Managing a Corporate Treasury Department

Session 2: Transitioning to the Modern Treasury

A Presentation to the
NY Cash Exchange
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FECG
THE FINANCIAL EXECUTIVES CONSULTING GROUP, LLC

Session 2 Agenda

- Breaking the ties that bind
- What does the other company do?
- The survey says…..
- Problems and opportunities
- Treasury Do's & Don'ts
- Implementing a transition plan
- Q & A

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Breaking the ties that bind

- Quick review
  - Session 1 – The "perfect" treasury
    - More planning, less processing; treasury is in the liquidity business
    - Fewer "moving parts", more integration
    - Less "float", more flows (cash, accounting, information)
- Bottom Line: Change is hard
  - Change is not free & has a cost
  - Change means risk, but can generate rewards
  - Doing nothing is really not an option given:
    - The demise of "covenant lite" credit facilities endangers access to external liquidity sources (i.e. "the market")
    - Slow (no?) growth environment which has impacted corporate operating cash flows (i.e. internal source of liquidity)

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What does the other company do?

- Reaching any goal requires a series of risk / reward decisions. Ask:
  - What are my peers goals?
  - How do I know if I am doing a good job?
  - How much risk am I willing to take?
- Setting goals via "benchmarking" can help
  - 4th annual survey conducted by the FECG looked at 25 treasury issues
  - Each company asked to rank 25 questions
    - 1 = most important
    - 5 = least important

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The survey says…..

- Sales size among 280 respondents
  - Small : 73% of companies had sales under $250 million
  - Medium : 10% had sales between 250 million – 1Bn
  - Large: 15% had sales greater than / equal to $1Bn+
- Respondents
  - Among Small / Medium
    - 58% were CFO, Treasurer, AT
    - 32% were VP Finance, Director, Controller, Ass't Controller
  - Among Large
    - 30% were Treasurer, AT
    - 46% were VP Finance, Director, Controller, Ass't Controller
- No longer have to be big to be global
  - 17% of companies with Sales < 1BN billed more than 20% of their sales in non USD
  - Business done outside the US (regardless of currency)
    - "Smalls" = 24%
    - "Mediums" = 36%

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The survey says…..

- Companies are becoming more sophisticated
  - 20% of small companies hedge their market exposure
  - 52% of medium companies hedge
  - Favorite Hedges: Forward or SWAP
- Multiple "platforms" (GL, ERP) in use
  - 61% at large companies
  - 37% at medium companies
  - 15% of small companies
- Implications
  - Operational risk issues ?
  - "Cloudy" view when managing liquidity?

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The survey says....(2)

- Treasury resources are small (mostly)

FTE	Small*	Medium *	Large *
1 to 3 FTE	22 %	54	15
3 to 5 FTE	6	7	32
5 to 7 FTE	3	0	15
> 7 FTE	1	4	27

* Totals < 100 % as some co. do not have a treasury function

- Technology still depends on old "systems"

% Mostly / solely dependant on Email, Spreadsheets, Bank Web Systems	Sales > 1BN
Cash Mgt – Collecting, Positioning, Transfers, forecasting	61%
Reporting	57
Debt Mgt – Track principal, interest accruals, covenant	43
Investment Mgt – Track portfolio, interest accruals	36
Risk Mgt	34

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The survey says....(3)

Too many "moving parts" (financial systems) at larger companies?	Sales > 1Bn	Sales < 1Bn
Multiple ERP systems	61%	17%
In house systems (billing, order entry, etc)	59	50
Bank systems	49	63
Treasury Workstations	26	7
Other 3rd party systems	56	24

- Implications
  - Reliance on many, older systems (spreadsheets) does not generate "global visibility" of financial results.
  - More profitability than liquidity systems – Treasury less important?

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The survey says….(4)

- Banking structures still too large?

# Banks in Use	Domestic %		International %	
	Sales < 1BN	Sales > 1Bn	Sales < 1BN	Sales > 1Bn
< 10	96	64	93	53
10 – 15	2	14	2	11
15 – 20		5	1	8
> 20	2	12		20
Not sure		5	3	8

- 10 banks or less "works", but still too many?
- Will lack of credit drive relationship change?
- Strategy – fewer banks or fewer bank accounts?

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The survey says….(5)

2010 rank	Most Important Top 5 of 25 Issues	2011 Rating (1 = most Important)
1	Improve cash forecasting capability	**2.4**
2	More efficiently manage working capital	**2.6**
3	Improve liquidity across business units	**2.6**
5	Seek out role in strategic plan	**2.6**
4	Optimize capital structure	**2.7**

- Forecasting most important due to more uncertainty in 2010 ?
- Top issues are all about "liquidity"

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The survey says….(6)

2010 Rank	Least Important Issues	Rating (5 = least Important)
1	Travel to business units	**3.7**
2	Reduce Number of bank Relationships	**3.6**
7	Develop positions on external Issues (Dodd Frank. Banking reform, etc)	**3.6**
8	Benchmark Treasury capabilities	**3.7**
4	Estimate market risks (FX, int. rates)	**3.8**

- Will managing most important be impeded by the least important
- Will demand for treasury resources exceed supply?

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Problems and opportunities

- Problem 1 - Can top 5 issues be completed without attempting the bottom 5?
  - Reporting – means communicating common goals and performance
  - Strategic planning – moving away from transactional thinking will yield better results
  - Risk Management – no one can accurately predict the future but failure to try is not an answer either
- Problem 2 – Cash forecasting is not being rewarded
  - Cash forecasting – Most important issue, but only 9% of companies had initiated or completed a program in the last 12 months
  - Working Capital – 2nd most important issue but only 5% of companies responding had a program in place
  - Possible reasons
    - Incentives – company focused on profitability, not liquidity?
    - Integration – multiple financial systems increase “friction” among lines of business / financial staff
- Problem 3 – How does treasury demonstrate “value”?
  - Future costs / market risks are difficult to measure
  - Financial statements measure historic events
  - What are best measures of liquidity? Risk?

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Problems and opportunities (2)

- Bottom line
  - Size by itself is not important in determining importance of issues
  - Issues of forecasting and working capital (i.e. operating cash flow) are key
  - Least important issues maybe preventing implementation of the most important (need for more resources?)
  - Technology alone is NOT the solution
  - Neglecting key issues can:
    - Make treasury less "visible" and valuable
    - No value = Restricted career options

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Treasury Do's & Don'ts (1)

1. **Do your diagnostic homework**
   - Only start serious discussions with banks or other vendors if you fully understand current practices;
     - Identify key needs/opportunities
     - Define project scope/objectives
     - Set measurable goals
2. **Do be realistic**
   - Change requires an organization to tackle twice as much work
     - How much time/effort treasury staff can devote to a special project in addition to their normal jobs?
     - Be prepared to change the changes
3. **Do exchange ideas with your peers who have addressed the same issues**
   - From other companies
   - From associations (e.g. via AFP, FEI, AICPA, etc)
   - From networking resources (e.g. FENG)

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Treasury Do's (2)

4. **Do seek answers to business issues**
   - The answers will not always be in treasury
   - Forecasting requires two way communication with the "owners" of the cash receipts or disbursements
   - Email is so 20th century – seek out interactive planning and forecasting tools
5. **Do become a planner not a processor**
   - Career choices are limited – how many Treasurers, VPs, CFOs process?
   - Understanding strategy is important regardless of company size or complexity

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Treasury Don'ts (3)

1. **Don't forget - a bank or vendor's primary objective is to sell**
   - When seeking change will their standard product (technology, bank service) fit your need?
   - Should I get a "bespoke" version in order to have a perfect fit for my company?
2. **Don't rely soley on an RFP "process"**
   - Focus on an the end result and see how much creative effort the banks/vendors are prepared to make to respond to your needs.
3. **Don't set unrealistic completion dates**
   - Treasury projects may not be high priority for everyone, e.g. IT, legal, unit controllers.

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Treasury Don'ts (4)

4. Don't be afraid to change

- As companies grows so does its need for change
  - For small companies - the larger the company the more there is a need for a treasury.
  - For mid size companies – Treasury needs to learn the business.
  - For larger companies – centralization is not enough: forecasting is key
- Keep it simple: Ex: hedging, bank account structure

5. Don't forget to measure the rewards from change; make it part of the plan

- To the business unit – lower operating expenses
- To the company – less borrowing / expenses
- To both – less risks or errors; greater certainty about the future

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Implementing a transition plan

- Start by catalog treasury's strengths
  - Staff – a "few good men/women?"
  - Assets managed – how much? How many counterparties
  - Trusted Advisor – banks, business units, etc
- How should treasury view its value added ?
  - Efficient processor ?
  - Skillful planner / forecaster of cash?
  - Technical expert concerning – GAAP, Tax, SARBOX, etc?
  - Skillful negotiator with 3rd parties (e.g. banks)?
  - Ability to control financial risks?
- Be honest / realistic about weaknesses
  - Staff – too junior? Unfamiliar with company businesses?
  - Information out of date / incomplete?
  - Technology out of date?

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Transition Plan (2)

- Assess current situation
  - The problem is never black & white and the solution is not a “treasury thing”; it is a team (i.e. task force) thing
  - Resist the “solution du jour” from vendors
- Establish goals that are:
  - In sync with company’s profitability plans
  - In sync with business users / suppliers of cash
  - Identify what:
    - MUST stay – market forces at work?
    - MUST go – internal constraints (but which ones?)
    - COULD go?
- When transitioning, track outputs from the 4 “flows”
  - Work flows
  - Information flows
  - Cash flows
  - Accounting flows

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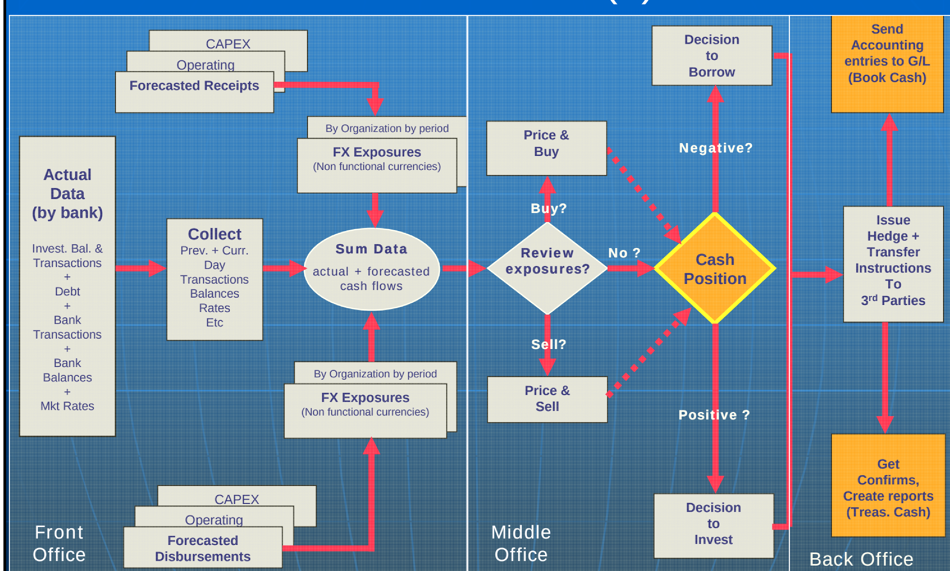
Transition Plan (3)



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Transition plan (4)

- A good plan focuses on benefits to the users
  - Tangible vs. non tangible benefits
  - What is the cost of quality?
- Building a business case for change
  - Cash flow benefits vs risk – function of balances, amounts, speed, opportunity.
    - Operating cash flows – from A/R, A/P, payroll, taxes, etc
    - Financial cash flows – borrow, investing, rates, maturity
    - Volatility?
  - Transaction cost benefits – services / prices / performance
    - Bank services – paper vs electronic?
    - In house processing has a cost
  - Staff utilization – tasks, work flows and hours worked
    - Treasury
    - Non treasury (local controllers, tax, audit, etc)
    - What is NOT getting done?

Transition plan (5)

- Relate transition plan to corporate planning process:
  - P & L – bank fees, net interest expense, tax
  - Balance sheet – level of cash, working capital, LT debt
  - Risk management
    - Units responsible for amount of funds;
    - Treasury responsible for cost of funds (i.e. immunize business units from rate swings)
    - Gains / losses, CTA accounts, % in non functional currencies, interest margins
  - Set up “contracts” with other company units
    - Business units - operating profits at set FX rates
    - Financial units – controls (auditors), tax credits (Tax)
- Establish metrics based on clearly defined metrics
  - Liquidity
  - Risk
  - When is as important as how much

Transition plan (6)

- Top 10 tasks to transition from "processor" to "planner" (ranked easy to hardest)

1. Rationalize bank network
2. Set target balances at banks
3. Re-bid bank services to obtain market prices
4. Work with other financial units to establish joint goals
5. Upgrade treasury technology

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Transition plan (7)

6. Set up pooling or netting arrangement at international locations
7. Create in-house bank
8. Obtain analytical tools to measure risk
9. Imbed performance measures into corporate planning processes
10. Work with business units as "internal consultants"

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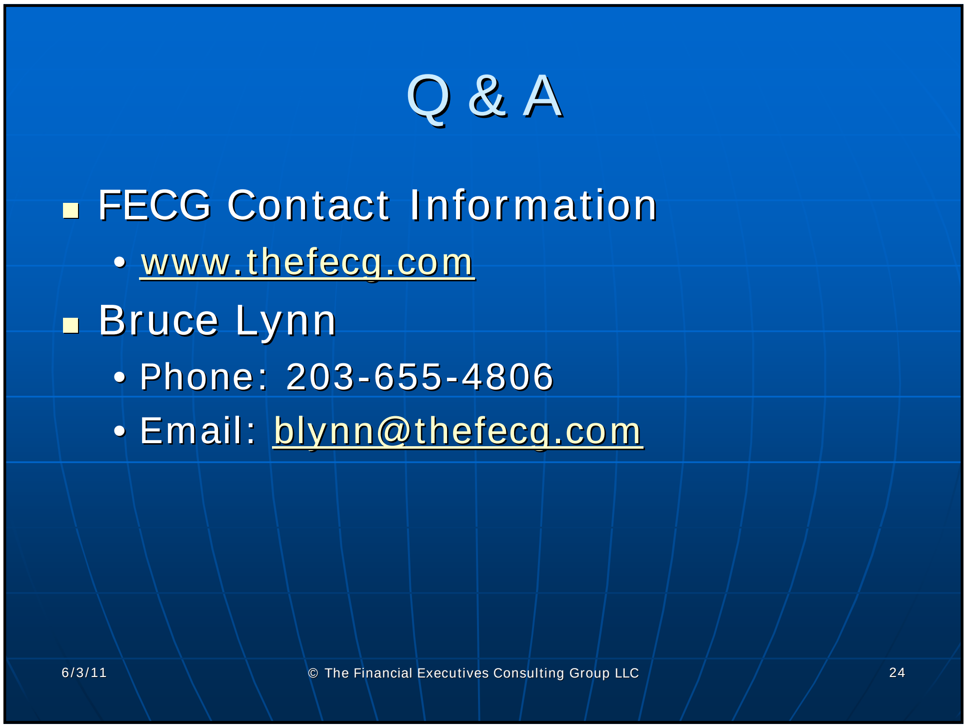
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