14-PAGE SPECIAL

CASH & LIQUIDITY MANAGEMENT

Kings of cash

The financial crisis triggered companies of all sizes to save hard and they aren't ready to spend again yet. Farah Khalique explains why

Governments around the globe are stepping up the pressure on companies by publicly expressing their dissatisfaction at what they perceive to be a lack of investment in the economy. At the end of October 2013, the UK's Treasury chief secretary, Danny Alexander, urged British business leaders to start spending their £500bn cash pile to help move the economy into 'top gear'.

But the message appears to have fallen on deaf ears. Days later, British oil and gas giant BP reported in its quarterly results that it had boosted its cash reserves by almost $10bn in less than a year, from $19.6bn at the end of 2012 to $29.5bn by the end of September 2013. This figure has steadily crept higher over the past few years, with its cash pile more than doubling since 2011. BP declined to comment for this article.

This trend is playing out across the globe as companies play it safe, according to market participants. US non-financial rated companies had racked up $1.48 trillion in cash by the end of June, with technology giant Apple leading the way with $147bn in reserves, according to estimates from rating agency Moody's. In March 2013, fellow rating agency Standard & Poor's claimed that European non-financial companies were sitting on a massive $1 trillion cash pile between them. Meanwhile, Japanese companies are hoarding some JPY 225 trillion ($2.4 trillion) in cash, according to data released by the Bank of Japan in June – a sum that is greater than Italy's GDP.

Save, save, save

The trend for companies to hoard cash may have stemmed from the financial crisis, but it shows no sign of abating now that there is a cautious return to growth.

"It is a sign of the economic times that [companies] are nervous about investing and are slow to make that investment," says Martin O'Donovan, deputy policy and technical director at the ACT.

Corporates are suspicious as to the authenticity of economic recovery, given the huge amount of central liquidity being pumped into the major economies, according to Nick Raich, chief executive of The Earnings Scout, a US-based macroeconomics research firm.

"Very few people believe that the global recovery in the US and Europe is real. It is a central bank-induced recovery; no one believes that if it wasn't for the Federal Reserve and the European Central Bank that we would be in this place," comments Raich.

This suspicion, combined with ongoing wrangling in Washington over the fiscal budget and the tax cost of repatriating overseas cash, appears to have induced US chief executives into a short-termist coma that is stalling the long-term economic recovery. "Excess cash is being used to buy back shares and pay dividends, which is good for shareholders in the near term, but a lot of companies aren't moving that excess cash to invest in people in the long haul," warns Raich.

The rise of the mini-banks

It seems that the financial crisis and sluggish recovery have done more than just make corporates nervous. They have fundamentally changed the way that corporates fund themselves, which means bloated cash balances are here to stay.

Corporates are turning to the bond market in droves because low interest rates translate into cheap, long-term funding. Apple famously issued a bumper six-tranche $17bn bond in April 2013, with coupons ranging from as little as three-month Libor plus five basis points to a maximum of 3.85%.

Global corporate bond issuance is bigger than ever, according to data provider Dealogic. More than 5,000 companies issued $1.9 trillion worth of bonds between 1 January and 4 November 2013 compared with about half as many companies issuing just $803bn in the same period in 2008.

The balance has shifted over the past five years from bank financing more towards capital markets, says Jean-Michel Carayon, senior vice president in the corporate finance group for Europe, the Middle East and Africa at Moody's. "Many corporates have moved from having huge bank facilities and little cash on the balance sheet to a more balanced liquidity model, with some bank facilities, but also sufficient cash.

"Investors are right to ask about a company's strategy, and a return to shareholders might be the appropriate thing to do"

"Some have issued more [in the bond market] than their refinancing needs would have suggested, therefore accumulating more cash."

This has led to the rise of the so-called 'mini-banks', as companies build up so much cash that they start to resemble financial institutions, according to the global head of corporate investment products at a European bank. "The multinationals want to become a bit independent of the financial industry. Many also have huge pension liabilities on their balance sheet, and use the cash to finance these liabilities," he says.

German electronics company Siemens even has its own banking licence, while some companies have taken the drastic step of avoiding the banks altogether. These days, airline easyJet does not invest a single penny in any mainland European bank, preferring instead to use money market funds.

Politicians accuse these companies of under-investing in the economy, but many have come up with novel ways of using their cash piles to benefit their suppliers. Mark Coxhead, managing director at supply chain finance solution provider Woodsford TradeBridge, says that many of its customers find themselves sitting on surplus cash piles and wondering what to do with them.

"The problem is that there is very little they can do with it on a short-term basis that gives any kind of return. But they can use the cash to pay their vendors early without getting stuck with changing payment terms," he says.

Large companies, such as mobile telecommunications firm Vodafone, offer supply chain finance programmes, where they offer to pay suppliers promptly in return for an early-settlement discount.

Political pressure

Nevertheless, politicians and investors alike have expressed their unease at the growing size of companies' cash balances.

"To start with, it was a natural reaction to consolidate, cut back on investment and preserve cash, but you do wonder now. Investors are right to ask about a company's strategy, and a return to shareholders might be the appropriate thing to do," says the ACT's O'Donovan.

It is inevitable that governments will apply increasing pressure on companies to invest their cash piles, and moreover investors' attitudes are changing, says Charles Cara, head of quantitative strategy at Absolute Strategy Research. "After the crisis, everyone wanted security with the least volatile stocks outperforming. But there are signs that is moving, with investors preferring high-growth companies that are investing."

Companies are increasingly returning capital to shareholders via buybacks and special dividends, but we have yet to return to the heady M&A pre-crisis days, according to Frances Hudson, global thematic strategist at Standard Life Investments. This has prompted a debate about whether governments should tax >

THE CASE FOR CASH

Politicians love to point the finger of blame at large corporations for hoarding billion-dollar cash piles, but the headline figures bandied about often belie what's really going on

Rio Tinto, the world's second-largest iron ore producer, had cash reserves of $7.2bn at the end of June 2013. Critics might argue that figure is burning a hole in Rio Tinto's pocket, but its global head of corporate finance, Jono Slade, begs to differ.

"There is no 'one size fits all' for the appropriate level of cash reserves and each sector is different," says Slade.

The mining sector's success naturally correlates with commodity prices, but these are prone to volatile fluctuations, not least of all the iron ore market, which is the bread and butter of Rio Tinto's business.

The price of iron ore tumbled by almost a third in less than two months over the late summer of 2012, demonstrating the potential effect volatility can have on cash flows. A healthy cash balance is key to weathering these storms.

Market volatility aside, the metals and mining sector is forward-looking and it needs its large cash piles to fulfil its future, long-term projects.

Rio Tinto's capital expenditure for 2012 exceeded $17bn, and the figure for 2013 is expected to total around $14bn.

"A cash balance of $7bn doesn't necessarily last very long when you bear in mind our high levels of capex and the potential commodity price volatility," Slade explains. "Inevitably, there will be bumps along the commodity road and we want to make sure we can carry on with those important projects and not run short of liquidity in the intervening period.

"Access to financial markets is not as reliable as it once was, whether via bond or commercial paper markets, and at times the banking sector has shown signs of severe distress. Because of quantitative easing we have experienced historically low interest rates, which have reduced the cost of carry. These all lead to holding large cash balances," says Slade.

The global banking crisis changed everyone's view of credit, and Rio Tinto is no exception. These days many corporates are looking very carefully at where their money is deposited.

The critics still argue that large multinationals should spend their burgeoning cash piles, but over the past few years, the mining industry has already invested in its future and returned capital to shareholders.

> "The global banking crisis changed everyone's view of credit, and Rio Tinto is no exception. Many corporates are looking very carefully at where their money is deposited"

Rio Tinto's net debt increased from $8.5bn at the end of 2011 to $19.3bn a year later due to its capital expenditure, acquisitions, dividend increases and completion of its $7bn share buyback programme.

Now is the time to save, says Slade. The miner is expected to further reduce its capital expenditure in 2014 and is targeting savings in its operating and exploration and evaluation costs by the end of 2014. "The mining sector is in cost control and capital discipline mode," comments Slade.

He believes it may be the uncertain economic outlook holding back investment or just the need to protect against potential liquidity shortfalls, which explains why companies haven't invested their cash as much as the critics would like. "We know from the global financial crisis that the world is a pretty volatile place and it is still going through some tough times, so a combination of cash reserves and access to bank lines is important for a company like Rio Tinto," he says.

large companies on their cash piles in a bid to encourage spending, but the idea has been met with much derision.

"It's not really the place of governments to tax [companies'] cash any more than they should suddenly turn around and tax savers for having money in the bank," says Hudson.

A corporate treasurer at a FTSE 100 company dismissed the idea as "crazy". "We don't do M&A and when we do, it's limited. The thought that some tax position might cause you to make rash business decisions is nonsensical."

And for the many SMEs that are crucial to powering economic recovery, the debate on cash piles is completely irrelevant anyway. William Beckett, founder of William Beckett Plastics, says that few SMEs can afford to hoard money. His company almost went bust in 2009 after business fell by 35% and he had to lay off 40% of his workforce, but he fought back.

"We invest everything in people, machines, technology and new products. You need to develop new products and markets, [otherwise] you don't deserve to be in business," he says.

Farah Khalique is a freelance business and financial journalist based in London

Rise of the business partner

HOW CAN TREASURERS INFLUENCE TRADE WORKING CAPITAL BY LIAISING WITH OPERATIONAL TEAMS? JOHN MARDLE EXPLAINS

Reports, surveys, white papers and questionnaires reveal treasurers' concerns over liquidity and funding time and time again. Often they cite inadequate cash flow forecasting and lack of visibility as being the reasons for 'sleepless nights'.

The usual method of addressing these concerns is to use technological or enterprise resource planning-type solutions that have so-called business information packages tagged onto them. They generate spreadsheets and graphs with lengthy analysis tables that do little to explain what is occurring 'behind the data' when it comes to cash.

Furthermore, the organisation's strategy is inevitably to 'internally satisfy' shareholders (regarding dividends), investors (regarding return of their cash as well as a return on their cash) and to generate cash flow from operations to stay in business. If necessary, it will establish a business plan that identifies any need to raise more capital from lenders or investors.

So a treasury function needs to adapt and be agile enough to deliver material that not only meets the internal satisfaction criteria, but also satisfies external stakeholders, such as the marketplace, sector analysts, credit agencies and regulatory bodies. At the same time, it needs to demonstrate to its peers, suppliers and customers that the organisation is 'competitive' and will be viable for the foreseeable future.

This entails the critical measurement and monitoring of not just quarterly earnings figures, annual reports, interim management statements and credit rating reports, but the 'management' by the treasury function of the figures that support these documents, namely working capital and, in particular, trade working capital. Why?

The traditional method of recording days sales outstanding (DSO), days payable outstanding (DPO) and days inventory outstanding (DIO) have proven to be very subjective (see my previous article in *The Treasurer*, December 2012/ January 2013, page 38). Therefore, the cash conversion cycle metric (DSO+DIO-DPO) has fallen from grace and cash flow measures, such as return on capital employed and cash flow from operations, have assumed greater significance. These two measures require a greater understanding of how the capital is employed in supporting:

- Trade debtors (customers who have yet to pay their debts);
- Trade creditors (suppliers who are owed cash by the organisation); and
- Inventory (stock and work in progress).

All other areas of current assets (CA) and current liabilities (CL), such as accruals, prepayments, reserves, etc, are internally generated provisions that are not cash-oriented. So the treasurer can exclude using the traditional working capital definition of CA-CL from their deliberations.

We can now see the treasurer's conundrum. Influencing cash flow, avoiding liquidity and funding gaps, and meeting the organisation's strategy and regulatory requirements, requires treasury to fully understand the customers' and suppliers' flows of cash.

So, it should drill down into the organisation's operational areas and establish detailed analysis of not just the current contract terms and conditions, but also the strategy that will be applied in the short, medium and longer terms to customers and suppliers, and how that will impact upon cash flow forecasts.

Case study

Recently, I reviewed the working capital arrangements of a major European media company. It was cash-rich, very acquisitive and had complex revenue streams. And this was one of its challenges. Shareholders wanted higher dividends, investors wanted 'growth' in their returns and suppliers wanted prompter payment terms. But bank covenants were due for renewal and some loans had horrendous 'on costs' regarding interest, management fees, exit penalties, etc.

Treasury needed greater visibility of how to balance all these demands. So we implemented a three-pronged attack on trade working capital as follows:

- We appointed three working capital champions who reviewed, reconciled and reported on the account terms and conditions and geographical strategies across the globe for customers, suppliers and inventory. They did this with the operational teams in these areas through the use of webinars, videoconferencing, meetings on the ground and regular telephone conversations.
- We produced narratives from each area that reflected the progress being made against predetermined key performance indicators (KPIs) that were fully agreed with the operational teams. These broke down each element of trade receivables, trade payables and inventory (stock and work in progress).
- We linked the cash strategy of the organisation to the KPIs via various initiatives, ie retrained credit control departments in understanding debt default analysis and securitisation/ factoring of sales invoices. In the case of suppliers, the purchasing function headed by a chief purchasing officer reviewed creditors and implemented an appropriate supply chain finance programme that could involve dynamic discounting. Inventory accounts were given named individuals who ensured accuracy and delivered programmes of work that reflected the

true value of the various types of stock and work in progress held.

Treasury is also expected to get involved in the other cash area that is increasingly included in the term 'working capital' and which directly impacts trade debtors and trade creditors, namely capital expenditure (capex).

In fact, the ACT's Glossary of Terms (www.treasurers.org/glossary/W) defines working capital as follows:

1. Working capital is commonly defined as the excess of current assets over current liabilities. This working capital requirement for a company has to be financed by borrowings, shareholders' funds, or a combination of both of them.

2. Some practitioners define 'working capital' more widely, to include fixed assets (in addition to the other working capital items included in the narrower definition in 1 above). This – more broadly defined – working capital requirement similarly has to be financed by borrowings, shareholders' funds, or a combination of both of them.

The fact that cash is required to acquire, improve, maintain and refurbish capital items – whether they be plant, machinery, equipment and/or buildings – means it is part of the statement of cash flows and impacts the cash flow from operations line on the cash flow statement. It could directly affect sales (for example, improved warehousing could cut inventory holding costs and therefore generate greater sales since costs are reduced, or new machinery could minimise scrap and improve efficiency, which again cuts costs and could increase sales). Suppliers could be affected by the location of a new building (leased or bought) due to logistics and freight costs or as a result of the installation of new equipment.

It is paramount that treasury is involved in operational matters related to capex. Why?

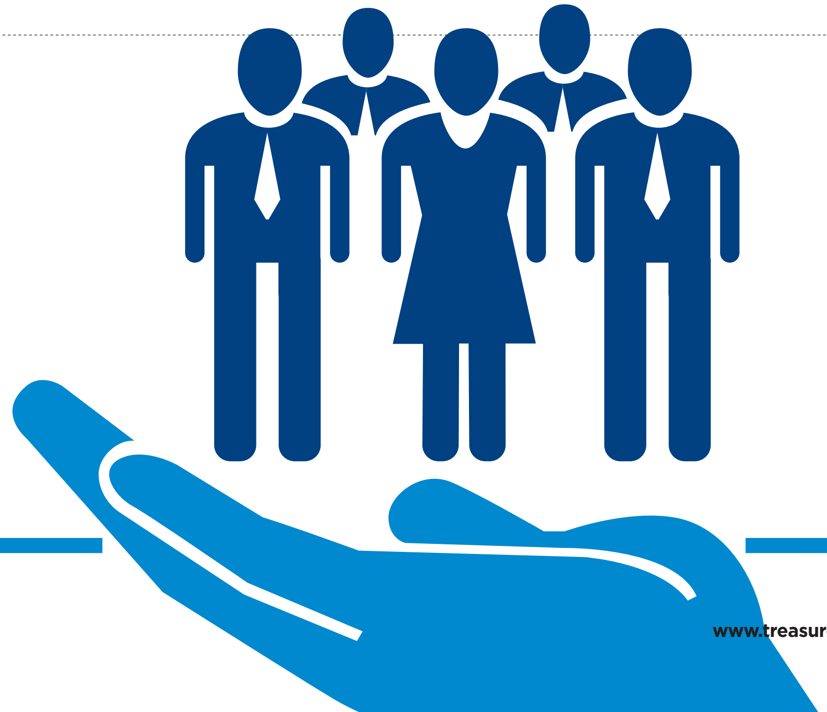
HOW CAN TREASURY BECOME A TRUE BUSINESS PARTNER?

- **Communication throughout the organisation is paramount. Communication to the management teams and board of directors needs to be timely, robust and transparent. It is also important to communicate with external sources, ie the investment community, customers, suppliers, credit rating agencies and, of course, your banking partners. Communication needs to be in an agreed format, with the actions not only agreed, but time-lined. Named individuals should be given the responsibility to deliver the narrative in a suitable language that the audience fully recognises. It is no good quoting financial terms like DSO to a sales guy or DPO/DIO to purchasing functions without first delivering KPIs that everybody understands and that they themselves actually produce and then measure, monitor and manage.**
- **Trade working capital requires specific skill sets associated with not just the area of trade working capital (where you might be an expert in receivables and securitisation, for example), but also in the legal and financial aspects of terms and conditions of supply according to geographical region or even sector.**
- **The capacity, capability and maturity of mindset of treasury team members needs to be fully understood. Taking a 'business partner' approach cannot just be 'bolted on' to the role of a treasurer; the amount of time required needs to be evaluated. In addition, it is important to explore the capability of the team members and, if necessary, enhance this with training or additional resources. Maturity of mindset will entail treasury team members understanding the culture of the operational teams, the environments in which they work and the constraints placed upon those teams, whether they are financial, operational or otherwise.**

- The values involved could be considerable and the funding needs to come from somewhere.
- The financing could be via leasing, contract, asset securitisation or by outright purchase.

An investor might question the purpose of the capex, shareholders could be angry about it (for example, there could be environmental or corporate social responsibility issues at stake, ie use of labour in 'unsafe buildings') and, of course, can the organisation's operational cash flow sustain that asset with regard to repayments, maintenance, etc, for the foreseeable future?

The timing of any capex is critical to meeting customer demands and suppliers could require months of advance warning to ensure supply chains are robust. Capex can also impact on the organisation's balance sheet in terms of the year-end disclosures.



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The best of friends?

There's a knack to managing relationships with your bankers whether you get on with them or not, says Graham Evans

It's hard to believe it sometimes. There you are at some prestigious sporting event, with a glass of top-notch plonk in your hand. Everyone is laughing and having a good time. You may even have just delivered a particularly witty *bon mot* that has both entertained everyone and cemented your reputation as a jolly good chap to have at these events.

Yes, it is hard to believe that they're not your friends. They're not your enemies either. Personally, they may like you a lot, but, ultimately, they're your bankers, and anything they do for you isn't an act of charity, but is in the best interests of the bank.

Of course, in many areas your interests overlap. If they can give you good service, they know you'll be happy. The guy pouring the champagne in the box at Twickenham would much rather be celebrating a mutually successful year than repairing the relationship with liberal amounts of hospitality.

It is easy to be cynical about these events. Thanks to the Bribery Act, we're a bit more wary. However, meeting your bankers and getting to know them is an important part of making the whole process work.

At least that's what I tell my wife every time the taxi pulls up and pours me out onto the doorstep.

Back to basics

But let's look at the basics on which a relationship will be built. If you are lucky enough, you may have been there at the beginning when the request for proposal (RFP) was done and the appointments were made. It almost goes without saying that it is important to get this bit right. If they don't understand what you want, and you don't understand what they can offer, then the relationship will struggle from the off. Not all banks are the same in the way they do things. That doesn't necessarily mean that some are better or worse, but each has a finite amount of investment dollars to spend each year and they don't all spend them in the same place. Do you want the bank with the fully automated statement delivery and payment-matching service or the one with the online case review tracking portal? The former might make fewer mistakes than the latter, but when it does… On the other hand, why should a bank need to develop a major system for tracking things it has done wrong?

The RFP is the basis of what you want, but it isn't a contractual document, and neither is the response (which has been written by salesmen and a specialist RFP team, probably). And it is also possible that there will be mutual misunderstandings of what you asked and what they wrote. After you've made the appointments, you'll then argue over the contracts before accepting most of their standard forms and terms and conditions. At the same time, you'll also agree a service level agreement (SLA).

The SLA is another non-contractual document. But it does represent agreed best practice. If you like, it is a method that shows you how deep the water is. It won't stop you from being flooded, though.

The turnaround times and so on will be worked out in the bank by the people who have to deliver them. It's important to shave off the added fat they've put in, but there's no point in reaching for the impossible. Why insist the phone must be answered after one ring when you know that's never going to happen? Decide what you can work with. There is no point in having a performance measure that is breached on day one. That'll just put it into disrepute.

(On a side issue here, a limit or target that is repeatedly breached will end up being ignored. It will be the target or limit that will be put into disrepute, not the breaching culprit. If you have a traffic light reporting system, it needs to be accurate, but realistic. Having everything at 'red' has less effect than having most things 'green' and one or two things 'red'.)

So, although it isn't contractual, getting the SLA right is important. It must include the

> Dialogue is key. Not just at the treasurer or admin manager level, but at all levels. Each level of your organisation should identify and talk to their opposite numbers. If the service you are getting isn't the service you want, tell your banker

things you think are important and that you stand a good chance of seeing delivered. If that isn't possible, then there's a good chance that either you've appointed the wrong bankers or you are focusing on the wrong things.

As part of sorting out the SLA, you will have to agree the regular performance reporting – both the 'what' and the 'when'. Many banks can give you a lot of the reporting you need through their internet portal, or your own in-house banking system may track what you want, on a daily basis. Realistically, the greatest frequency you are likely to get for full reporting is monthly; most likely it is going to be quarterly.

The other issue is how soon after the period of reporting you are going to receive the report. A quarterly report issued a month after the end of a quarter is likely to be of little use.

Having agreed the service standards and the reporting frequency, you will then want to meet the bankers regularly to discuss their performance and other issues. Such meetings are great consumers of time. If you're based in the city, and your banker is, too, then you can probably arrange them fairly easily: meet up for an hour, then go on your way. If you are based in the provinces, then it becomes more of an issue. Some relationship managers like the idea of doing a grand tour, when they go up to an area and visit half-a-dozen clients or so in a week. Under those circumstances, it isn't always clear that you are the subject of their undivided attention. Of course, you may be able to judge your relative importance to them by whether they structure the trip so that you are one of the clients they take out to lunch.

Although regular meetings tend to come out top in the list of 'Ways to manage your bankers', they can sometimes be an inefficient or inappropriate use of time. If things are going well, then you have no need to meet. If something went wrong at the start of the quarter, it'll be old news by now and any reporting back on the discussions will be even further into the future. In practice, these meetings are actually the best place to discuss future plans, not past performance. And to refine the SLA to ensure it continues to remain relevant to your business.

What these meetings should never be about is springing a surprise on the banker.

In fact, the best way of handling your relationships with your banks is to ensure that there are no surprises at any stage (except for when they tell you they're slashing their fees).

Dialogue is key. Not just at the treasurer or admin manager level, but at all levels. Each level of your organisation should identify and talk to their opposite numbers. If the service you are getting isn't the service you want, tell your banker. Tell him or her now. Don't wait until the quarterly review and then tell the banker you're replacing the bank because of poor service. All that does is create work for you and perpetuate the cycle of unsatisfactory service.

Your relationship with your banker should be the equivalent of knowing the barman in your local pub. You might not get free drinks, but you'll get served first and he'll get your order right.

FIVE STEPS TO SUCCESSFUL BANK RELATIONSHIPS

1) Make sure you know what you want.
2) Make sure your banker knows what you want.
3) If you have a problem, tell them now.
4) Reporting has to be timely and relevant.
5) Nothing should ever be a surprise to either side.

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Watch this space

eBAM MAY ONLY BE IN ITS INFANCY, BUT IT WILL PROBABLY TRANSFORM THE PROCESSES FOR OPENING AND CLOSING BANK ACCOUNTS IN THE LONG TERM. CHRIS JACKSON EXPLAINS

Opening and closing bank accounts and amending mandates to add and remove account signatories remains a labour-intensive and onerous task for many treasurers due to the paperwork required by their banks. Fortunately, advances in bank account management are making these processes much easier for companies with complex bank account structures.

Electronic bank account management (eBAM) is an industry-wide initiative within the banking sector. Its aim is to allow existing clients of a bank to open and close bank accounts, and to amend mandates on those accounts, via electronic rather than paper-based methods. In addition, eBAM uses legally binding digital signatures (electronic codes attached to documents that verify the sender's identity and maintain document integrity), so treasurers will no longer need to collect and send signatures on paper to change the structure of their company's accounts.

The international banking community has worked with corporates, messaging provider SWIFT and technology vendors to ensure that eBAM solutions and terminology are standardised across the industry and provide adequate support to multi-banked corporates.

Companies in the US are leading eBAM and digital identity adoption in significant numbers. Although uptake has been slower in Europe and the UK, realisation of eBAM is starting to gather pace as more corporates become aware of its capabilities. Asia is also starting to embrace eBAM, even though local regulators still require banks to capture and retain various legal paper documents. Running these in parallel with electronic processes is, at least, a step in the right direction.

DISPELLING SOME MYTHS

While eBAM will certainly benefit companies that use it regularly, it shouldn't be seen as the absolute panacea for all your account-servicing woes. Here are some common myths surrounding eBAM as well as responses to them:

Everyone needs eBAM
Don't get caught up in the hype. If you don't need to open and close accounts regularly, and your mandates don't require constant revision, then you may not see much benefit.

It's an industry standard
That is certainly the long-term goal, but eBAM isn't there yet. In the short term, banks' differing back-office platforms and requirements will mean that they will still need their own specific documentation and information. In the longer term, the desire is to move towards a more industry-wide standard – similar to SWIFT messaging – but for now corporates will have to set up discreet eBAM systems with each of their banks.

I can use eBAM from the outset to open accounts
Unfortunately not. The initial know your customer processes that you undertake with a bank will still need to be paper-based. Once these first accounts are open, however, you are free to use eBAM as much as you like.

Benefits of eBAM

Put simply, the benefits of eBAM are efficiency, visibility and control. When a paper request has been submitted to the bank, the client has no way of knowing whether it has been received safely and completed correctly. Furthermore, they cannot follow it through the bank approval process during which opening the account may take many weeks, possibly resulting in lost business opportunities and revenue for the company.

With eBAM, treasurers will be able to open and close accounts either through their treasury management system (TMS) if they have the necessary add-on software or through their bank's proprietary portal. Both channels will be integrated with digital signatures, allowing for the easy collection of account signatories even if they are not physically present. Once submitted, treasurers will know when their request has been received, where it is in the bank approval process and when a new/additional account has been activated.

Another advantage of eBAM is the reporting capability that it provides. Corporates that use eBAM can get real-time reports on their bank account structures. This is a major boon when it comes to meeting audit and compliance obligations since businesses that adopt eBAM will be able to produce customised reports – for example, of individuals who were named on mandates over a certain time period – and demonstrate a high level of visibility and control over their banking arrangements.

It is also a good opportunity for companies to get their back-office account management in order by checking that individuals who have left the company are no longer named on mandates and to add new signatories where appropriate. They may also want to consider rationalising bank accounts and bank relationships as part of the housekeeping process since eBAM is not a single system across the banking industry. Instead, companies must have separate eBAM systems in place with all their main transactional banks.

Finally, although switching to eBAM will require some upfront investment in many cases, the actual day-to-day processes of opening and closing bank accounts and managing mandates should be no more expensive to companies because banks are not proposing to charge them more for using eBAM. Instead, it should be a way for banks to enhance the service that they provide to their clients.

Getting ready for eBAM

So, how do you decide if eBAM is right for your business at this point in time? As a general principle, the companies that will get the most benefit from eBAM are those that have large numbers of bank accounts and complex mandate structures as well as those that make changes to their accounts and mandates on a regular basis. Companies that have simple account structures and mandates with signatories who rarely change will have less need for it, although the ability to generate reports on their account structures may be useful. Paper will remain an option for smaller organisations that do not manage numerous banking relationships. (See the box 'Dispelling Some Myths', left.)

If it sounds like eBAM would help your organisation, consider the following points when it comes to implementation:

1. Know your starting point. Have a clear view of which of the company's accounts are held with which banks, which signatories are mandated on these accounts, and the authorised staff who are permitted to make changes to accounts and mandates.

2. Tackle the paper trail. eBAM has been designed to reduce the paperwork required from your bank, but how paper-intensive is the process for opening bank accounts within your own organisation? If you want eBAM to work effectively, then you need to embrace electronic processing and make back-office processes less paper-based.

3. Review your IT requirements. Work with your bank(s) to understand if your company needs to invest in additional software to support eBAM.

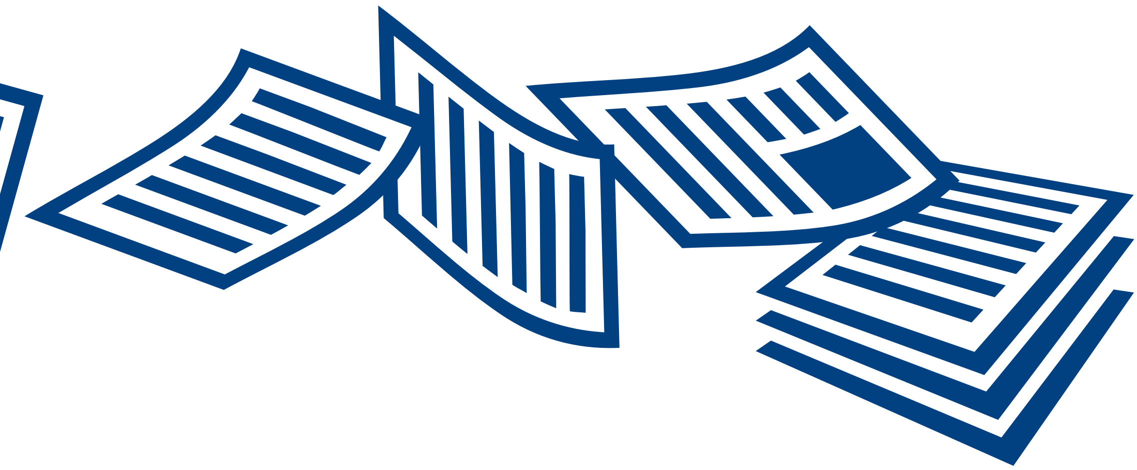
4. Be discerning. Don't assume that you need eBAM with every bank that you work with. Identify your core banking partners, where you have regular account servicing needs, and focus your energy here.

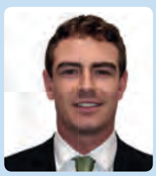
5. Get the right resources on board. If your company's needs are complex, pull in the right level of resource so that when it is done, it is done properly.

Without doubt, eBAM is the future of bank account servicing. As with any technology, you should not embrace it simply because it has arrived, but as a result of consideration as to how it can be used to benefit your organisation.

If there is no benefit, then there should be no uptake. Many companies will take eBAM from some of their banking providers and not from others; plenty more won't use it at all for now. Nevertheless, forward-thinking treasurers from organisations of all sizes should be talking to their banks about eBAM's powerful long-term potential.

What eBAM will deliver





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BARCLAYS

Forecasts and funding

IN THE FINAL ARTICLE IN THIS SERIES, SARAH BOYCE OUTLINES POINTS TO CONSIDER WHEN IMPLEMENTING A CASH FORECAST PROCESS

Access to funding, whether for short-term liquidity or long-term structural debt, is vital to the survival of an organisation. Cash forecasts, which are an important component of efficient funding, are therefore important not only to treasury, but to the whole company.

How to establish a cash forecast process

As cash forecasting is a continuous process, and not a one-off exercise, planning the details of the process in advance will be time well spent. Consider the following:

◆ **The importance of senior management sponsorship.** Although treasury may be the principal users of cash forecasts, little of the information required normally resides within treasury and therefore forecasting must be a company-wide effort. Getting FD support when implementing a forecast cycle can make a crucial difference to the quality and hence usefulness of the forecasts.

◆ **The purpose of the forecast.** An appropriate forecasting technique needs to be selected to suit the purpose of the forecast (for example, for short-term liquidity or long-term funding decisions) and its time horizon. This will influence the level of detail required, frequency of update and the extent of any sensitivity analysis to be undertaken.

◆ **Design the output.** Agree with all users of the forecast what it needs to look like. For example, the FD may want a graphical dashboard presentation, while treasury may require a summary spreadsheet. Many companies use spreadsheets for generating cash forecasts, although there is increasing use of treasury management systems, enterprise resource planning (ERP) or consolidation systems, any of which may influence the design of the output.

> An appropriate forecasting technique needs to be selected to suit the purpose of the forecast

◆ **Information sources.** Having agreed what data is required, in what format and when, the data must be sourced. Sources will vary between companies even within the same industry, but may include:

- Bank balance reporting systems;
- Accounts payable and receivable data;
- Investment plans (capital budgeting plan) including acquisitions; and
- Tax and dividend payments.

It is always preferable to use the skills of those who know a particular aspect of the business best when sourcing information.

◆ **The feedback loop.** In order to ensure accuracy and a continuing focus by the business on forecasting, a feedback mechanism is required.

The forecast should always be reconciled to actual results and refined to improve future accuracy. This accuracy may be related to the nature of the business (for example, a small number of large cash flows with uncertain settlement dates) or to internal processes and systems (timeliness of input, accessibility of data from systems). Accurate information may also be more difficult to obtain in decentralised groups or in those with cross-border operations where time zones or cultural differences can cause confusion.

The challenge is in communicating the value and importance of forecast information to the operating units, rather than it being perceived as merely an exercise in control by head office. Remember to celebrate success and communicate when things are working well.

Conclusion

Cash flow forecasting can be very time-consuming and needs to be justifiable on a cost/benefit basis, but it can be an invaluable tool for the business. Yet it will only be truly useful if it is:

◆ Prepared using reliable base data provided by individuals who understand the importance of what they are doing;

◆ Produced using time horizons appropriate to the purpose for which it will be used;

◆ Updated regularly to reflect changes or known future events; and

◆ Checked against actual numbers and refined by feeding back to contributors over time to improve accuracy.

If you'd like more information on cash management and an opportunity to learn from some of the best in the business, why not consider attending the Annual Cash Management Conference run by the ACT each year? The next conference takes place 12-13 February 2014. For more information, see www.treasurers.org/cashmanagement

ADVICE FROM THE PROFESSIONALS

EXPERIENCED TREASURERS OFFER THE FOLLOWING HINTS AND TIPS BASED ON REAL-LIFE EXPERIENCES THAT MAY BE HELPFUL IN SAVING YOU TIME AND MONEY:

◆ The accuracy required in forecasting depends on the company's circumstances. For a company up against borrowing limits, accuracy is vital. If a company is planning for the longer term, less accuracy is required (it never turns out as you expect, so don't waste effort on spurious accuracy). Think cost/benefit and specify the cash flow forecast accordingly.

◆ Accuracy initiatives can include:
- Process improvements: improving the administrative processes of the 'purchase-to-pay' and 'order-to-cash' cycles;
- Systems improvements: improving cash forecasting systems, for example, by creating automated interfaces between the treasury and ERP systems, to retrieve payables and receivables data;
- Training: aimed at improving the knowledge of cash forecasting and the processes; and
- Performance measurement: measuring the accuracy of the forecast can lead to a better understanding of variances, which can be discussed with the business.

◆ It was the intercompany that seemed to throw our forecasting out. No two units would ever agree on what they thought they would trade between themselves, or on the timing.

◆ Beware trapped cash – it's useless unless you can get it back to the group.

◆ Consider the currency of the flows (not necessarily the reporting currency generally used by the business).

◆ Timing differences impact the opening position – check that the cash forecast excludes items that have already cleared the bank, but includes those that have yet to clear the bank. Understand the approach to value dating taken by your banks.

◆ If business units are responsible for supplying information, that information needs to be concise, on time and in an agreed format:
- Data is impacted by time zones, organisation culture, integration and quality of data from various sources; and
- Be careful about currency issues. A proper short-term forecast needs to be by bank account, medium-term ones by currency, whereas consolidation systems often used in cash forecasting actually destroy this information.

◆ Is the overall cash number realistic given what you know of the business?
- Most people will think of a number and divide by 12 to get an annual budget, so get a feel for the rhythm of your cash flow. Use judgement in assessing whether the forecast is consistent with the shape of the business.
- Understand that everyone has their own agenda – for example, marketing is almost always optimistic; production may always expect to spend capital and get the new line working sooner than they ever do. Treasury can always adjust the forecast manually, but record what's been done and why for future reconciliations.

◆ Produce a range of forecasts – optimistic to median to pessimistic. Such a range can give more information than a single-point type of forecast.

◆ Take care at quarter-end and financial reporting dates, especially in shorter-term forecasts, since the focus in the business may switch to financial accounting and give misleading information about cash.

◆ Operating units won't/can't focus on cash unless they are measured on an interest charge or credit. (Which means you need to be able to calculate/charge it.) Neither can you expect them to manage cash 'properly' unless they have the same view over their balances as you do, and they get the reports, etc.

◆ Most people don't understand that an accounting cash balance (book) is a million miles from real cash (bank). Depending on the purpose of the forecast, it may be advisable to do a reconciliation between the opening accounting balance and the cash/net debt balance.

◆ Forecasting is not a one-off activity; it is a learning process. Actual events will rarely, if ever, match the forecast. Understand variances and use this to improve the next forecast.

◆ Ensure that managers use the information provided and demonstrate to the wider business that they are using it – otherwise the whole process will lose momentum and falter.

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