a pooling arrangement in Scandinavia and a pooling arrangement via local trading companies in France and the Benelux.

Around 75-80% of Bodycote's total business is derived from Europe and the US, where treasury has direct automated control and can fund and defund on a daily basis. In the remaining countries manual funding and defunding is arranged following analysis of weekly cash reporting and forecasting. In emerging markets such as China, Brazil and India, where daily funding/defunding is difficult, Hughes says it's a case of arranging local overdrafts to manage cashflow, although in some territories this inevitably creates a surplus that can't be repatriated.

"In our emerging markets we're limited by local exchange controls, which means that cash management must be carefully timed in line with our capex and working capital requirements," he adds. "As these are all growing businesses, repatriation will become more of an issue in the future, so the arrangements for managing cash and capital structure must be put together very carefully at the outset."

RELATIONSHIP BANKS Bodycote has a small group of eight or nine core relationship banks globally, along with several local banks. It aims to use a single core relationship bank for each country in which it operates.

"There is insufficient ancillary business to justify our using a single bank group for global cash management, so while we use several banks globally we endeavour to use a sole or relationship bank in each individual country," says Hughes. "It seems that each acquisition the group made inevitably brought with it three or four new banks, which then needed to be replaced. We're currently continuing our bank rationalisation in Austria, Switzerland and Italy; once that's completed we will tackle Eastern Europe."

Those relationship banks selected are used by Bodycote to repatriate cash from countries in which it is well established, such as ING in the Netherlands and Belgium, HypoVereinsbank in Germany, Handelsbanken in Scandinavia, Wells Fargo in the US and HSBC in Asia, Middle East and Latin America.

"My challenge is to get better control of that 20-25% of the group's turnover we don't yet control directly," adds Hughes.

Graham Buck is a reporter on The Treasurer
editor@treasurers.org