

A WHOLE NEW BALL GAME



AS IRELAND PREPARES FOR THE INTRODUCTION OF THE EURO **PAT LEAVY** OF FTI EXPLORES THE ISSUES FACING COMPANIES IN THE CHANGEOVER PROCESS.

Ireland, particularly Dublin, has become the premier location for establishing corporate treasury operations in Europe over the past 15 years. Dublin has built up an excellent capability and infrastructure for corporate treasury management through the International Financial Services Centre (IFSC). The region offers an attractive and robust corporate tax rate, which is available for profits from finance and treasury activities, and costs of its financial centres are still attractive compared with other European financial centres.

This has meant that Ireland is recognised as an attractive location and it continues to attract many new corporate treasury operations. Consequently, the euro changeover project has been a critical issue for both international and regional treasury centres located in Ireland, as well as indigenous Irish companies.

THE EURO PROJECT. As Ireland accelerates towards the final conversion to the euro on 1 January 2002 it is interesting to reflect on the experience of treasurers in Ireland to date, the issues arising and the implications for Irish corporate treasury in a new single currency environment in the future. Firms are at different stages in their changeover process in the final stage of euro conversion. To emphasise the immediacy of the completion of the euro project, the following actions are taking place:

- the Central Bank of Ireland has already supplied financial institutions with euro notes and coins, and, subject to specific conditions, also to some retailers;
- under the national code of practice, dual prices should have been displayed in all locations since 1 October 2001;
- all Irish Pound bank accounts will automatically convert to euro-only accounts on 1 January 2002;
- retailers are asked not to accept Irish Pound cheques dated after 31 December 2001; and
- Irish Pound notes and coins will not be accepted after 9 February 2002 and all legacy currency cheques must be lodged before 15 February 2002.

Irish companies have received a constant stream of information about the euro and its implications since 1997. The Irish

government and its agencies, the Euro Changeover Board of Ireland, financial institutions, professional associations and the press have all played an active role in providing information about the euro to the business community so treasurers have been kept well informed about the euro project.

EFFECT OF THE EURO ON STRATEGIC ISSUES. The impact of the euro on corporate treasury in Ireland has been significant but not necessarily in the areas expected. While currency risk has reduced for some euro base companies, the overall reduction in currency risk is limited because 63% of Irish exports and 71% of Irish imports are with non-euro participating countries.

However, there has been an improvement in the availability and maturities of financial instruments for currency risk management purposes because of the greater liquidity of the euro over the Irish Pound. The same can be said for interest rate risk management tools. The greatest strategic change has been the convergence of Irish and euro interest rates (see *Figure 1*). This has resulted in cheaper cost of funds and lower returns on surplus cash.

It was expected that the euro would result in new sources of debt financing through access to euro capital markets, commercial paper and securitisation programmes. While this has happened to some extent, it is really only the larger companies in Ireland which have benefited from this.

International and European treasury centres based in Ireland have been at the forefront of establishing cash pooling and concentration structures for their pan-European cash management activities. Despite the barriers that arise here, such as the lack of European fiscal harmonisation, different local regulatory and legal requirements and varying banking regulations and infrastructures, there has been a significant degree of success in structuring euro banking arrangements more efficiently and facilitating the movement of euro funds in a more cost-effective manner.

IMPACT OF THE EURO ON OPERATIONAL ISSUES. At the operational level, the two areas that have required the greatest attention are systems and banking arrangements. The systems dimension applies to both accounting and treasury applications.

'THERE IS CONCERN ABOUT THE ABILITY OF SYSTEMS PROVIDERS TO RESPOND TO QUERIES TOWARDS THE END OF DECEMBER, WHEN MANY WILL BE LOOKING TO MIGRATE THEIR APPLICATIONS'

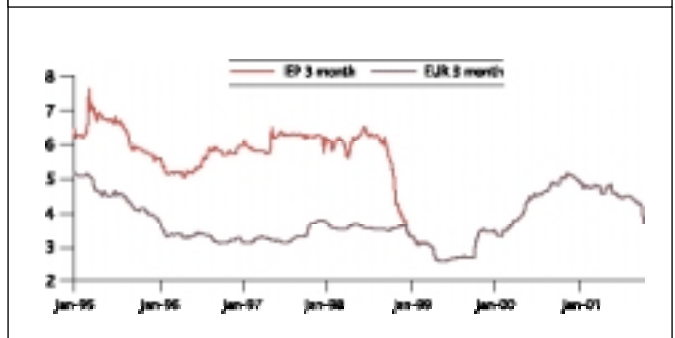
The choice of changeover approach – of either a 'big bang' approach or a gradual switch – is influenced by both strategic issues (such as competition, costs, prices and profitability) and the status of the individual company's technology. Some companies found that their applications were not being upgraded to facilitate euro changeover, while the functionality of euro upgrades varied considerably. For example, some upgrades include a dual currency option, while others provide only a conversion facility. Businesses have been constantly reminded of the need for careful pre-planning for the changeover to their systems and to ensure that conversion routines follow precisely the legal requirements for euro conversion – for example, the use of six-figure conversion factors and prescribed rounding arrangements. There is concern about the ability of systems providers to respond to queries towards the end of December, when many companies will be looking to migrate their applications all at the same time.

The banks have been very much on top of the changeover process. Dual bank accounts are already operating in both Irish Pounds and euros and all legacy hold accounts have been converted to euro accounts. From 1 January 2002 there will be no Irish Pound accounts, although bank statements will show reversed dual display features (that is, all euro transactions converted to Irish Pound values) for some months. It is unclear how many businesses that use specially printed company cheques have not yet arranged for printing and testing. Interestingly, the single currency doesn't apply to euro paper payments, as euro-denominated cheques drawn on Irish banks cannot be used in other participating countries because of different clearing systems and standards across Europe.

Banks have been in contact with corporate clients about their euro cash requirements since early 2001, and companies have been asked to reserve the amount required. But there is evidence that some firms have not given proper consideration to their needs. Some of the final hurdles for businesses to overcome include the following:

- the conversion of payroll from Irish Pounds to euro. Dual processing for electronic payroll payments is currently available, but from the beginning of January all payments files will be assumed to be denominated in euros;
- the redenomination of the nominal par value of share capital to an appropriated rounded value in euros; and
- the development of 2002 budgets by line managers in euros for the first time.

FIGURE 1
THREE-MONTH INTEREST RATES.



EXPERIENCE OF THE CHANGEOVER PROCESS. Many of the larger companies in Ireland established euro changeover project teams at an early stage of the process. The treasurer was often the project team leader, with participation from all relevant disciplines in the organisation. The process involved:

- gathering information about the euro and the proposed change process;
- identifying key strategic business issues;
- relating to changeover plans of customers and suppliers;
- reviewing existing IT systems and applications for euro compliance/upgrade;
- implementation planning; and
- communication and staff training.

Some of these companies had to address teething problems, particularly in respect of systems, and not all the system conversions have gone smoothly. Some firms have adopted a wait-and-see approach and are now scrambling to identify and address issues. This means that problems have arisen simply because companies have been unprepared. There is still concern that some small- and medium-sized firms are not yet properly prepared for euro changeover.

One of the significant economic concerns of the government is that businesses do not try to disguise price increases as part of the euro changeover. While there is no direct mechanism available to prevent such activity, an approach of 'naming and shaming'; has been adopted, with consumers being encouraged to exercise their purchasing power against offenders. The Irish Business & Employers Confederation (IBEC) is promoting a code of practice for the retail trade in the changeover period and companies which subscribe to the code are listed on its website (www.ibec.ie/euro).

FUTURE TRENDS AND DEVELOPMENTS. The final introduction of the euro and the transparency it offers should further enhance and accelerate Ireland's attraction as a location for international and European treasury operations. Furthermore, in the past, many of the treasury operations established in the IFSC were tax-based. The tax factor, while still present, is now less important. Multi-national corporations (MNC) set up treasury operations in Ireland as the group needs to have a treasury service for its European or international entities and to professionally manage the treasury risks these generate. Indeed, many of the treasury operations now being set up in Ireland do not have a tax dimension. The business needs basis for treasury operations is a welcome development in

Ireland, as this will result in more robust structures, which will not be as mobile as more tax-based structures.

OUTSOURCING. The trend towards outsourcing of treasury operations is now well-established and is set to continue. Initially, US MNCs have outsourced their European or international operations in Dublin, but now increasingly more European companies are outsourcing their treasury functions, and the final changeover to the euro will make the selection of Ireland even more attractive.

There is also now a tendency to segregate the treasury function into strategic and operational elements. Strategic covers higher level risk management, critical financings, treasury advice to group entities, supporting key corporate initiatives and treasury policy. Operational includes routine service provision to group entities, transaction execution and mid- and back-office tasks. While some companies will outsource most of their treasury functions, including many of the strategic elements, many now realise that the operational treasury does not add value from a scarce resource and they opt to outsource this element.

We expect to see more companies, especially European ones, selecting the outsource option, not only for quality service and value, but also to meet the current drive towards headcount and cost reductions, and the single currency will facilitate this consideration.

TREASURY TECHNOLOGY. Euro transparency and commonality also provides a platform for further developments in treasury such as the application service provider (ASP) solution for treasury IT. But while vendors may claim that treasury systems/IT are becoming more user-friendly, they are actually becoming more complex, yet companies and their treasuries are becoming more dependent on them. Companies are struggling to stay on top of treasury IT and to get full value from it. It is now necessary to have a continuous availability of a combined treasury business and treasury IT-literate resource in order to utilise IT effectively in the treasury function. However, such a resource is scarce and most companies are unable to justify it. For those reasons we believe that ASP solutions for treasury IT will develop as a trend.

DRIVING CHANGE. The changeover to the euro for Irish treasuries will be completed in a matter of weeks. Participation in the euro is one of the factors that make Ireland, particularly Dublin, an important location for treasury operations. The single currency will also facilitate future changes in the way in which treasury operations are managed, especially in the areas of outsourcing and ASP solutions.

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