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CORPORATE TREASURY

REASONS TO BE CHEERFUL

OUTLOOK Despite global uncertainty, the UK's economic situation is improving, which is good news for treasurers, writes **Christian Doherty**

There's never been a shortage of experts claiming to accurately predict where the economy is going, and how fast. Indeed over the last few years a cottage industry has grown up around the continuing economic uncertainty, with predictions of impending economic collapse seemingly being issued on a daily basis.

For corporate treasurers, then, acceptance of those factors they can't control must sit alongside the need for a clear vision of what they can do to protect their businesses in a time of such instability.

The main priority for most treasurers now is to understand the prospects for the economy in the medium term. And so it's tempting to describe George Osborne's most recent effort as a "Keep Calm and Carry On" budget. There were few radical new measures, and very little deviated markedly from what was begun last year. Deficit reduction remains the focus, while the Chancellor once again reiterated his determination to help the private sector drive the recovery.

So that leaves the UK economy aiming for a sustained recovery in line with expectations and so far, signals are mixed. Interest rates remain low but GDP growth is still stubbornly refusing to shift into a higher gear.

That said, there are reasons to be cheerful: manufacturing performance – which can deliver serious benefits to the economy in terms of exports and employment – is picking up, while the PMI signs are better. But unemployment is still a concern. And the only way to tackle that will be through job creation in the private sector.

With that in mind and as we reach the mid-point of 2011, treasurers can afford themselves a level of cautious optimism. The UK is experiencing sustained, albeit fragile growth; interest rates remain low, and rebalancing of the economy is beginning to take effect. Added to that a banking sector that seems to be recovering from its nervous breakdown, and the signs are good.

But while the global economic recovery has taken hold in some regions, serious dangers do remain. Fiscal tightening and de-leveraging by Western households may stall the incipient growth. Meanwhile the threat of bank failures and sovereign default may have temporarily slipped down the news agenda, but they remain real.

CONTINUED ON PAGE 03

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Your feedback is valued by us. Please send in your opinions to editor@raconteurmedia.co.uk
For information about partnering with Raconteur Media please contact Freddie Ossberg T: 020 7033 2100, E: fo@raconteurmedia.co.uk, W: www.raconteurmedia.co.uk

CONTRIBUTORS

CHRISTIAN DOHERTY
Christian Doherty is a freelance business journalist with 10 years of experience of writing for a range of titles including *AccountancyAge*, *Management Today* and *Financial Director*.

NEASA MACERLEAN
Neasa Macerlean writes for the national newspapers and other titles on a range of issues including business, the law and energy. She qualified as a chartered accountant.

HEATEHR MCKENZIE
Heather McKenzie is a freelance journalist and editor with 27 years of experience in journalism. Her expertise spans financial services from wealth management, investment banking, through to commercial banking and trade finance.

ROD NEWING
Rod Newing is a chartered accountant who worked in the City before becoming a management consultant. He is now a freelance journalist whose work has been published around the world.

PETER WILLIAMS
Peter Williams is a financial journalist and chartered accountant. He is editor of *The Treasurer*, published by the ACT, and writes extensively on treasury, cash, taxation and financial reporting issues.

CONTINUED FROM FRONT COVER

The Eurozone will remain, at least for the short term, to be the focus of attention. Politics aside, instability and uncertainty within the zone will bring with it a significant financial risk, principally focused on currency movements.

Therefore most corporate treasurers are looking with some nervousness towards overseas markets, particularly in the Eurozone. But while the threats of sovereign default have not altogether vanished, the ratings agencies do appear to be affording those countries most in the firing line – Greece, Portugal and Ireland – a little more credit in their efforts to restructure their fiscal deficits.

For treasurers, then, the fluctuations in currency prices will present the most immediate threat in the coming years. Naturally corporates in all regions will need to be aware of the dangers of trade disputes and the rise of protectionism. In that context, sectors outside banking and finance – automotive and pharmaceutical, for example – may still be vulnerable to shocks.

But undoubtedly, things are better than they were. Looking back over the early part of 2010, treasurers looking to refinance will have seen a growing number of three-year facilities negotiated by corporates.

By contrast, in Europe, the market has been driven by an increasing number of five-year facilities being agreed, with banks happier to offer longer tenor of facilities in order to lock down deals. For instance the likes of Bacardi and Carlsberg are now borrowing at five years. And although pricing hasn't returned to historic levels, terms and covenants have. A strong investment client will often see terms turning in their favour and that is translating into longer tenor of refinancings across a range of sectors.

Most experts agree that as the year wears on, that trend will continue. It might not appear to be so, but there is huge competition for refinancings among banks. The bank league tables, that serve to rank the institutions on how much lending they can get out of the door, are re-appearing, leading to greater competition for premium business.

However, there needs to be some caution added to that: the depth of liquidity in the market will only become clear when M&A activity returns to something like its pre-recession level. And that's unlikely to happen while the bond syndicates continue to be vulnerable to external shock; in many bankers' opinion, that would likely take the form of a sovereign crisis in Spain, Greece or elsewhere.

And of course, while the banks are making more encouraging noises, there's the ever-present issue of regulation. So in that context, treasurers cannot afford to ignore Basel III, which recently came into force. It will impact pricing because banks' costs will be increased and that will likely be passed on to clients.

And swiftly on the heels of Basel comes the recommendations from John Vickers' Independent Banking Commission. The mooted new capital and liquidity requirements are more onerous on banks than Basel, while the other central proposal to make banks separate their investment and retail arms to make sure that troubles in one wouldn't impact on the other will also have a ripple effect should they come into force as planned.

The big question for treasurers looking to read the runes will be: how those and other changes will impact the levels of liquidity available?

> Corporates in all regions need to be aware of the dangers of trade disputes and the rise of protectionism

Crises in places like Greece are still a worry for corporate treasurers

INTRODUCTION

The background to any discussion of financial matters is the financial crash or 2008, the worst in a generation or more. Its reverberations are still being felt by the whole world, of course, but corporate treasurers more than most are still adjusting to the post-crisis world. In this report we aim to look at the most pressing issues that face treasurers in 2011.

So on pages 4 and 5, we look at the vital issue of training. Gone are the days when you could learn treasury on the job; these days proper training is a prerequisite – the consequences of mistakes are too grave, and too obvious. We all know now, if we didn't before, that the global financial system is more interconnected than ever, and the biggest training providers are expanding their horizons to train more overseas treasurers.

And then there is the problem of liquidity and of access to funding. With banks still reluctant to lend, treasurers are having to look at innovative ways of ensuring that money flows through their companies. They are also forced to become creative in finding sources of money and entities that once seemed exotic, such as Islamic finance, sovereign wealth funds or Chinese and Indian banks, are becoming real options. We look at these issues on page 14.

Uncertainty and risk both loom large for the treasurer, and on p11 we look at strategies for managing a fluid situation and how to ensure that you are prepared for the worst, while on pages 12 and 13 we address the issue of managing risk, something which has become a central issue for all businesses following the financial crisis. On page 6 we look at the liquidity challenge.

Amid all the technical talk, morality still plays a large role in all business, and that is at least as true for the treasury function for everybody else. On page 10 we investigate the importance of training staff to behave ethically.

Underpinning the whole of treasury, of course, are the systems that are built on top of SWIFT system. This has revolutionised the way that treasurers can track and allocate money, and on pages 8 and 9 we look at just how such systems have made the treasurer's job easier – and at the same time far more complex.

It's reminiscent of the ancient Chinese saying – or was it a curse? – may you live in interesting times. We certainly do.

Jeremy Hazlehurst, editor