How the Swiss manage corporate treasury risk

Felix R. Gasser and Carl Mantel of PricewaterhouseCoopers set out the findings of a survey into risk management practice and treasury controls in Switzerland.

In 1999, PricewaterhouseCoopers carried out a survey on 'Corporate treasury controls and performance standards in Switzerland', supported by the Swiss Association of Corporate Treasurers. The results of the survey, which followed a first study performed in 1996, provide an insight into trends in risk management, controls and performance standards, and identifies new initiatives and challenges for treasurers both in Switzerland and abroad.

Information and data for the survey were gathered during interviews with corporate treasurers of 40 leading companies, whose market capitalisation represents more than 70% of the Swiss Market Index for non-banks. Survey participants comprised major Swiss firms with a group treasury function and treasury centres of foreign corporates in Switzerland.

The key findings of the survey are set out below.

Treasury organisation and responsibilities

Nowadays the role and responsibilities of the treasury function go well beyond cash and liquidity management. Compared with 1996, an increased centralisation of key treasury tasks was observed; and material financial risks are now managed increasingly on a group-wide basis by dedicated specialists.

Interest rate management, foreign exchange ('FX') transaction management, FX economic exposure management, group bank relationship, tax management and insurance are more often performed at group level than three years ago. In general, participants expect the centralisation process to continue.

Most corporate treasuries in Switzerland continue to be organised as service centres; and the establishment of a treasury committee or risk committee is becoming best practice with major companies.

Risk management approach

Most companies, ie 85% of those surveyed, continue to apply an active risk management approach. Some 3% of the participants take positions unrelated to the business, and another 12% pursue an approach of fully hedging treasury risks. There was no company that did not apply any hedging at all. Equally, there was no common approach to risk management. Corporates pursue different goals and risk strategies depending on factors such as size and capital of a company, risk tolerance, industry particularities, technical know-how and systems capabilities, just to name a few.

Furthermore, consideration is given to a company's core competencies when actively managing, hedging or transferring risk. The number of corporates taking positions unrelated to the operating business has further decreased.

Active FX dealing, with the aim of generating a profit, is usually not part of the mission of a treasury function; the vast majority of corporates do not want to build up additional risk positions and thereby tie up economic risk capital.

During the last few years, various new risk management approaches have evolved. Some companies no longer address individual risk types separately.

There is a new trend towards integrated risk management by jointly managing financial, operational, insurance and other risks with a fully dedicated risk specialist, eg a chief risk officer. Around 23% of participants already have such a position in place. This move towards integrated risk management provides opportunities for treasurers to become the risk manager of tomorrow's corporation.

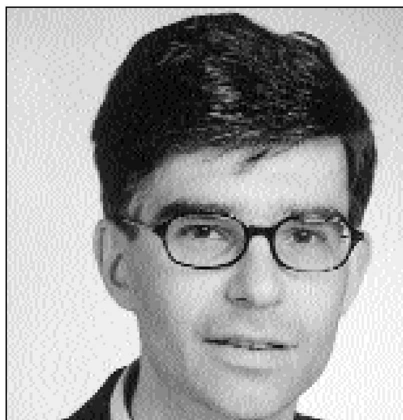
Control standards

The survey shows that the majority of companies have formal policies in place for:

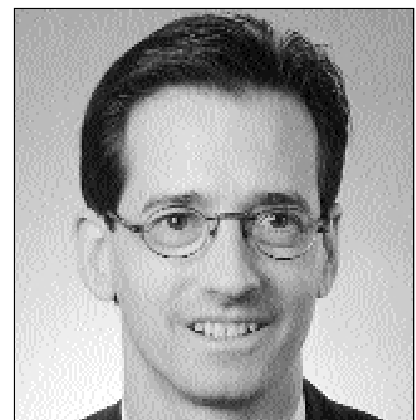
- debt management;
- investment management;
- interest rate exposure;
- FX transaction exposure; and
- FX translation exposure.

The use of policies for interest exposure management is still only applied by 55% of the participants, which is surprisingly low for this core treasury function.

Across all corporates, a wide range of derivative products is used to manage risks. Several companies still do not restrict risk strategies (eg no uncovered short sales) or explicitly define authorised instruments in their policies. The latter is considered particularly important for

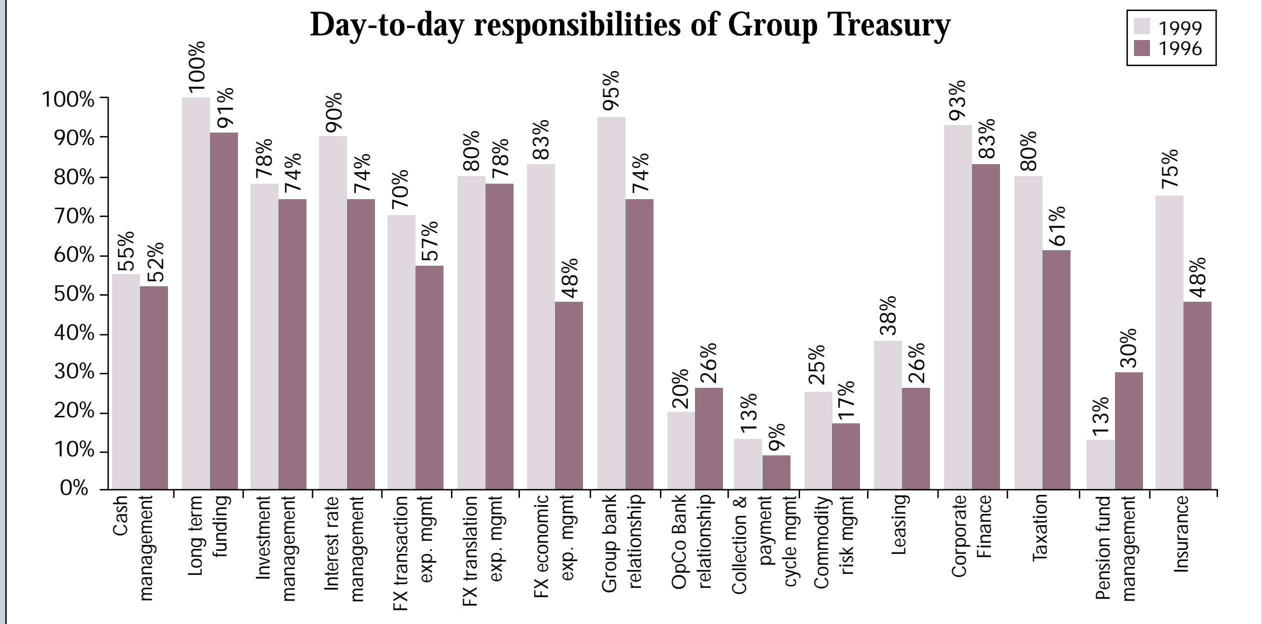


Felix R. Gasser



Carl Mantel

FIGURE 1



structured and 'exotic' products in view of the implications for the monitoring and handling of such instruments.

Among leading treasuries there is a consensus that risk controls are necessary. The use of control parameters by corporates in Switzerland has gradually increased over the past three years. However, the survey shows that for a large number of corporates there still remain gaps in respect of a comprehensive risk management framework, which should comprise formal policies and procedures, effective controls as well as performance measurements. Certain control tools, which are considered to be effective for risk management, such as exposure limits, value-at-risk limits or sensitivity analyses, are not widely applied. In the field of interest rate exposure management, which is a technically demanding area, tailored controls are often missing.

Performance measurement

Is treasury doing a good job? Performance measurements and the definition of specific benchmarks are a cornerstone for board members, senior management and the chief financial officer to assess whether treasury units are working effectively and whether they add value to the company. Some 87% of the participants stated that they consider performance measures to be either 'highly important' or 'important'. Performance measurement is particularly applied at group treasury level. Six out of 10 corporates measure performance for FX exposure management. Performance measurement for other core treasury activities such as interest rate exposure management, short-term liquidity and long-term debt/investments is applied by approximately a third of all companies. Among those corporates applying performance measurement, there are only few applying risk-adjusted measures.

Staff and technology

For four out of 10 participants, corporate treasuries in Switzerland have a size between one and four persons, including support staff. Our survey does not indicate significant changes of staffing levels compared to 1996. Only a small number of corporates remunerate their treasury staff based on individual performance. More companies are remunerating their treasury staff on a team performance basis than in the past.

Several corporate treasuries have gone through substantial technological change

FIGURE 2

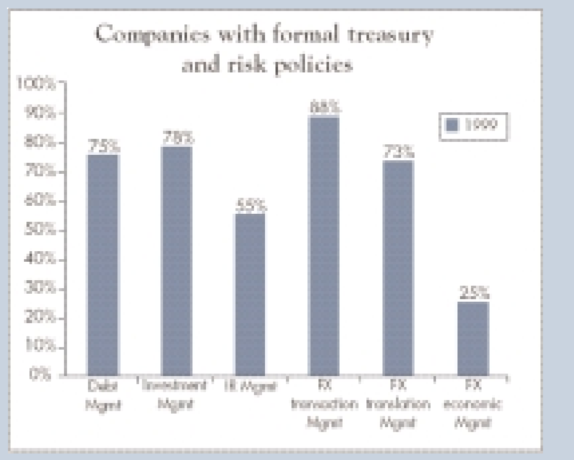
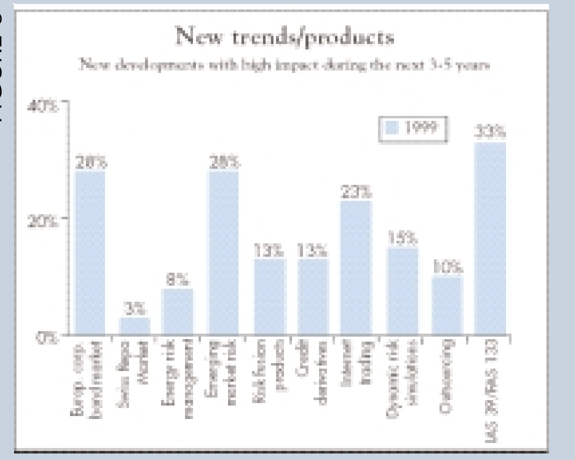


FIGURE 3



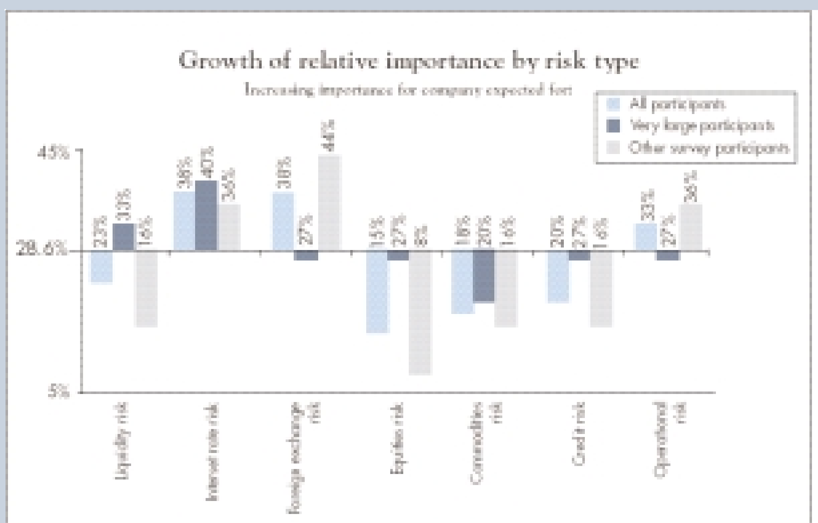


FIGURE 4

during the last three years. Our survey examined the use of technology and extent of automation among corporate treasuries across the major process areas.

More than half of the participants now use treasury management packages to manage their core treasury processes such as deal recording, deal confirmation, operational reporting and settlement instructions.

The number of treasuries applying in-house developed treasury systems has significantly decreased compared to our 1996 survey.

New challenges for treasuries

Our survey also looked into new developments and challenges that treasurers may face during the next few years. New products are offered to corporate treasuries every day. New instruments include risk fusion products, credit derivatives, contingent capital solutions, multi-trigger options, weather derivatives and more. Besides the technical understanding of these complex products, the appropriate capture of such instruments in a treasury management system is undoubtedly a challenge.

Participants were also asked to assess how new trends and products will impact their treasury and risk management during the next five years. High impact is primarily expected from the European corporate bond market, emerging market risks, internet trading and the new accounting standards on financial instruments (IAS 39, FAS 133).

Participants were asked to determine two out of seven risk types, which they believe will become more significant for their company in the next three to five years. The questionnaire included liquidity risk, four market risks (interest rate, foreign exchange, equities and commodities), credit risk and operational risk.

Corporate treasurers of very large corporates envisage spending more time on interest rate risk and liquidity risk in the future, while other survey participants will increasingly focus on foreign exchange risk, interest rate risk and operational risk. ■

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