Treasury Trends

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A Treasurer's Oughtobiography - a tale of things that could, should or would be being done

There are always things in life we want to do but can't – whether a factor of time, dollars or capability. In treasury, it is no different. Busy people just keep getting busy and, all too often, projects get relegated on the priority list as a result of more pressing time critical actions. This does not mean that previous priority tasks become less valuable of course.

The Covid-19 pandemic had a significant impact on global economies, businesses, and financial markets. It served to change the priorities for many. In treasury circles, cash retained its 'king' status, with other areas of interest likely to now benefit from some attention.

No prizes for could or should have. Take ten to check:

- When bank lending and other services were last benchmarked?
- That your interest rate policy is fit for purpose?
- That you are comfortable BCP policies exist - and have been tested?
- That treasury gets an appropriate level of focus?

Understanding the changes to bank lending

Prior to the pandemic, corporate lending practices were relatively stable and predictable. Since then, some elements of lending have 'evolved'.

Risk Assessment: In the wake of the pandemic, banks have become more cautious and meticulous in assessing the creditworthiness and risk profiles of corporate borrowers. They now place greater emphasis on factors such as cash flow stability, debt serviceability and risk mitigation strategies as well as applying more rigorous due diligence processes to evaluate the financial health, industry exposure and resilience of borrowers.

Industry Exposure: The economic downturn had a disproportionate impact on certain industries, while others remained relatively resilient or even saw growth.

Sustainability: The pandemic brought sustainability and environmental, social, and governance ("ESG") considerations to the forefront of corporate lending. Banks are now incorporating ESG factors into their lending decisions, recognising the importance of sustainable business practices. Borrowers with strong ESG credentials may enjoy, or start to enjoy, favourable lending terms, as banks increasingly align lending portfolios with their own sustainability goals and investor preferences.

Naturally, as some will find themselves in the 'less attractive' category now in terms of attaining finance and services, others will benefit from being in the 'right' sector, better structured, able to tell a stronger sustainability story, etc. But, even if you are in the favoured category, and had adopted the simple but logical approach to 'extend existing' facilities in 2019/2020, it may well mean you have not been appropriately benchmarked for five or six years. It might be timely then to take the opportunity to review fully your use of cash, external borrowing requirement, facility make-up, covenant and reporting demands, as well as pricing.

For those struggling to retain bank engagement, other work may need to be done around capital structure, funding options, consideration of other providers and so on – ie update the 'lender ready' pack.

Working in a higher interest rate environment

For many treasurers and CFOs, the majority of their professional experience has been in a low interest rate environment. A hard lesson for some but it has been essential for those responsible for managing treasury risk to shift thinking to assess the impact of rising interest costs on overall expense, debt and investment profiles as well as overall financial health.

Ensure the interest rate risk part of the treasury policy is fit for purpose. Too often businesses moved away from policy when interest rates were 'low' – and were too late to respond as rates started the move higher. It is best an organisation develops its own policy, and adheres to it. If not, lenders can, and do, impose minimum hedging requirements – which may not reflect your own preferred risk profile.

Focus on efficient cash management, ie optimisation of cash conversion cycles, ensuring timely collections and efficient payment processes. By actively managing working capital, there is less reliance on external funding and thereby a lowering of the impact of higher borrowing costs. Assessing the number of banks holding cash, the structure of bank accounts, opportunities for pooling, etc are all projects that typically produce worthwhile outcomes. Saying farewell to a duffle bag of bank tokens and dongles is an added bonus for some!

Evaluate Investment Strategies. For those with surplus cash, it is important to not just chase the yield. Policies still need to be complied with, and it is important to conduct thorough due diligence and risk analysis before making any investment decisions.

Strengthen Financial Forecasting. Accurate financial forecasting becomes paramount in a higher interest rate environment. Forecasting models should ideally be able to incorporate the impact of rising (or changing) interest rates on cashflows, borrowing costs, and debt servicing. This will support more informed decisions, anticipate funding needs, and proactively manage interest rate risk.

Maintain Open Communication. Collaboration across finance, project managers and areas such as procurement is crucial to aligning organisational objectives and achieving planned outcomes.

Being prepared – BCP in place

Another area often sitting in the wishlist of treasurers and CFOs but often being put off 'for now' is the ultimate in risk management – Business Continuity Planning ("BCP"). The covid era underscored the importance of robust 'disaster recovery' strategies, highlighting the need to develop contingency plans to ensure the uninterrupted functioning of treasury operations during unexpected events – of whatever nature. We've seen examples of establishing remote working capabilities, strengthening communication channels, diversifying key vendor relationships as well as ensuring policies, procedures manuals, delegated authority rules, etc are up to date – and lodged with all appropriate stakeholders. We suggest partners such as banks be brought into discussions around BCP as the impact of not being able to receive or pay monies is likely to feature highly on any risk register.

Resisting the snooze button on treasury

The amount of 'other things' businesses and CFOs have to deal with in recent years is astonishing but it can be costly to relegate treasury too far down the list of tasks to do. Effective treasury doesn't always need a lot of time, but it needs 'some'. All too often exposures change, debt facilities near maturity, cashflow stumbles and so on. Assuming treasury will still be there when it suits is not necessarily a good approach. For sure, separate the 'must do' elements from the 'ought to do' – but it is likely more prudent to not have all in the second group.

Just ask those that have 'suddenly' learned that their bank cannot extend lending or other facilities anymore (due to own performance, sector concerns, ESG scoring, offshore issues, etc), or that hedging is now more than anticipated given an extreme fall off in sales or inability to source from previously reliable markets, or that a major customer has fallen over and cashflow issues now cause severe impacts on their own ability to meet obligations around payments, covenants and so on.

If you miss the basics, you run the risk of achieving nought.

Avoid the noughtobiography …

In conclusion, corporate treasury risk management has witnessed notable changes in the past three years. The day to day or routine still has to be done – and likely with fewer resources than before. Fires will always have to be fought but there is merit in taking a quiet moment to plan or strategise. Your advisor will be pleased to update the Partnership Plan ahead of, or at, your next meeting.

There ought to be no surprises in treasury.

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