

BETTER BUSINESS PRACTICES



TODAY, IT'S ALL ABOUT CUTTING COSTS AND BOOSTING EFFICIENCY. SO HOW ARE TREASURERS FARING AND WHAT ABOUT THE FUTURE? **DAVID HARRISON** OF ERNST & YOUNG REVEALS ALL.

The Association of Corporate Treasurers' (ACT) recent UK Treasurers' conference in Brighton was headlined 'Reshaping treasury policies and processes in a new world'. Not surprisingly, one of the key themes throughout the event was the combination of business drivers and technology enablers that together are causing the treasury community to focus on operating as efficiently as possible.

The drivers are clear. As Ronan Dunne, the Head of Finance at mmO² and keynote speaker on the first morning of the conference, said, treasury cannot expect to be excused from the pressures facing the business in general and the rest of finance function in terms of demonstrating cost consciousness, efficient delivery and generally being 'lean and mean'. The enablers were discussed in a series of presentations on treasury structure, systems and outsourcing, together with a host of stands demonstrating what is available.

In this article, I will look at some of the main areas to focus on to reduce costs and improve efficiency, what treasurers are doing in practice and the challenges faced if tempted to proceed too far down this road.

AREAS TO INVESTIGATE.

SIZE AND STRUCTURE. The knee-jerk reaction when pressured to cut costs is to reduce numbers. For many companies this can present a challenge. There is usually a minimum size required for a treasury function to operate viably, to be able to maintain suitable cover arrangements for periods of absence of key personnel while retaining the appropriate degree of segregation to ensure adequate controls.

For larger, more geographically dispersed groups, head count reductions may appear easier. Treasury or treasury-related activities are likely to take place in a number of locations. These may just be local cash management operations but there may be regional treasury centres or fairly autonomous local treasury operations. In these cases, a natural reaction to pressure to reduce costs is to increase centralisation.

This can be presented under the banner of 'reducing duplication of effort', 'letting people (that is, the finance people outside the

Treasury operations Survey 2003

The statistics quoted in this article are taken from the Treasury Operations Survey 2003, which was conducted by Ernst & Young's Financial Services Risk Management Practice in conjunction with The ACT. In the survey, we invited members of the ACT to respond with an assessment of the current state of treasury operations in their firm. The objectives of the survey were:

- to provide a reference point to analyse aspects of modern treasury operations and financial risk management practices in the UK;
- to share experiences and assist organisations of all sizes in these areas;
- to identify the latest trends in aspects of treasury controls and performance measurement in the operations and financial risk areas; and
- to provide an update on the impact of technology on some treasury processes.

The final report is available on the ACT website www.treasurers.org and the Ernst & Young website www.ey.com/uk. Copies can also be obtained by contacting Tina Kirkland at Ernst & Young on 020 7951 4891.

core treasury area) focus on their real job' or 'concentration of specialist skills and resources'. Each of these may have its merit and immediate savings are likely to be generated, but there are longer-term consequences for the effectiveness of the treasury operation which may not manifest themselves immediately.

TREASURY MANAGEMENT SYSTEMS. An array of systems exists designed to improve the efficiency of treasury operations. At the heart is the treasury management system (TMS) itself. Other systems in the treasury area include external data sources, confirmation matching systems, automated dealing platforms and electronic banking systems.

While each of these can deliver efficiency improvements in its own right, the real prize is the additional efficiency improvements that can be gained through connectivity. This includes all the treasury centric systems mentioned above, but also extends beyond treasury. Examples of the latter include linkages between the TMS and the general ledger system, or the accounts payable and receivable systems.

OUTSOURCING. Outsourcing treasury has been a constant theme for many years and of many conferences. It has many variants: the use of fund managers for discrete investment portfolios, third-party treasury providers to handle regional operations, full outsourcing of transaction execution and associated activities. Some of the arguments associated with centralisation can be applied here, particularly for the smaller or regional treasury operation. Treasury skills are specialist and relatively expensive, the size may not be sufficient to generate economies of scale or make it economic to install the necessary control features around the treasury operations.

THE CURRENT PICTURE.

The recent Treasury Operations Survey 2003, conducted by Ernst & Young's Financial Services Risk Management Practice in conjunction with the ACT, looked at current and anticipated future trends in treasury operations and allowed us to see what organisations are actually doing in these areas.

SIZE AND STRUCTURE. About 60% of the treasuries surveyed had been resized in the past two years but in only 14% of cases was this explained as to meet pressure to reduce costs. More fundamental organisational changes or changes in ownership were regarded as much more significant factors. Looking ahead, a similar percentage of respondents expected resizing over the next two years. However cost pressures were again not expected to be a dominant factor in this, independent of changes in the size of the organisation as a whole. It appears that changes in treasury size and structure have reflected more widespread changes in the business rather than occurring as a result of specific cost pressures.

SYSTEMS. TMSs are perhaps not as widely used as one might expect – 30% of respondents continue to rely on spreadsheets or manual methods to track their treasury activities. Internet-based dealing portals are not widely used at present but there is an expectation of increased usage over the next two years, with a clear preference for multi-bank platforms (see Figure 1). Where a TMS is installed, it is connected to an electronic banking system in 41% of cases and to the general ledger in 36% of cases. These statistics suggest that there is clearly scope for increased efficiency in this area.

FIGURE 1
DELIVERY CHANNEL USED FOR TRANSACTING FOREIGN.

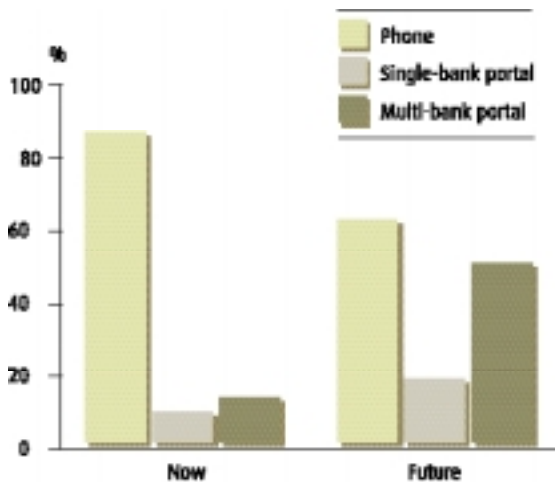
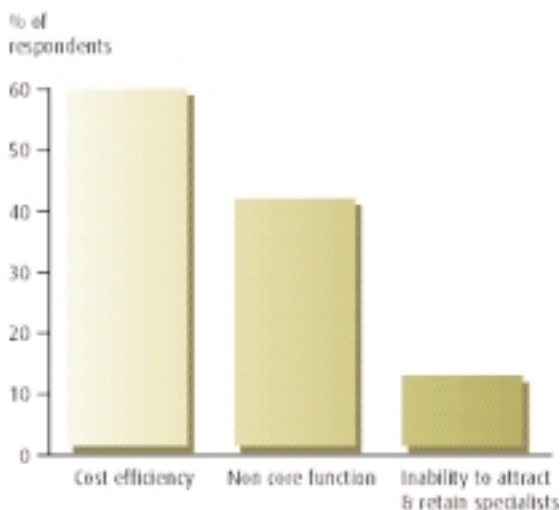


FIGURE 2
MAIN DRIVER FOR OUTSOURCING.



OUTSOURCING. What is the actual evidence on outsourcing? 30% of survey respondents outsourced some aspects of their treasury operation, with the clear driver being cost efficiency (see *Figure 2*). Looking ahead, 38% are considering outsourcing some treasury processes in the future, although this number was significantly higher for those who had already outsourced some functions than for those who had not. The fact that two-thirds of those who had outsourced were satisfied that it had achieved their expectations was clearly encouraging them to consider extending the process.

POTENTIAL CONSTRAINTS.

In pursuing the constant drive for efficiency, it is important to be aware of the potential dangers that can arise.

THE NEEDS OF THE BUSINESS. The role of treasury involves identifying and managing the financial risks of the business. The traditional characterisation of treasury as either a cost or profit centre has gone and treasury is now regularly described as a value-adding service centre. However, to deliver this service treasury needs to have the time and resource to understand the risks in the business, to help the business units themselves to better understand the risks and to work with those units to implement business as well as financial risk mitigation strategies. The survey shows how far there is to go in this regard; only 26% of treasurers regard their business units as having a good understanding of financial risks, even though the vast majority of treasurers say they actively work to promote their services and act as advisers to the business units. It appears that more rather than less effort is needed in this regard.

EXTERNAL FORCES. The environment in which the treasurer operates is constantly changing and treasury needs to be equipped to meet the challenges this poses. The main current focus is, of course, the challenge posed by IAS 39. This has been described as the most complex accounting standard ever introduced and, with the possible exception of its transatlantic cousin SFAS 133, this is may be true. It is certainly the one which places the most demands on the UK treasurer. However, the implications of Basel II for funding arrangements and the consequences of Section 404 of Sarbanes-Oxley Act are other issues of immediate or imminent concern.

ACHIEVING THE BALANCE. So treasurers find themselves caught between, on the one hand, the cost pressures facing the business and, on the other, the need to maintain or improve the quality of service delivered to the business and to meet the challenges posed by the changing external environment. The means to do this are available. It involves, to pick another comment from the conference, in the memorable phrase of the UKT Chairman, Stephen Crompton, "being brilliant at the basics".

Once the operational side of treasury can be assured to run smoothly, whether this be achieved by outsourcing some or all of the operations, or by improved automation and connectivity coupled with rock solid processes, there is the time and space to improve the service to the business and handle the next external challenge. The difficulty is in achieving this state.

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