ALTERNATIVE FUNDING

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Treasurers are looking further afield for sources of money

FINANCING In the UK banks are still loathe to lend, but other institutions such as Chinese and Indian banks are looking for places to put their money. The clever treasurer should pay heed, writes **Neasa MacErlean**

■ One of the main issues keeping corporate treasurers awake at night is access to finance. Bank lending to business fell 4.3 per cent in the year to February, and some other important sources of funding have also shrunk back. However, there are alternative financing supplies which can be tapped into by organisations that plan ahead.

Many advisers believe that corporate treasurers need to research alternative funding sources even if they do not need the money now. They believe that the bank lending market is going to be both in shorter supply and more expensive for the foreseeable future. "Banks are going to look at the markets where they make the most money, those that are growing fastest," says consultant Bob Lyddon of Bob Lyddon & Associates. "Overseas opportunities will be cut out, and treasurers are going to find there are fewer people to help them." He thinks that regulatory plans to force banks to hold more capital will make them concentrate on a core of profitable lending clients, supporting them mainly in their domestic markets. The requirement to increase their capital reserves will also make lending more expensive.

Those organisations which are demonstrably doing well will not have trouble getting access to cash, says PricewaterhouseCoopers partner Chris Tilbrook, a specialist in debt finance. "If your proposition is right, there's loads of liquidity," he says. But whether or not their businesses are doing well, many corporate treasurers will want to look into alternative sources. Even in those cases when banks are still keen to lend to particular businesses, they are tending to limit their stake at lower levels than before. Lending above £500 million nowadays will usually involve more banks and other lending parties than it did before.

Alternative funding sources range from the equity and debt markets to overseas sources, supply chain management and more specialist options such as Islamic finance. There are also ways of preparing organisations so that they are much more likely to succeed when they seek funding, and there are money management methods which can reduce the need for external financing in the first place. For the majority of organisations, however, the alternatives to traditional bank finance are limited. For most SMEs (small and medium-sized enterprises), they boil down to invoice-related or asset-based lending. And those markets are getting tougher. The invoice-discounting sector "is probably more conservative today than it was a few years ago," says Rob Hunt, SME and mid-market refinancing partner at PricewaterhouseCoopers. "They are looking for more quality," he says, adding that their advance rates have fallen and that they have moved out of riskier sectors, such as construction, recently. Factoring and invoice discounting are ways of getting up to 90 per cent of the value of an invoice paid, by a specialist financing company, as soon as the invoice is raised. It works best for businesses whose turnover is increasing, says Hunt. In cases where revenue is flat or falling, asset-based lending may be a better alternative.

Larger organisations will also be able to look to the equity and debt markets. Nearly £12,500 million of debt was raised in 2010 on the mainstream US dollar private placement market by non-US organisations, according to specialist publication Private Placement Monitor. This was up a third on 2009. Most of these placements are for more than £50 million. Some other parts of the bond market have been surprisingly buoyant recently, including the high-yield end and the floating rate sector. Corporate default rates have been lower than expected and are encouraging investors back into the market. The US's collateralised loan obligation (CLO) market is also showing signs of taking off again after slumping during the downturn, and might help stimulate CLO liquidity on this side of the Atlantic in the next year or two.

In the equity markets, there appear to be more companies trying to raise smaller tranches of capital in specialist placements. Richard Brown, head of equity capital markets at solicitor Hogan Lovells, is seeing a trend for pre-IPO financings and for small equity fund-raisings of under 10 per cent. A pre-IPO (initial public offering) is a way of raising one last tranche of private financing before a company goes public. A small equity fund-raising of under 10 per cent can be done cheaply (without the need for the usual documentation) and quickly (often overnight). Both means are a way of avoiding being exposed to equity markets for weeks. "IPO markets are fickle beasts," says Brown.

Islamic finance is another source of funds which used to be regarded as specialist but which is now becoming more widespread. London is the second most important location, after Dubai, for this type of funding, according to accountant BDO. Unable to borrow on the money markets or to use derivatives, Islamic banks avoided the main problems of the financial crisis. "This has to be classed by corporates as opportunistic and specialist finance," says Bob Lyddon. "But anything around leasing can work very well with Islamic finance."

Companies expanding abroad face both challenges and opportunities in getting the funding. "If you want to fund operations in Shanghai, you have to fund them locally in Shanghai," says Adrian Rodgers of consultant ARC. "Investing in China is forcing corporations to do all sorts of things that they would rather not do." However, there may also be assistance available from sovereign wealth funds abroad and from foreign banks. "There's definitely a move from Chinese and Indian banks to increase their level of lending," says Chris Tilbrook. "A number of them are looking to set up bases over here [in the UK]. It will get more straightforward." The China Investment Corp is an example of a sovereign wealth fund that is currently having its funding increased by its government. China wants to diversify its foreign investments away from US government bonds, and assisting its own companies, particularly in the technology area, to invest in attractive European businesses.

> London is the second most important location for Islamic finance, after Dubai, and it remained stable after the financial crisis

Whichever sources of finance they investigate, corporate treasurers have to plan ahead. "You must stay well-informed and keep all of your lines of communication open," says Stuart Grant, HSBC's head of corporate and structured banking. Heather Swanston, one of PricewaterhouseCoopers' restructuring partners, advises corporate treasurers "to act early" if they need to raise finance. A lot of loans are due to run out in 2014 and those companies need to start acting soon, she believes, if they want to be in good enough shape to get refinancing. Steps they can take include reducing debt by making non-core disposals and managing cash better.

Introducing a specialist treasury work station can assist in getting finance on better terms, says Kevin Grant, chief executive officer of IT2 Treasury Solutions: "Some of our clients get improved credit ratings and can borrow at better rates." These systems can also reduce the need for short-term borrowing.

Experts are agreed that corporates are going to have to work harder in the search for finance. "Corporates have to be prepared to make more disclosure," says Stuart Grant of HSBC. "Corporate treasurers are going to have to travel more," says Bob Lyddon. But the good news is that the finance should be there for treasurers who can make a strong case.