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FINANCIAL SERVICES ADVISORY PRACTICE

Getting the most from a Treasury Function

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6 November 2006

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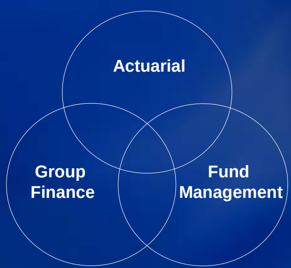
Getting the most from a Treasury Function

- A typical scenario
- Treasury Best Practice
- Implications for the Actuarial Team
- Discussion

Where are we now?



The Corporate Treasury Function

Main treasury functions

Liquidity & Cash Management	Currency Management	Funding	Corporate Finance
• Short-term management of cash • "Foundation" of treasury management	• Converting & hedging currency receivables & payables • Managing impact of movement on balance sheet	• Arranging bank & capital market debt	• Managing the corporate financial structure
• Cash flow forecasts • Working capital management	• Pricing in foreign currency • Currency derivatives e.g. forwards, swaps, options	• Term loans and deposits • Corporate bonds • Interest rate derivatives	• Financial ratios • Covenants • Benchmarking • Rating agencies

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What value does Corporate Treasury add?

- Treasury risk management e.g. interest, currency volatilities – adverse movements can reduce reported profits
- In-house bank to global entities – reduction in costs due to savings on FX and interest spreads can be significantly greater than traditional savings such as transaction processing and bank fees
- Global cash pooling – reduction in number of bank accounts, cross boarder transactions
- Reduction of manual tasks via automation e.g. automated bank reconciliation, online trading and confirmation
- Bank relationship management e.g. negotiating commitment funding, overdraft facilities, bank charges, transaction processing fees
- Centre of excellence – advice on compliance, treasury accounting, M&A support, credit rating agency management, tax

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What makes a successful Treasury Function?

Key success factors

- Thorough understanding of underlying business
- Alignment of treasury objectives with organisational objectives
- Articulation of treasury's response to the organisations financial risks

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Characteristics of Best in Class Corporate Treasuries

- Centralised Treasury Function
- High degree of STP (or initiatives to improve STP)
- Clearly defined roles and responsibilities (including Treasury Committees)
- High calibre staff
- Strong bank relationships
- Low cost base as a % of revenue
- Established KPI's e.g. hedging efficiency, cost of funding, ROI
- Interdepartmental integration e.g. AP, Sales and Marketing, Taxation
- Constant drive for improvement e.g. benchmarking
- Strong internal audit function

Achieving Success – Corporate Treasury Blueprint

Identify corporate financial risks

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Formulate treasury's response to financial risks

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Construct detailed treasury policies strategies and procedures

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Define structure for implementing policies, strategies and procedures

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Establish control and review systems

Financial Risk Analysis

- Foreign exchange rates
  - transaction, translation, economic
- Interest rates
  - net cost of debt portfolio, interest earned on investment portfolio, capital value of loan stock
- Equity
  - change in value of investments e.g. shares in a joint venture,
- Funding
  - longer term funding of the company e.g. availability of bank debt
- Commodity prices

Formulating Treasury Objectives, Policies & Strategies

Common Approach

Objectives	Policy	Control Framework	Strategy
Set and align treasury's objectives to finance objectives and by extension to corporate objectives	Complete and obtain Board approval of treasury policies	Design Control Framework for approving, implementing, monitoring and controlling treasury strategies, processes and procedures	Document and obtain Board approval of detailed strategies to meet objectives within approved policies

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Treasury Structure and Organisation

Structure

- Cost centre
  - exposures are fully hedged, treasury does not 'add' to financial risks
- Value added cost centre
  - as with cost centre but additional services provided without significantly increasing risks e.g. netting currency flows
- Quasi profit centre
  - aims to enhance profitability by active financial risk management within limits of approved policies e.g. discretion to decide on proportion of foreign exchange exposure to hedge
- Profit centre
  - similar to quasi profit centre but there is more freedom to 'create' profits e.g. taking bets on future market movements

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Treasury Structure and Organisation

Organisation

Centralised

- Treasury Centre provides treasury services to the group
- May have regional centres for legal and tax reasons

In House bank	Agency
• Treasury Centre acts a bank to the group • Third party deals to meet the requirements of operating companies are contracted by and in the name of the Treasury Centre • Banking benefits and costs of managing the group's financial risks are assigned to the Treasury Centre	• Third party deals are contracted by the Treasury Centre on behalf of and in the name of operating companies • Services to operating companies are charged on a cost plus basis

Decentralised

- Separate treasury function at an operating company level
- Operating companies have autonomy over treasury activities

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Review Mechanisms

Daily / Weekly

- Bank reconciliation
- Limit breach reports
- Position reports

Monthly

- Management pack
- Variance reports
- Inter-company reconciliation
- Financial statements review

> 1 Month

- Management pack
- Variance reports
- Benchmarking
- Independent review
- Compliance reports
- Policy review

Trends

- Straight through processing
- Use of web based Application Service Providers
- Business Intelligent Systems for cash flow forecasting
- Centralisation
- Compliance monitoring

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Summary

To maximise the benefit of Corporate Treasury detailed, in-depth answers must be provided to the following:

- What are the financial risks?
- What are the risk propensities of stakeholders?
- What are the risk management policies, processes and procedures?
- What are the performance measures?
- What are the review and control mechanisms?

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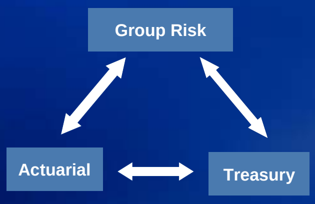
Risk Management

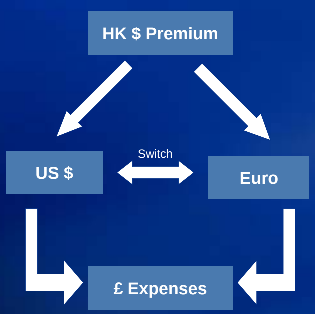


- Risk Appetite
- Risk ownership
- Risk management
- Risk measurement
- Developing risk management tools

Liquidity and Cash Management

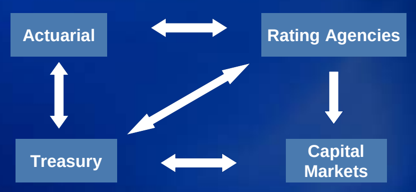
- Developing short term cash flow models
- Understanding the drivers
- Product design
- With Profit fund optimisation

Currency Management



- Potential for profit / avoiding costs
- Currency Risk management
- Product design
- Earnings volatility management
- Identifying Treasury as profit centre

Funding and Corporate Finance



- Capital Measurement
- Cost of Capital

- Capital Requirements
- Managing the rating agencies

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Questions for discussion

- Is your Treasury function centralised or decentralised?
- Do you have a strong relationship with your Treasury department?
- Does your Treasury function fully understand the risks involved with the business?
- Does your Treasury function understand how you can help them?

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