

Managing the Modern Treasury

A Presentation to the
Financial Executives International

by

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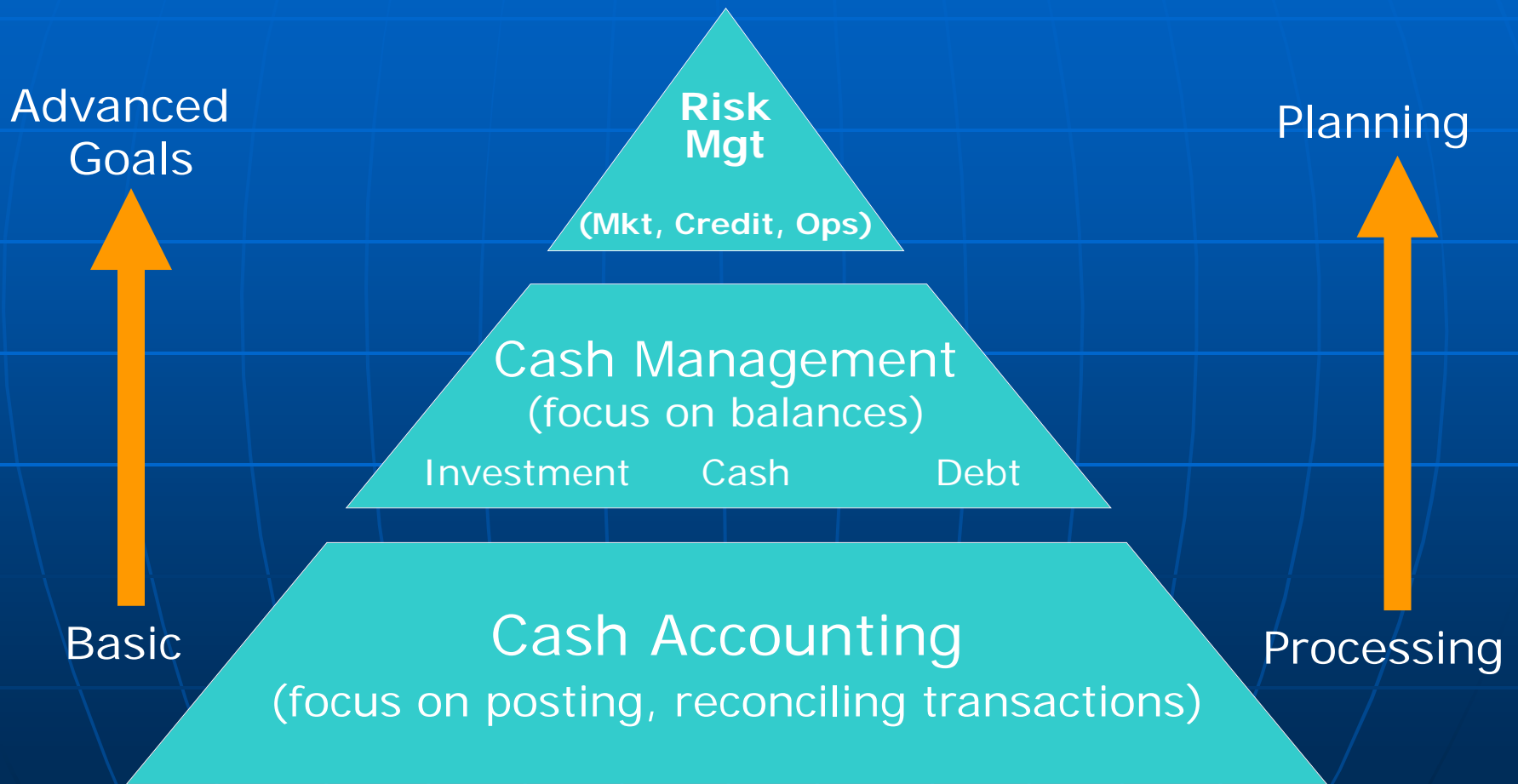
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Agenda

- The traditional role of corporate treasury
- Why treasury's scope needs to change
- Key policies and procedures for the modern treasury function
- Best practices for the modern global corporate treasury
- Making it happen – transitioning from traditional to modern
- Q & A, discussion

The Traditional Treasury

- Focused on Processing
- Resources devoted to repetitive tasks

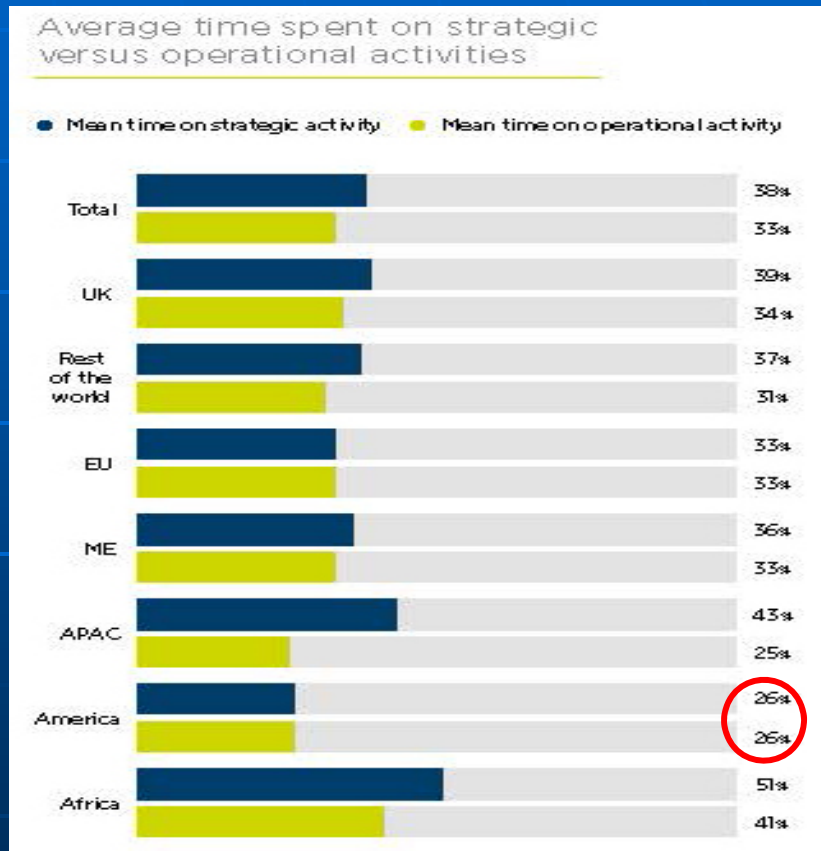


The Traditional Treasury

- Number of S & P companies using cash flow metrics is low
- % of time spent on “strategic” activities is low

S & P 500 Free Cash Flow (FCF)			
Year	Mention in 10K	Defined?	% D = 423
2002	38	19	9
2007	79	28	
2012	94	46	
2017	121	61	29

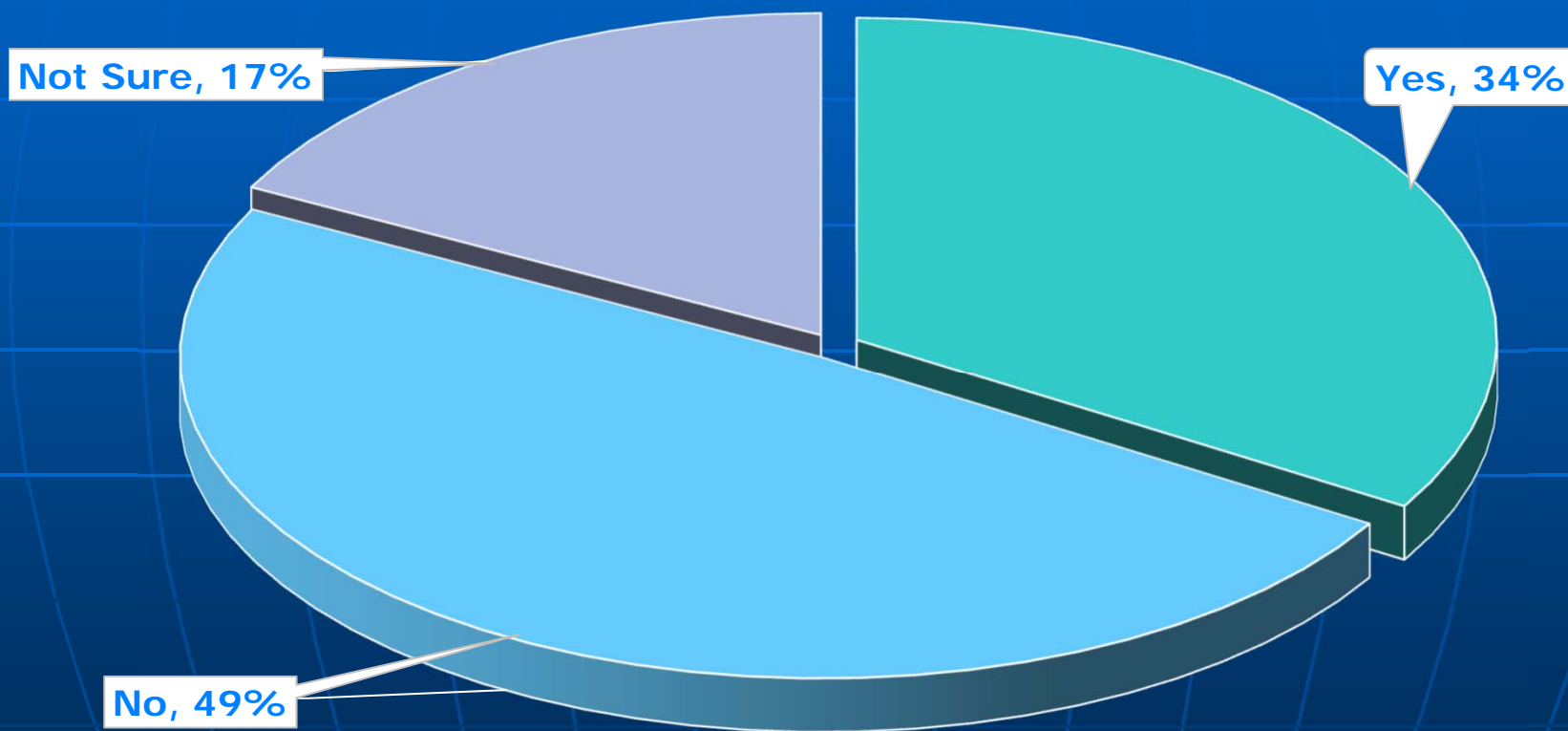
Source:
Georgia Tech Financial Analysis Lab Report - April 2018;
ProEDGAR Online Database, www.pro.edgaronline.com/



Source: Business of Treasury 2018, Association of Corporate Treasurers (ACT)

Polling Question 1

Q1 - Is Your Company Considered "Investment Grade" by a rating agency or bank?



The Traditional Treasury (2)

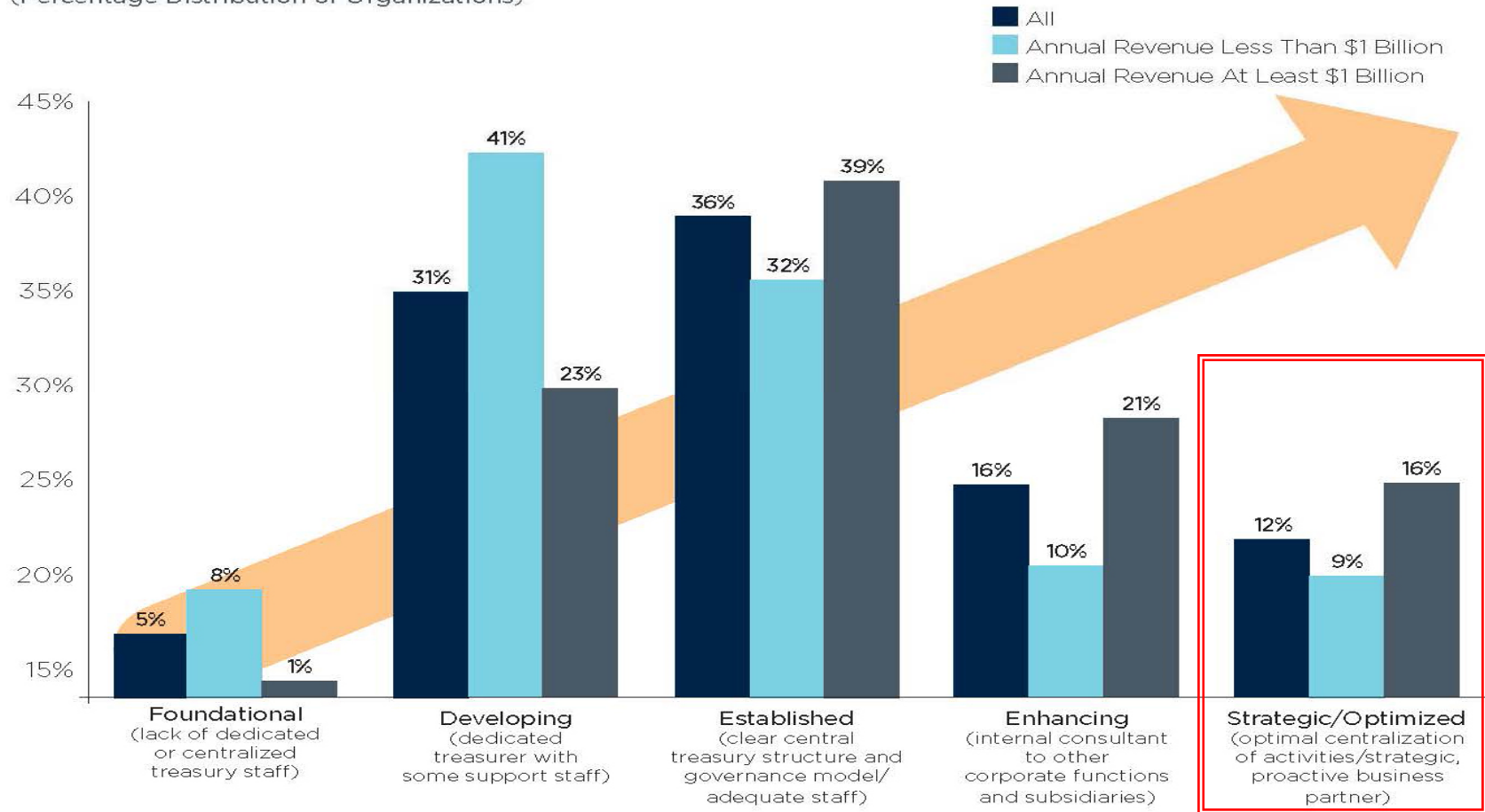
Key Metrics Used Treasury Department Success	2014	2017 All	Sales < \$ 1Bn	Sales > 1Bn
Reduced Borrowing Costs	58%	63	57	69
Liquidity Targets	55	62	57	66
Reduced Banking Expenses	51	49	43	53
Risk Management Effectiveness	49	39	42	38
Capital Structure Support	47	55	46	63
Income Generation	28	32	37	28

- Metrics are mostly P & L oriented
- 51% of Treasuries feel organization NOT using its capabilities*
- 36 % Treasuries NOT part of executive committee or "C suite"*

Source: AFP 2017 (344 responses) p10, p11, p24 / 2014 p11, p12 (243 responses) Strategic Role of Treasury Surveys

The Traditional Treasury (3)

Position of Treasury Department on the Maturity Spectrum
(Percentage Distribution of Organizations)



Source: 2017 AFP Strategic Role of Treasury Survey, p3

The Traditional Corporate Treasury (4)

- Daily cash management operations
 - Obtain yesterday's bank transaction data, identify exceptions, update A/R and A/P records
 - Prepare today's cash worksheet, identify borrowing/investment levels, execute transactions
 - Heavy transaction processing workload
- Bank Relationship Management
 - Maintain lists of banks, contacts and accounts
 - Periodically review / negotiate credit facilities
 - Monitor activity / fees via account analyses

The Traditional Corporate Treasury (5)

- International Support
 - Execute FX spot and forward transactions
 - Assist foreign units to set up pools, netting, etc.
 - Managed as a separate unit within Treasury
 - Limited knowledge of tax impacts of treasury activities
- Capital Markets
 - Support CFO in negotiations for public debt issues
 - Limited knowledge of alternative markets / instruments
 - Intercompany borrowing opportunistic and uncoordinated
- Treasury personnel have limited experience
 - Treasury staff recruited from banking/cash/accounting background; mostly domestic, not involved in the business
 - Promotion usually internal; Treasury staff have low visibility and rarely move into non-financial functions

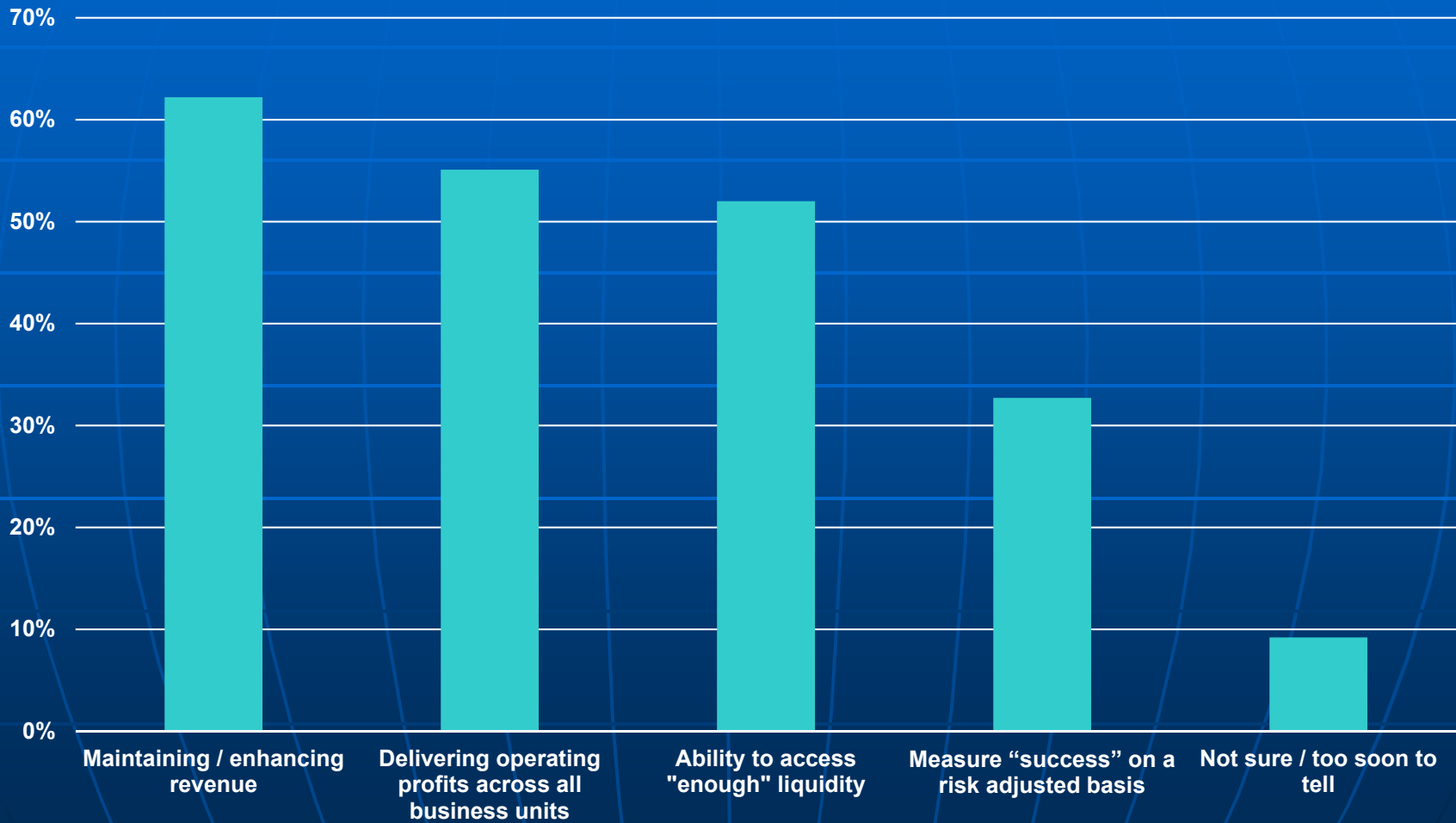
The Traditional Corporate Treasury (6)

■ Bottom line

- Treasury viewed as a processing (not strategic) unit or cost-center -> value added seen as low
- Limited planning or policy responsibilities
- Problems are solved rather than prevented
- Highly dependent on spreadsheets, emails and multiple bank systems because:
 - Treasury systems not priority for corporate IT
 - No integrated views of global cash position or future liquidity needs (i.e. forecast)
- Low headcount - "outgunned" by Controllers or other financial or operating units

Polling Question 2

Q2 - Key Issues To Confront Your Company in 2019



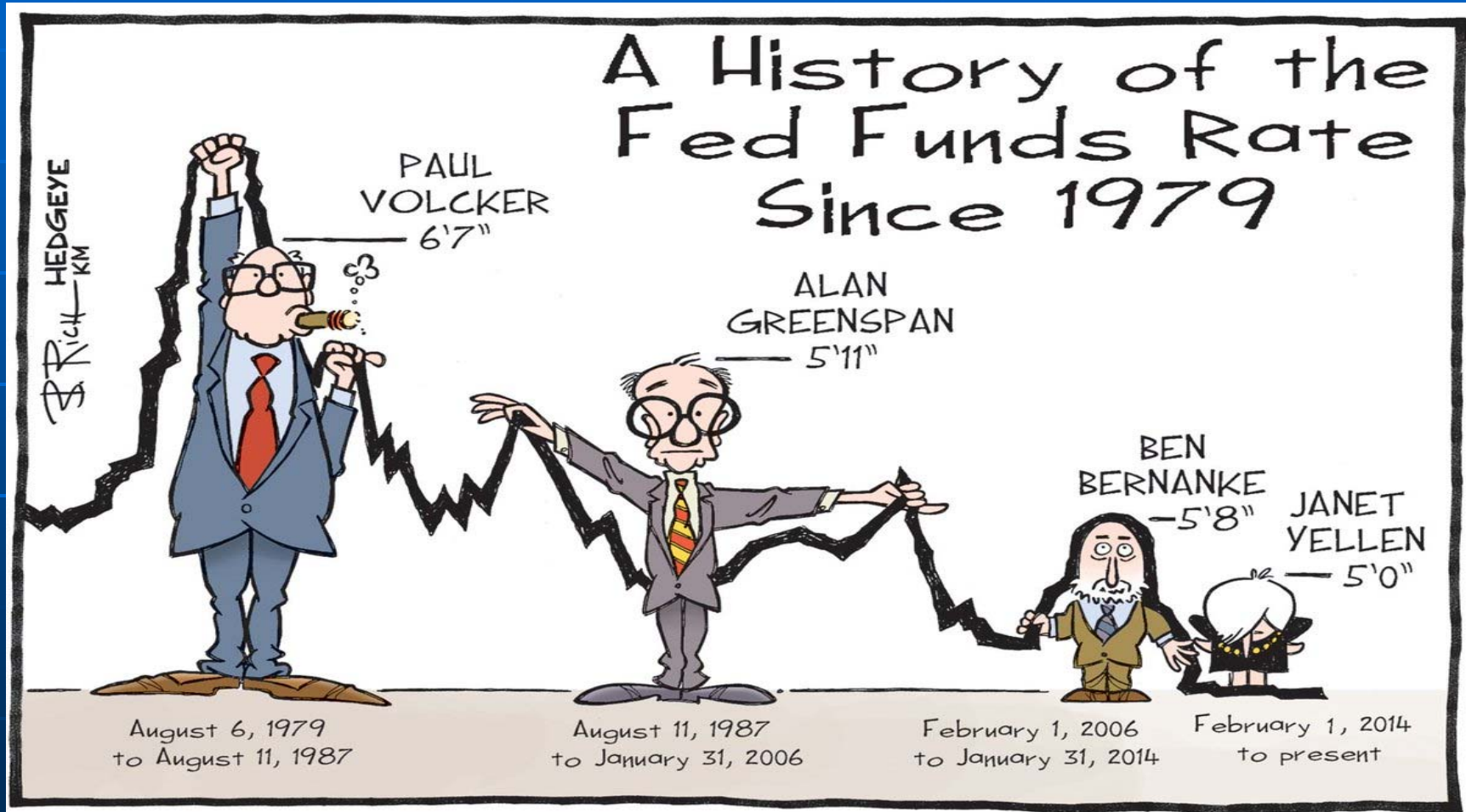
Why Treasury needs to change

■ External factors

- Competitive nature of business = 24/7 demands “global cash visibility” and alternatives in the capital markets (i.e. do I have enough of the “right” credit?)
- Demand for interaction with key corporate customers – “my AR is your AP”; not all customers are profitable
- More complex/unpredictable financial markets
 - New US tax laws – increases after tax debt costs, limits interest expense deductibility
 - More complex transactions – Use of derivatives expands the need for pro-active management of FX, interest costs, commodities
 - Activist investors seek “best” use of cash (or give it back!)
- Regulatory or accounting changes, e.g. Brexit, Basel III (liquidity ratios), lease accounting (leases are debt too)

Need for Change – External Trends

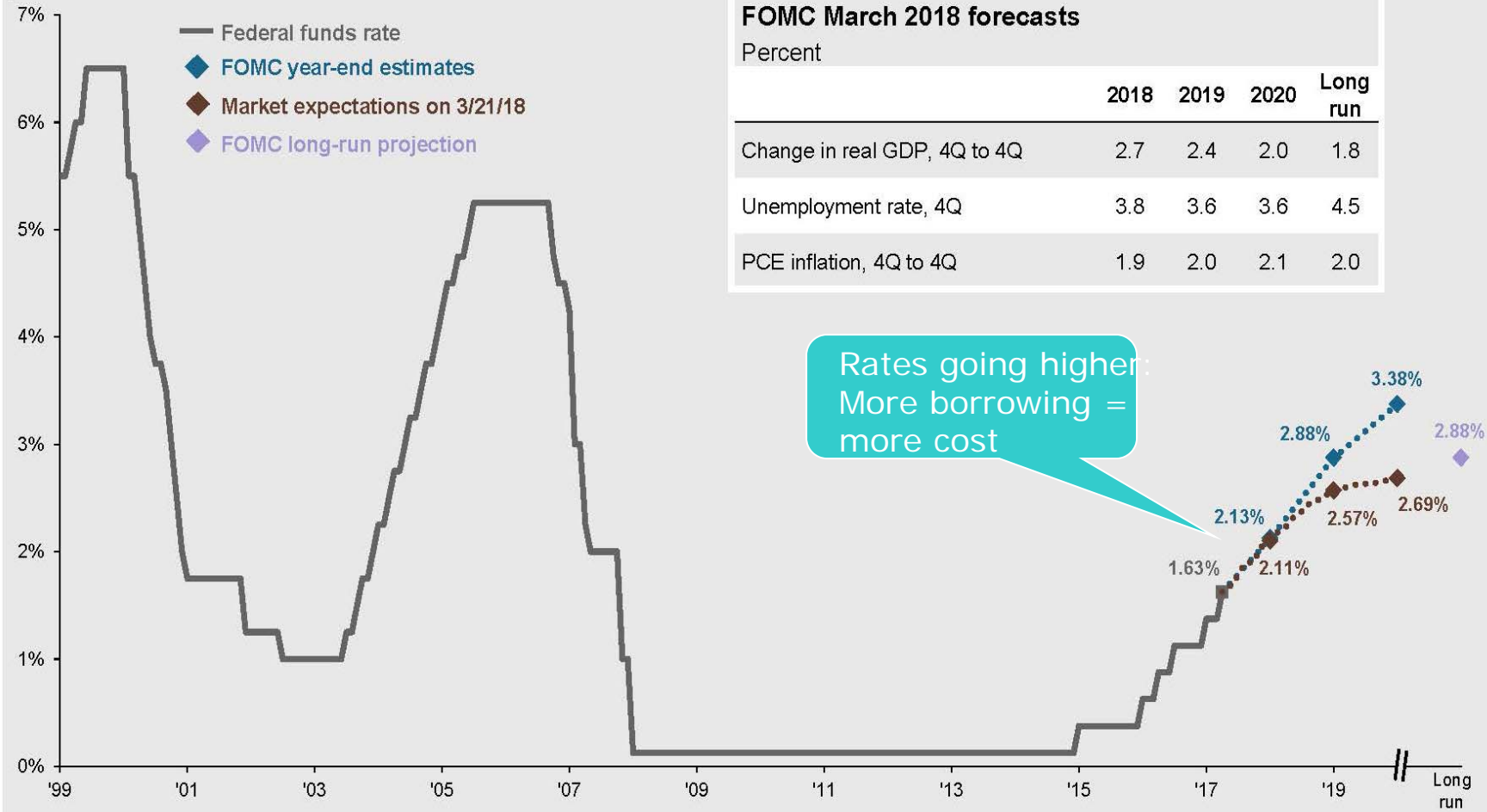
Rates increasing now that Jerome Powell is Chairman (6 FT)



Need for Change – External Trends

Federal funds rate expectations

FOMC and market expectations for the fed funds rate



Need for Change – External Trends



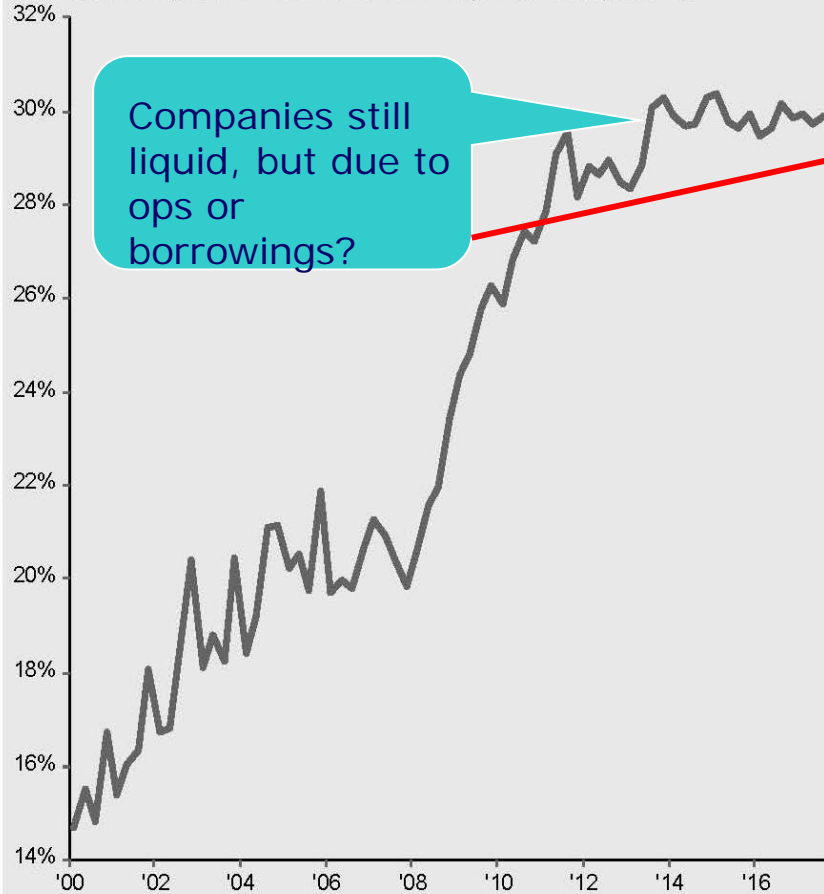
Need to change – Internal Factors

- Internal factors
 - International business and associated interco. FX risks have become more visible
 - Quality of a company's financial management is increasingly recognized as a key competitive factor
 - 70%+ senior management seeks focus on liquidity, risk and working capital management (per 2017 AFP survey)
 - Skills from FX hedging programs can be applied to other risk management issues
 - Keeping up with the competition = strategic views needed
 - Acquisitions - Improving market means higher prices?
 - Best use of funds - CAPEX vs Debt Repay?
 - Cash - Use it or "lose" it (i.e. payouts to investors)

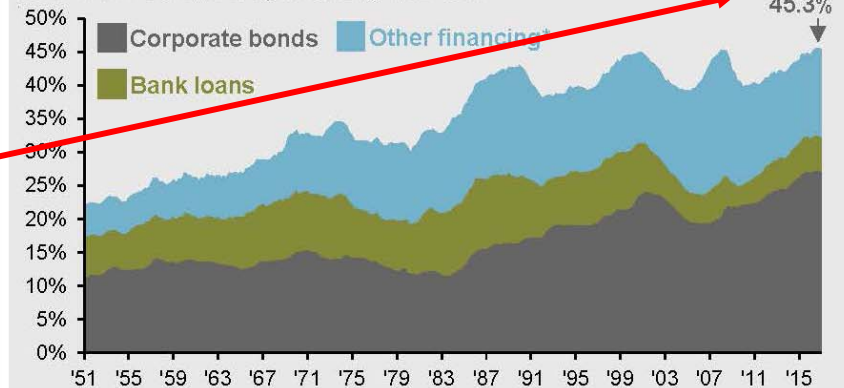
Need for Change – Internal Trends

How much liquidity is “enough” ?- sources

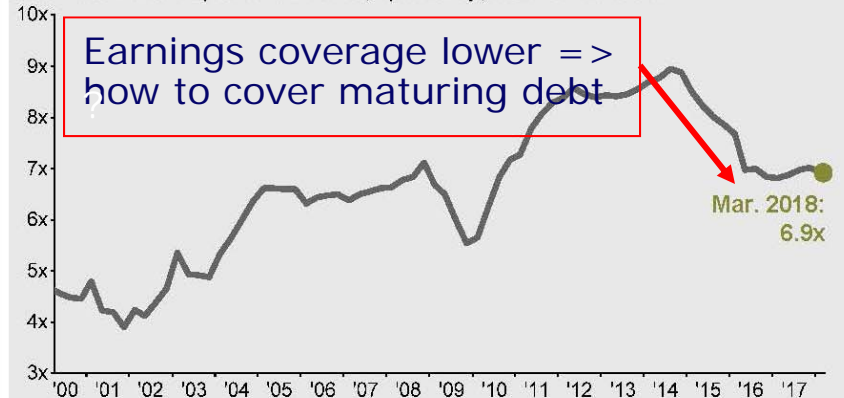
Corporate cash as a % of current assets
S&P 500 companies – cash and cash equivalents, quarterly



Non-financial corporate debt
U.S. non-financial corporations, % of GDP



S&P 500 interest coverage ratio
EBIT/interest expense on debt, quarterly, last 12 months

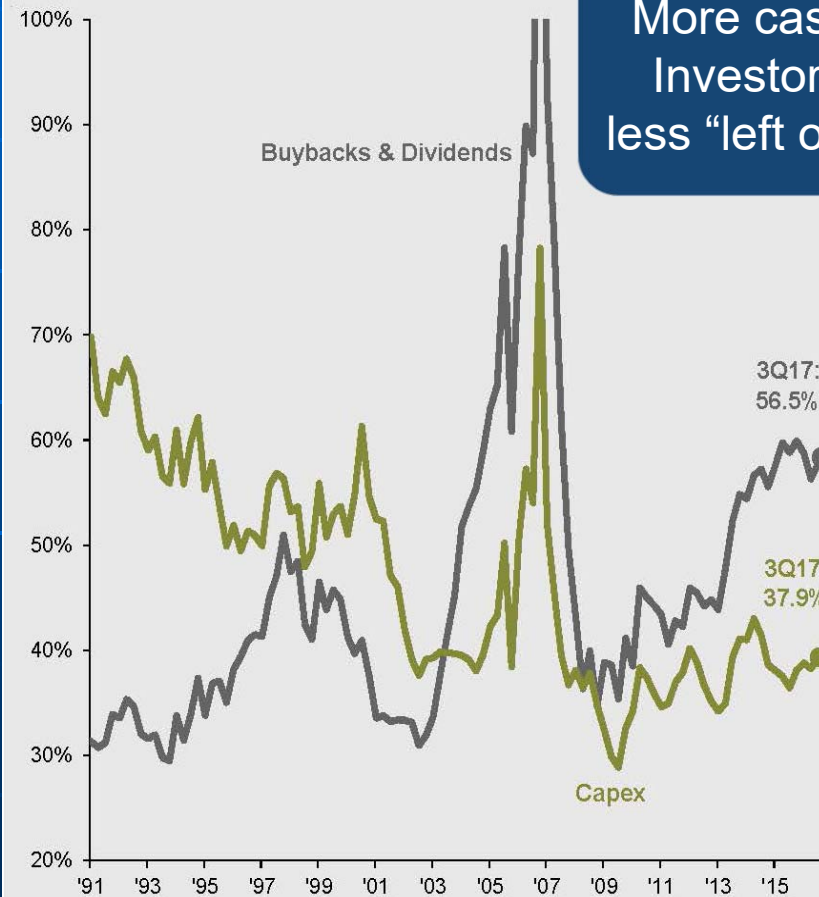


Need for Change – Internal Trends

How much liquidity is “enough” ?- uses

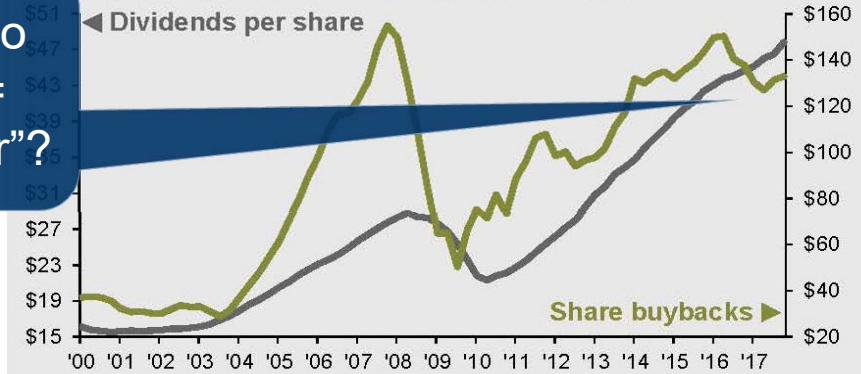
Uses of S&P 500 cash flows*

%, 4Q moving average



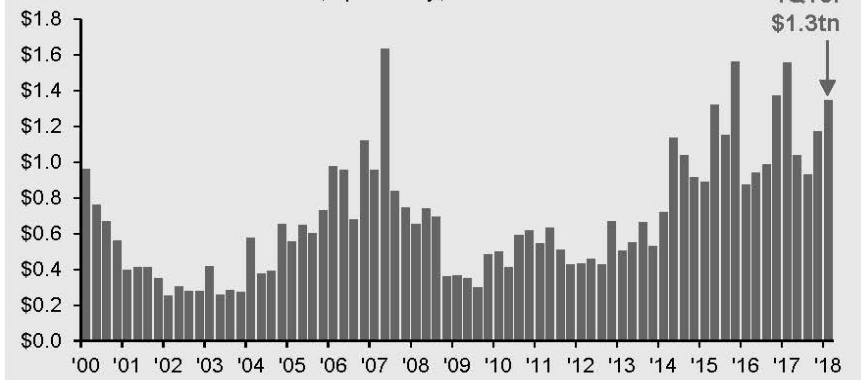
Cash returned to shareholders

S&P 500 companies, rolling 4-quarter averages, \$bn



Mergers and acquisitions

Value of deals announced, quarterly, \$tn

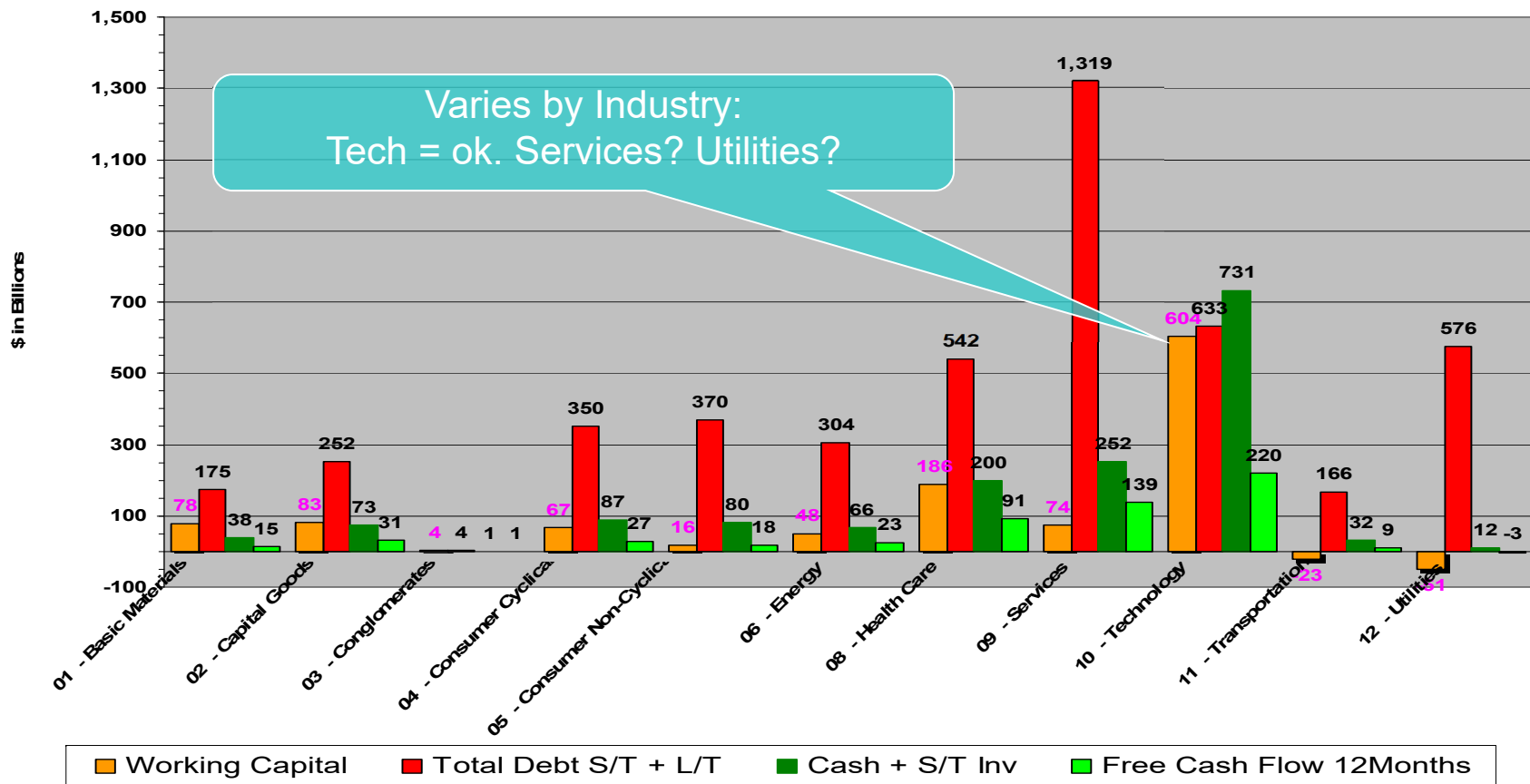


Need for Change – Internal Trends

How much risk (debt / free cash flow) is “too much”?

Snapshot - S & P 500 Non Financial Companies (425 co.)

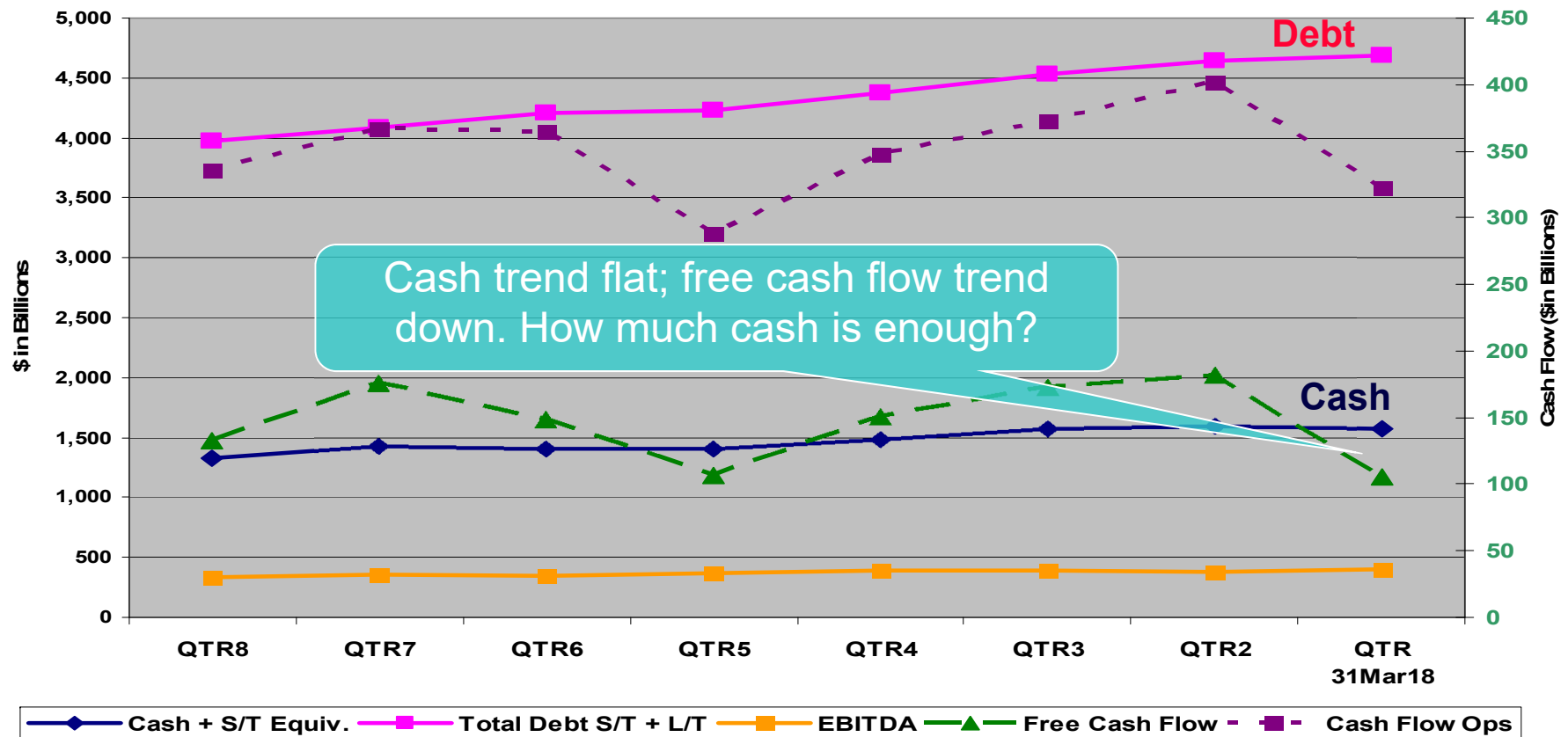
(Selected Results - 12 months ending 3/31/18)



Need for Change – Internal Trends

Treasury to CFO: We may not have “enough”?

S & P Non Financial Companies (423 companies)
Quarterly Trends as of 3/31/18



Why Treasury needs to change (2)

- Consider this near term scenario :
 - Your competitor has highest cash levels in 5 years giving them CAPEX, R & D options
 - Your debt / equity ratios are steady (but that "can" kicked down the road is still there)
 - Market forces cannot be controlled
 - "Guarantee" of low interest rates has ended
 - Bad news : variable rate debt to cost more
 - Good news : higher earnings on invested cash
 - No assurances FX rates will remain stable
 - Floating NAV or other restrictions limit MMFs
- Is Treasury equipped for this scenario?
 - Measuring "success" is key?
 - What outcomes will determine it?
 - What metrics to use? (Hint: Fee Cash Flow)

Why Treasury needs to change (3)

The Role of Treasury Today

Top 10 (of 21)	Leads	Supports
Borrowing long term (capital funding / sourcing)	79%	6
Investing – long term	61	15
Payment Strategy & Execution (in / out)	60	24
Working Capital Mgt	54	28
Capital Planning / Allocation	50	31
Counterparty Risk Analysis	49	24
Internal Financial Consultant	40	36
Insurance Purchasing	38	28
Leasing	37	27
Insurance claims Mgt	31	30

Sources: 2017 Strategic Role of Treasury, p11

Why Treasury needs to change (4)

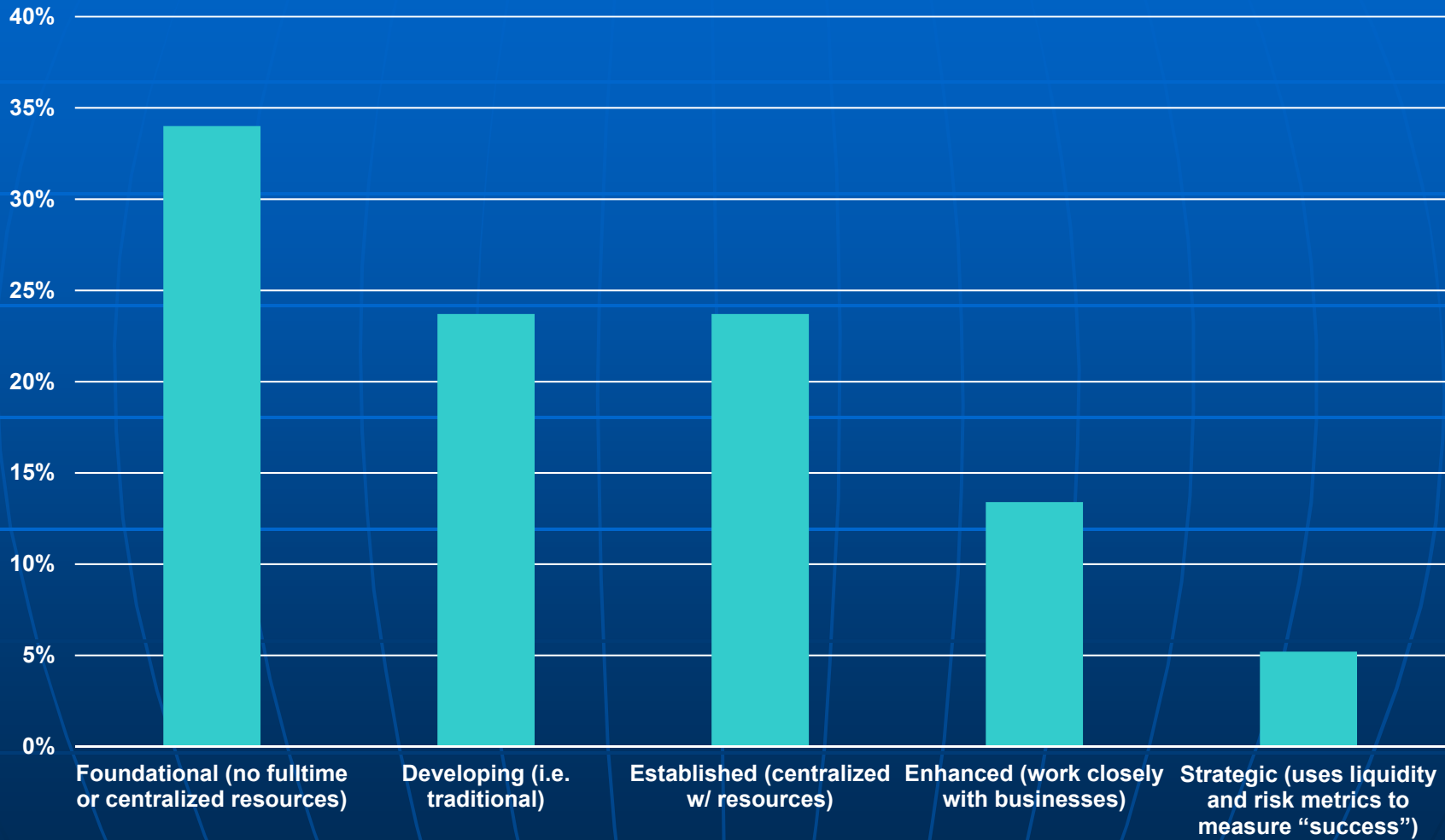
The Role of Treasury Today

Bottom 10 (of 21)	Leads	Supports
Employee Benefits	7	48
Supply Chain Mgt	10	46
Business Development	11	50
Accounting / SEC Compliance	15	50
Business Continuity Planning	19	45
Retirement Management	21	44
Mergers & Acquisitions	22	50
Assessing Financial Technology	24	42
Financial Planning & Analysis	27	53
Enterprise Risk Management	28	44

Sources: 2017 Strategic Role of Treasury, p11

Polling Question 3

Q3 - How Mature is Your Company's Treasury Department?



Overview of the Modern Treasury Function (1)

- Treasury should be a strategic unit that adds significant value to the corporation by:
 - Increasing automation of routine cash/banking transactions
 - Shifting workload from transaction processing to strategic analysis/decision making
 - Centralizing global funding/banking/FX (but leave execution local)
 - Focus on forecasting and future events
 - Develop “success” metrics (e.g RAROC or “risk adjusted returns to capital”)
- Treasury becomes pro-active
 - Become a problem solving resource for business units
 - Takes economic ownership of the cash flow statement making operating, investment and financial cash flows
 - Broader career opportunities become available as staff becomes knowledgeable about global cash flows

Model for the Modern Treasury Function (2)



- Policies Highly Visible
- Interactive Communications
- Plan, Actual & Forecast in Sync

- Functions & Systems integrated
- Performance Metrics in Place to Demonstrate Value

6 Key Activities for the Modern Treasury

1. Global oversight of for liquidity and risk
2. Maintain access to sufficient funding at all times
3. Risk management role expanded beyond FX/IR
4. Internal consulting and information resource for corporate management and business units
5. Reduce processing costs and bank charges
6. Actively participate in major company initiatives, e.g. strategic planning, IT, compliance, M&A

1. Global oversight role

- Formulate, document, distribute and update enterprise wide policies/guidelines
 - Liquidity management (internal & external)
 - Intercompany transactions and loans (allocation)
 - FX/IR risk management
 - Bank selection and counterparty risk
- Works effectively with other company units:
 - Operating
 - Enforces the use of standard market rates
 - Establish currency of billing rules for intercompany and 3rd party trade transactions
 - Forecasts encourage liquidity to focus on future business, not just accounting for activities that have already happened
 - Financial
 - Tax - Optimizes capital structure and after tax cost of funds
 - Controllers - Standardize rules for settlement of intercompany transactions
- **Bottom line – More planning, less processing**
 - Treasury is in the funding business
 - Resources best spent on future activities to control risk

2. Maintain access to funding

- Funding has suddenly emerged as a challenging issue for many companies
 - Traditional external funding sources now unreliable or “pricey”
 - Bank loans, CP, IPO, equity issues, long term bonds
 - Term loan waivers not routinely granted
 - Risk of shortfalls in sales volume and pricing
 - Minimal interest income on surplus cash
 - Counterparty risks now much more important
- Consider “make or buy” decisions to access internal liquidity
 - Tighter control of A/R and A/P (i.e. working capital)
 - Centralize then utilize surplus cash more quickly (daily, not monthly)

3. Scope/objectives of risk management

- Treasury must make itself the focal point for risk analysis and management within the corporation
 - Acquired FX/IR skills give Treasury a firm foundation to manage other market or credit risks e.g. commodities, employee option programs, “enterprise risk management”
 - Risk management is a key component of strategic planning
 - Treasury’s forward-looking orientation complements Controller’s “backward look” based on historical GL data
 - Senior management needs analysis of future P&L impacts
- Risk analysis and management is a sophisticated function
 - SEC rule 33-9089 (Board must disclose its role in risk) will require more highly educated staff with quantitative skills
 - Support will require upgrades and utilization of specialized software.
 - Even a TMS may not “work”

4. Treasury as an internal consulting resource

- Treasury can work with business units to:
 - Increase P&L by upgrading working capital mgt, applying improved techniques and benchmarks
 - Identify market exposures and hedging alternatives, and analyze cost/benefit strategies
 - Analyze FX impacts on product pricing strategies, e.g. currency of billing, fixed price lists
 - Hedge manufacturing costs, e.g. metals, energy, oil, sugar/cocoa/coffee etc.
 - Analyze customer credit risk and develop better customer financing programs

5. Treasury's focus on reducing operating costs

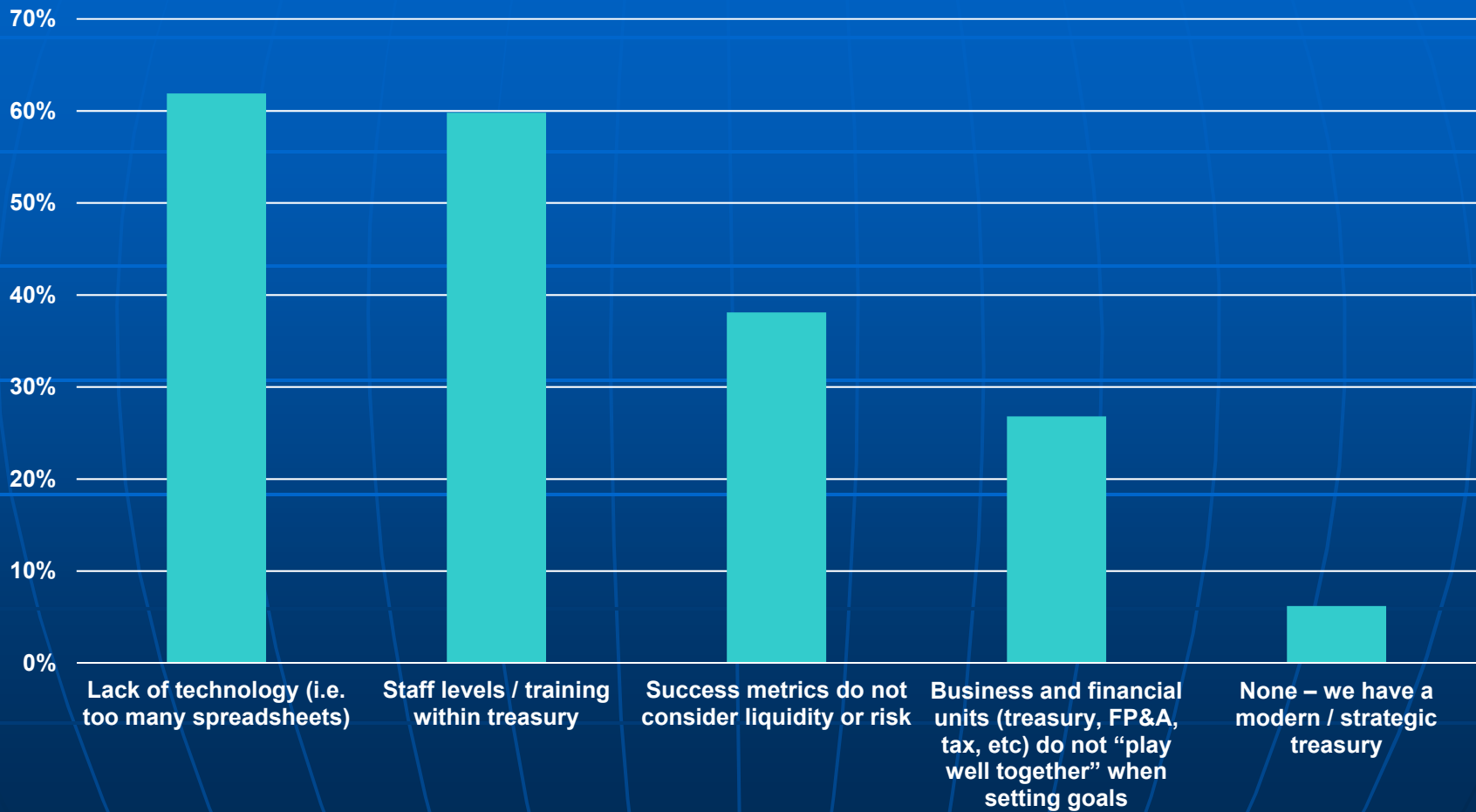
- How treasury can do more with less
 - External cost control
 - Rationalize bank account structures - companies have too many accounts, which create excessive "maintenance" bank fees
 - Replace paper based services with electronic services e.g. EFT, check imaging, purchase or T&E cards
 - Internal cost control
 - Automate daily bank and cash operations - e.g. treasury workstation as single platform for cash, debt activities across multiple banks
 - Move to portals for managing FX or investments reducing need to process multiple paper statements, spreadsheets on FX contracts, etc.
- Improve forecasts to shorten cash conversion cycle
 - Emphasize AR collections to increase funds in
 - Balance with AP disbursements to time funds out
 - Require intercompany settlements to reduce borrowings, FX needs?

6. Treasury as a pro-active corporate unit

- Treasury needs to interact within the company at least as much as with financial institutions
 - Works closely with
 - FP & A – cash flow forecasts (bottom up = top down?)
 - Tax on global capital structures and cash repatriation strategies
 - Inter Company borrowing – why are the “children” borrowing?
 - Should be an active contributor to major corporate initiatives, e.g. ERP updates, M&A, SOX compliance, China strategy, SS Center ops
 - Provides important information to business units via treasury intranet (i.e. TMS)

Polling Question 4

Q4 - What Issues Constrain Company's Ability to Move From Traditional To Modern Treasury?

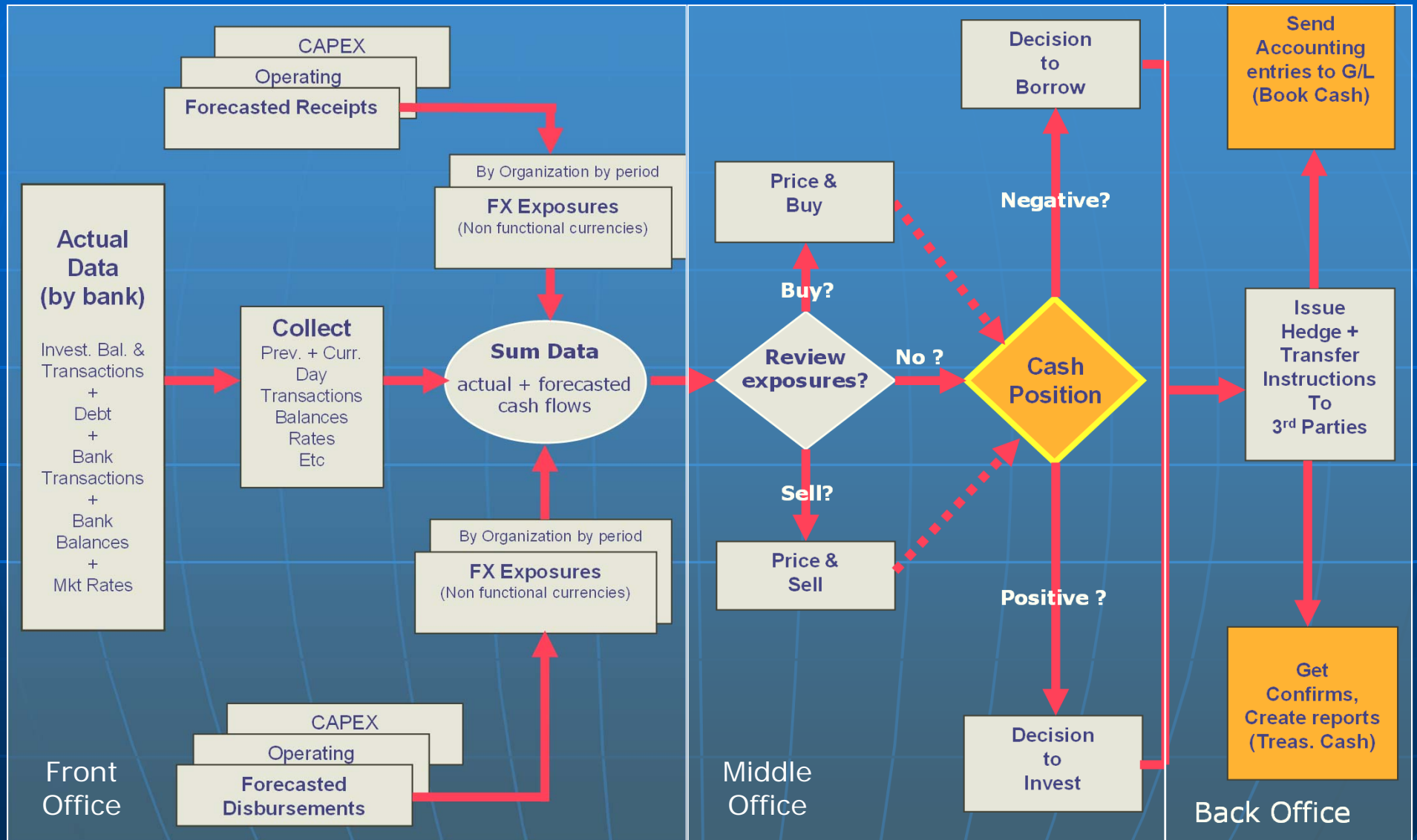


Making it happen

- Seek a good plan then execute it well
 - Step 1 - Start with the most important
 - Top 3 from FECG's "Treasury Issues 2018" survey (Q15):

Activity (1 to 5 Scale: 1 = high)	Rating 2018	Rating 2017
Improve Cash Forecasting Capability	2.1	2.2
Improve Liquidity (internal + external)	2.4	2.5
Manage Working Capital	2.5	2.5

Make it Happen: Managing the “Flows”



Make it Happen: best practices for the modern treasury

- Create clear written policies, updated regularly
- Define performance measurement criteria
 - “What gets measured gets managed”
 - Normal business concept (e.g. P&L, ROI, stock price)
 - Adopt measures of liquidity and risk (rarely attempted in corporate treasury today)
 - Benchmark treasury vs. peer companies
- Rotate staff between finance and business units
 - Have staff to visit principal business units at least annually, especially international
 - Require staff to follow a continuing education program

Make it Happen: Transition plan

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 units to establish joint goals (e.g. working capital?)
5. Upgrade treasury technology

Make it Happen: Transition plan

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

Q & A

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