CLUB DIRIGENTI AMMINISTRATIVI E FINANZIARI

Finanza e Tesoreria durante e dopo la crisi

Gestire i rischi finanziari

Torino, 28 ottobre 2010

pwc

Agenda

1. Global treasury Survey 2010
2. Financial Risk Management Framework

Global treasury Survey 2010

1

PwC Global Treasury Survey 2010

This year's PwC Treasury Survey focuses on the impacts on the Treasury function stemmed from the global financial crisis and economic downturn. How did treasurers face with the crisis[1]? Were they prepared? How is the crisis going to shape the Treasury function? Which are the long-term lessons learnt?

585 Treasurers Responses - 330 Multinational Companies[2]

26 Countries - 5 Continents - 12 % Italian Companies

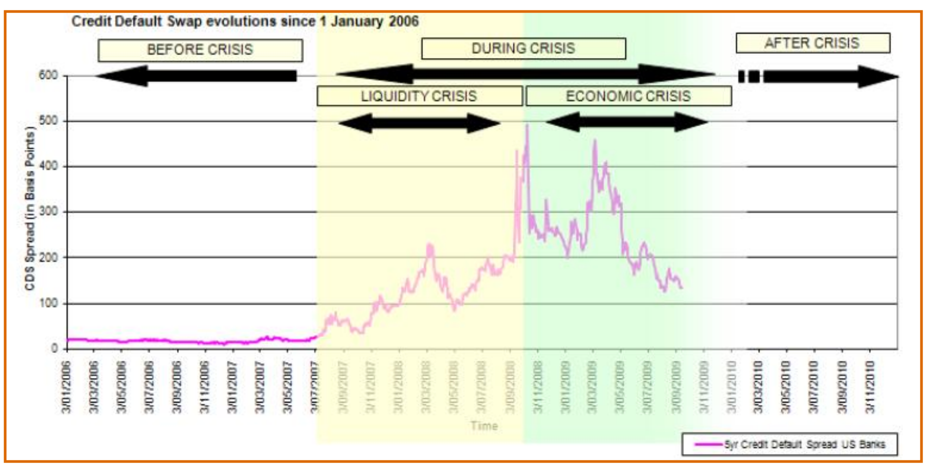
[1] For the purposes of this presentation, the crisis has been defined as running from July 2007 until today

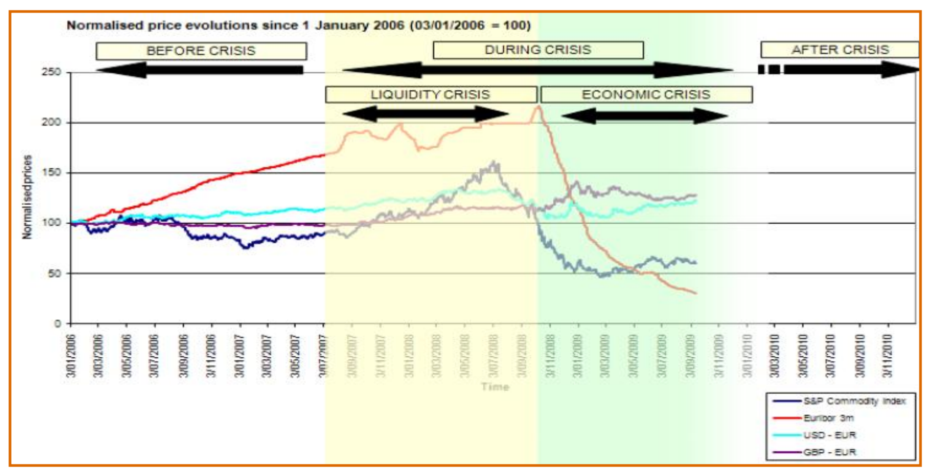
[2] The PwC Global Treasury Survey 2010 participants belong to all industry sectors with turnovers ranging from less than Eur 1 billion to over Eur 10 billion

Credit crunch and economic crisis

- "Credit crunch" refers to the liquidity squeeze which precipitated the crisis and its inception can be back dated to July 2007.
- Credit Default Swap (CDS) spreads shot up to unprecedented levels, sharpened by the subsequent Lehman Brothers' collapse in September 2008.
- For most treasurers this was the period when the availability of easy liquidity stopped abruptly, leading to the highest level ever of uncertainty.
- Parallel, this was also the period of the run-up in commodity prices.

- By the summer of 2008 commodity prices began to slide as the liquidity crisis turned into an economic crisis.
- Treasurers were not only coping with the problem of accessing liquidity from the financial market, but realized their revenue streams were drying up too.
- This period was accompanied by turbulent times on the FX markets, since previously stable currency pairs began to swing wildly.





Treasury Survey key findings

- ✓ Treasury Organization
- ✓ Changing dynamics in bank relationship management
- ✓ Keen focus on counterparty risk management
- ✓ More sophisticated cash management solutions
- ✓ Diversified long term funding and covenant negotiation
- ✓ Focus on working capital management
- ✓ Active approach to commodity risk management
- ✓ Active approach to FX risk management
- ✓ Accounting: Help, hindrance or cause?

Treasury Organization

The survey sample brought together a representative cross section of treasury function sizes and it shows that most treasuries come from geographically dispersed businesses (covering ten or more countries). (Figure 1)

Survey participants operate with an under-resourced treasuries head office with an average head office of around 5 people (Figure 2)

Staffing levels at head office should reflect the growing centralization and specialization seen as being needed to manage the complexity of risks and regulations faced by today's treasury.

Many companies did not appear to give best practices the priority they deserved, treasurers have experienced budgetary constrains and the crisis has shown that the consequences of neglecting the treasury function can be critical.

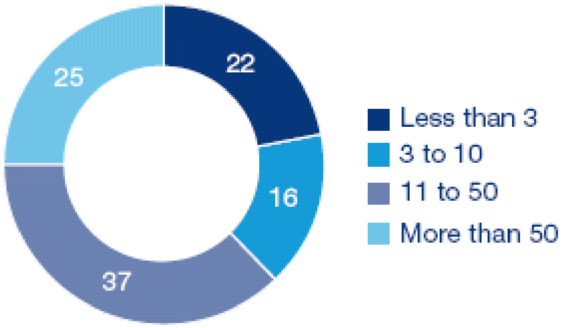


Figure 1: Activities in number of countries

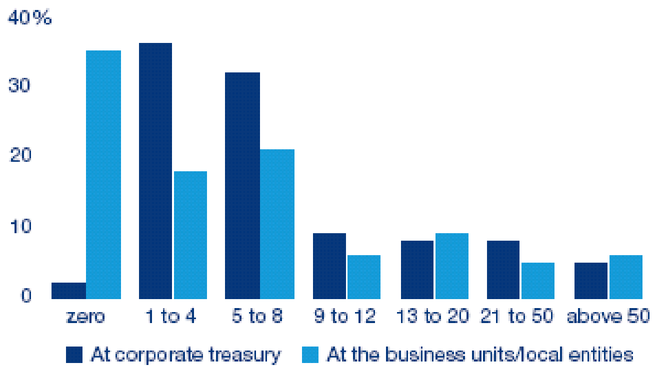


Figure 2: Deployment of treasury staff

PwC view: Under-resourced treasuries had difficulty managing all risks adequately. High staffing levels at head office are needed to manage the complexity of risks and regulations faced by today's treasury. The key challenge for treasury teams is to press the case for sufficient resources to implement best practices.

Changing dynamics in bank relationship management

The crisis has stressed one thing perhaps more than any other: the importance of good bank relationships.

Nearly 80% of participants now believe that bank relationship management is a high priority compared to the only 56% prior to the crisis. (Figure 3)

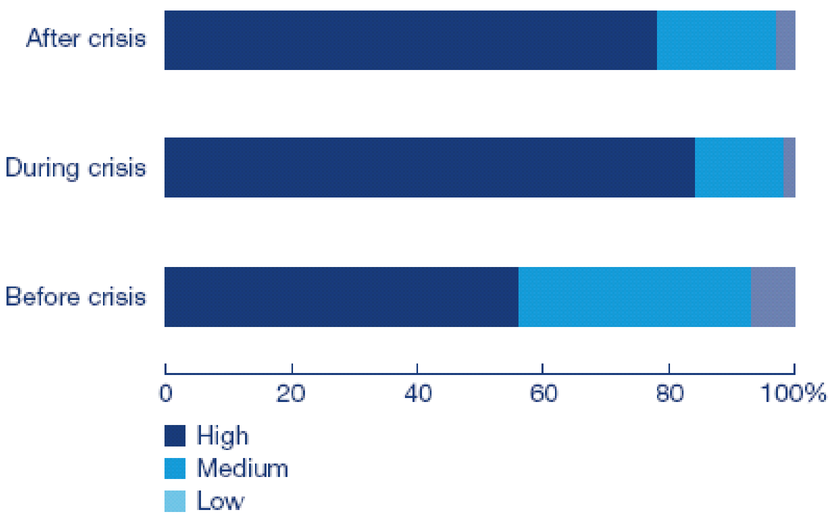


Figure 3: Importance of bank relationship management

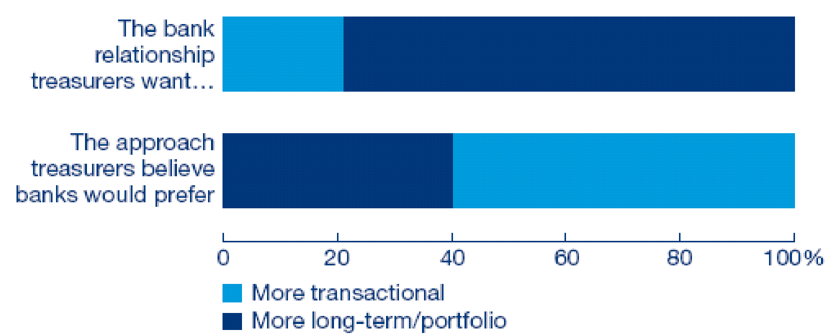
Due to the need for funding and liquidity, Bank Relationship Management became extremely important during the crisis.

The survey shows also that most treasurers now want a long term relationship more than ever, but note that their banks are moving to a more transactional focus. (Figure 4)

Treasurers are facing the particular dilemma of wanting to place their business with a small selection of banks to help secure funding on the one hand and diversify their banking panel to reduce counterparty risk on the other.

It may be possible to have both to some extent, but this will require more transparency and detailed monitoring (including balanced scorecards) on both sides to ensure the relationship stays mutually beneficial, and hence robust, in the longun.

Figure 4: The relationship dilemma



PwC view: Treasurers need to develop scorecards to measure how much revenue/profit is made by the banks on the overall relationship. This will allow them to develop a more transparent and reciprocal relationship that highlights the mutual value being created for both sides.

Diversified long term funding and covenant negotiation

The Survey results show that for most companies funding became more difficult, for some impossible. (Figure 8)
The pressure on the availability of funding has forced many participants to focus more on diversifying their sources of finance. This trend is expected to continue post-crisis. There has been a definite move away from bank facilities towards bonds, though this is happening gradually. (Figure 9)
40% of participants increased the amount of surplus cash to help ease funding risks.

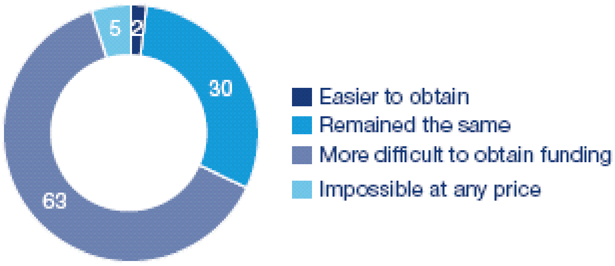


Figure 8: Availability of funding during the crisis

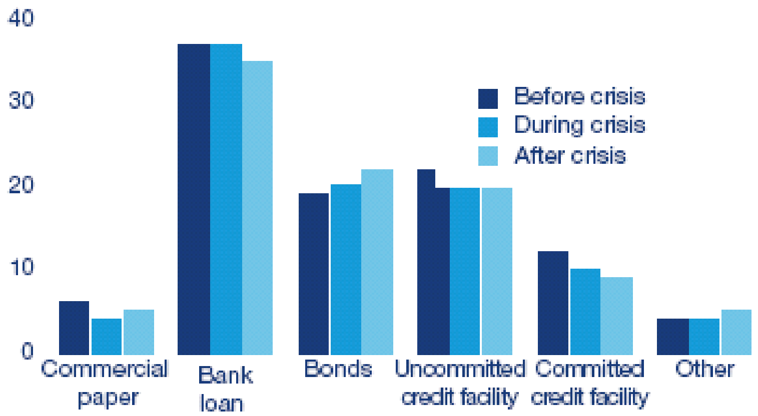


Figure 9: Sources of funding

PwC view: it is important that companies weigh up the costs against the availability of new funding sources. Covenants became critical and now more important.

Future best practice will therefore focus much more closely on the detailed design of covenants and better reporting compliance and forecasted compliance under adverse scenarios

Keen focus on counterparty risk management

Counterparty Risk is not just about bank failure, but also about the chance that payments might be frozen or credit access dried up. Treasurers have realized that banking counterparties do not necessarily need to collapse to withdraw funding and other services.

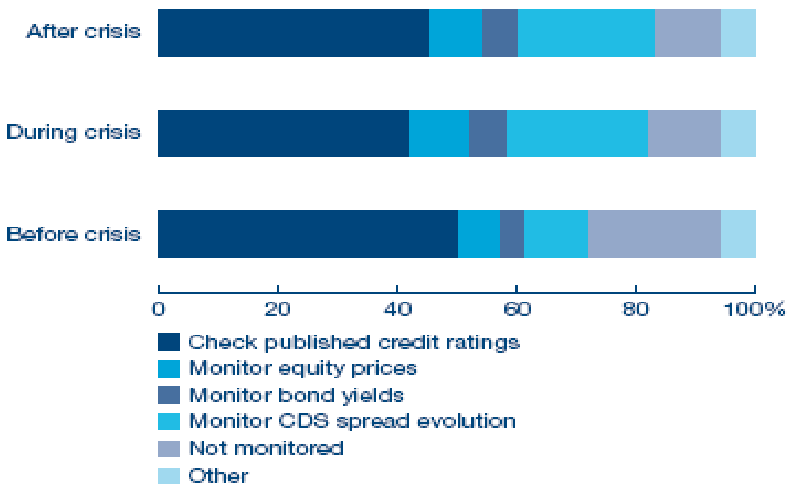


Figure 5: Approach to counterparty risk management

Counterparty Risk gains in sophistication.

More than 80% of participants perceive it as either a medium or high priority. Best practice is evolving in line with this sharper focus. The credit rating monitoring has increased through more earlier warning indicators such as CDS spread, equity prices and bond yields. (Figure 5)

Credit limits have been defined using fair values and potential future exposure for financial investments and derivatives

Monitoring is becoming more sophisticated

Yes, banks can fail.. or drop out of your core list !!

More sophisticated cash management solutions

The Survey results show that during shortage of liquidity period, it is crucial to improve the visibility and control on the cash position. Given this scenario, companies hence have to face with the optimization of the liquidity management. Liquidity structures, which centralize available cash, will tend to be more global after the crisis (41% after versus 28% before), highlighting the need for visibility and control. (Figure 6)

In Italy cash pooling structure appears less sophisticated compared to the European scenario; indeed the prevailing cash concentration structures are domestic, despite the post-crisis trend towards a cross-border (at European level) of liquidity concentration and management. (Figure 7)

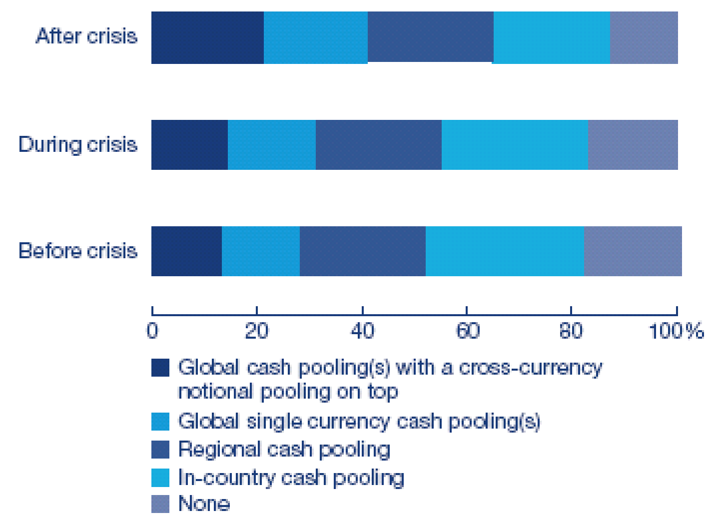


Figure 6: Liquidity structure in place

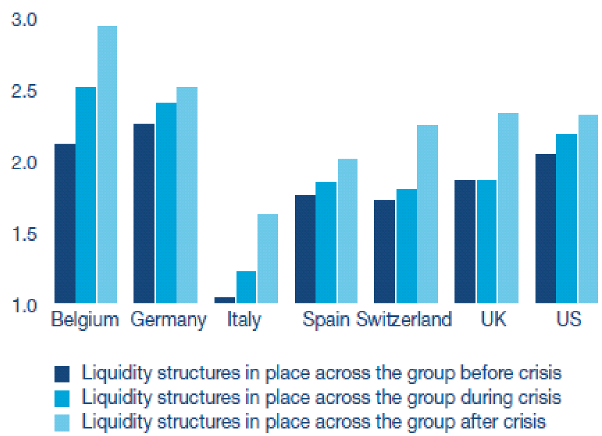


Figure 7: Liquidity structure in place by country

1 domestic cash pooling; 2 European cash pooling; 3 global cash pooling monocurrency ; 4 global cash pooling multicurrency;

PwC view: Companies need to demand and implement more sophisticated and global liquidity solutions in order to improve visibility and control on cash

Focus on working capital management

The survey confirms that during the crisis the importance of working capital rose significantly. Even post-crisis, more than 70% of the respondents expect the importance of working capital management to remain high. (Figure 10)

The survey reveals also a patchwork of approaches to optimizing working capital; the redesign of internal processes is seen by participant as the main foundation for improved efficiency.
The quick-win initiatives initiated during the crisis have now been largely implemented and most participants are now moving on to a more integrated and enduring assessment and redesign of internal processes. (Figure 11)

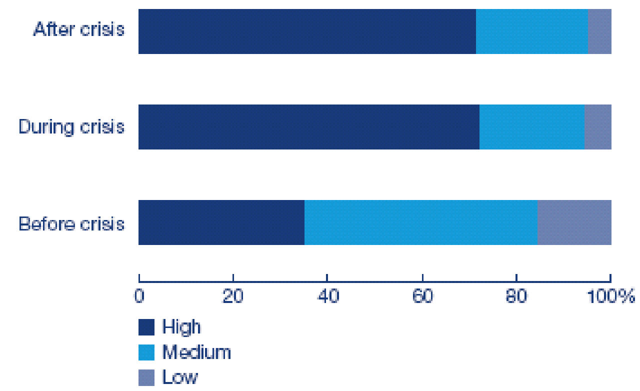


Figure 10: Importance of working capital management

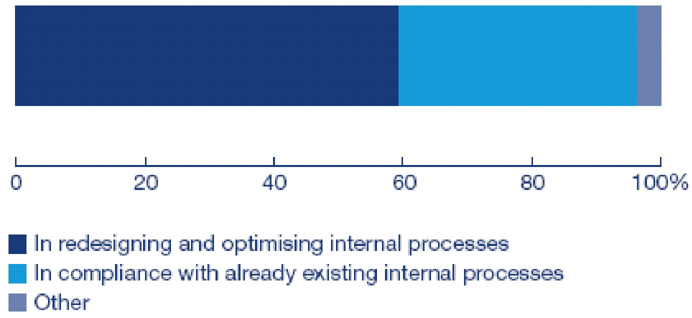


Figure 11: improvement area for working capital management

PwC view: Most treasurers are aware that best practice working capital management comes from foresight, planning and robust management processes. Given the cross-functional nature of working capital management, only a holistic assessment covering all areas will uncover inefficiencies in the underlying processes. As the urgency of the crisis eases, now is the time to critically re-assess these, and drive improvements with one fully integrated approach.

Active approach to commodity risk management

80% of participants recognize that they have some form of commodity exposure. The survey shows that standardized hedging techniques are insufficient to cope with the unprecedented market turbulence.
Many companies are then moving from a relatively standardized approach towards more active management.

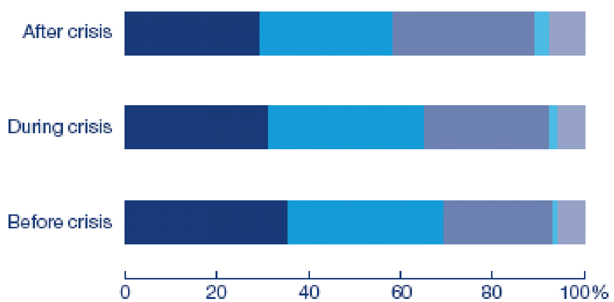


Figure 11: Importance of commodity risk management

The need for flexibility and specific functionality in capturing commodity exposures are considered by many to be beyond the capabilities of traditional TMS and that companies consequently have to either develop their own in-house system or simply rely on Excel sheets for the management of these risks.
(Figure 12)

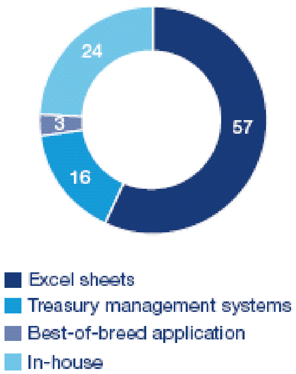


Figure 12: Commodity risk management system in use

The Italian companies reacted to the crisis in terms of improvement in the commodity risk management, approaching the level gained by the US and Switzerland. (Figure 13)

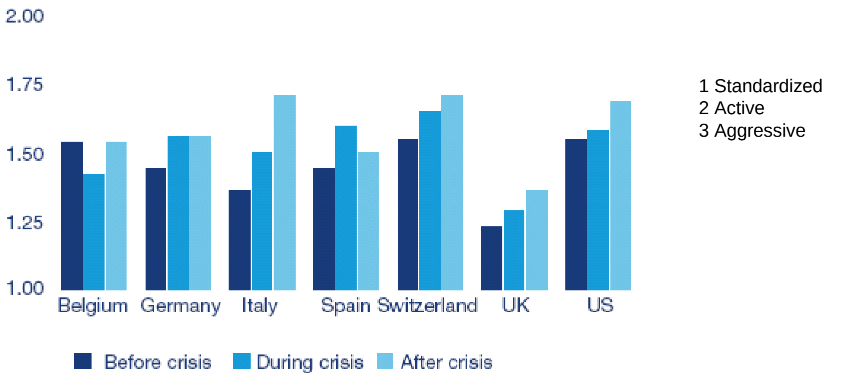


Figure 13: Sophistication of commodity risk management by country

PwC view: Benefits will be realized by companies that are able to integrate commodity risk management with traditional financial risk management activities while staying close to the business. This will pave the way for the realization of key synergies and would allow for effective and flexible hedging strategies to be put in place to appropriately manage the risks posed by volatile markets.

Active approach to FX risk management

The survey confirms that the significant volatility across a large number of currency pairs during the recent years has led treasurers to focus additional attention on FX risk management. (Figure 14)

Increased volatility than is forcing many participants to explore more active and/or longer term hedging strategies (Figure 15); horizons increased with opportunistic hedging in some currencies, however, others decreased horizons as business forecasts became unstable. Larger companies focus is now on reducing earnings volatility over several years.

PwC view: There is not always a right or wrong approach to FX hedging. In our view, what is important is to clearly identify the hedging objective(s), then keep adapting the hedging strategy to ongoing changes in the business and to ensure that the parameters of the strategy (types of exposures to hedge, hedging horizon, types of hedging instruments, etc.) remain in line with the company's business model and evolving management objectives.

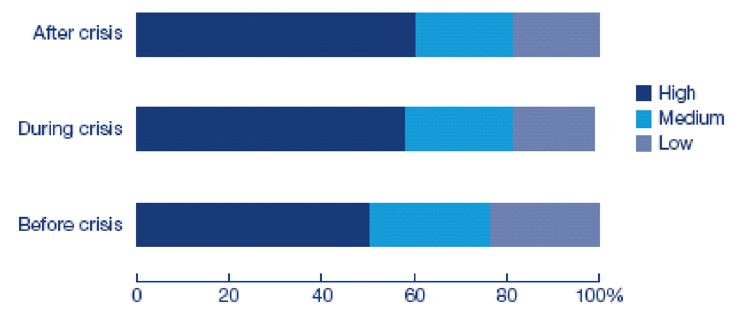


Figure 14: Importance of currency risk management

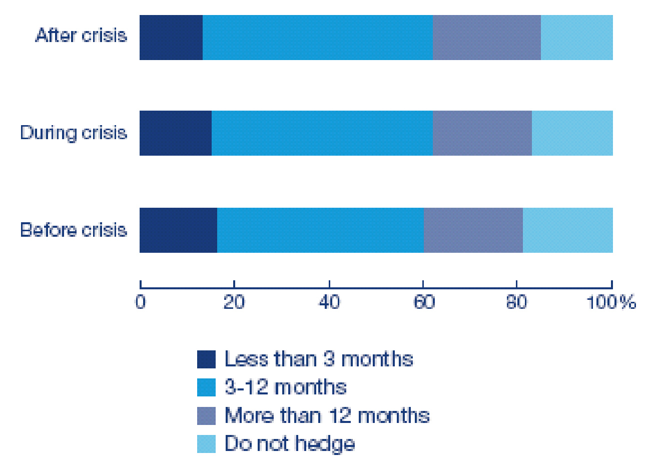


Figure 15: Time horizon for hedging currency exposure

Accounting: Help, hindrance or cause?

The survey highlights that the swings and uncertainties seen in various markets during the crisis have encouraged a gradually increasing number of participants to curtail the volatility in their financial statements through the use of hedge accounting. (Figure 16)

The crisis has intensified the spotlight on financial risks and therefore provided an extra incentive to use hedge accounting to help avoiding the potential shareholder unease caused by pure accounting fluctuations in their income statement. Despite this, accounting standards are still seen as too complex for many companies; hedge accounting is more widely used by larger corporate. (Figure 17)

PwC view: The credit crisis has highlighted the benefits of reporting fair value for financial instruments – and exposed its limitations.
Reporting fair value, although imperfect, remains the best available method for most financial instruments. However, the desire to expand the use of fair value needs to be tempered until the method's limitations are fully understood.

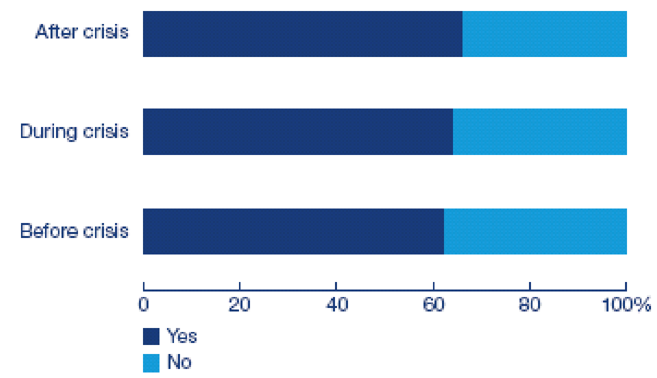


Figure 16: Hedge Accounting applied

Revenue size of company	Applying hedge accounting
More than €10 billion	81%
€1 billion – €10 billion	69%
Less than €1 billion	53%

Figure 17: Hedge accounting applied by size of participant

Top of Treasury's agenda now

The survey underlines the importance of setting clear priorities and smart management of resources. Top item on the Treasury agenda are now:

- **Funding:** it is important to focus on how to manage funding under a range of different scenarios. Treasurers will also be looking at how to manage existing relationships more effectively, while diversifying funding options and opportunities

- **Cash management:** investment in the redesign and implementation of more efficient cash management structures can pay dividends by making more cash available for use in the business and reducing the need for borrowing. This involves a combination of systems, organizational improvements and bank account restructuring

- **Technology and systems:** despite their implementation being generally complex and costly, new tools and technology are essential in efficiently supporting almost all other areas of improvement:
  - Faster access to data via integrated platforms
  - Ability to perform multiple scenarios efficiently
  - Ability to upload real-time market feeds to effectively measure exposures
  - Ability to calculate potential future exposures
  - Automate the increased visibility and control over cash

Figure 18: Top of the treasury agenda today

Most of the steps needed to safeguard firms from risks and losses are features of prevailing best practice, rather than being particularly innovative. So why weren't these implemented?

Future improvements

Participants look forward to improvements mainly in: cash flow forecasting, working capital management , bank relationship management, organizational structures. (Figure 19)

Participants also anticipate an evolution in risk management policies, which could well reflect the more active approach. All of the identified improvement are to be supported by developments in risk management tools and technology.

According to the survey, it would appear also that once treasurers have taken on board the lessons learnt about funding during the crisis, they can resume their focus on risk management and cash management.

Boards and treasurers themselves now realize that the function needs to integrate with the business to really understand and manage the financial risk dynamics of the enterprise. (Figure 20)

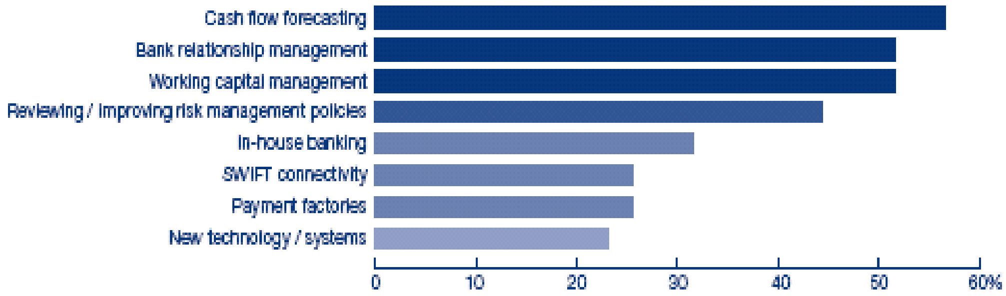


Figure 19: Future improvements

Figure 20: Where treasuries can add value in the next five years

Technology and processes in the form of in-house banks, payment factories and SWIFT connectivity are seen as promising new areas, which should allow increased control, visibility and forecasting of cash.

The focus is also switching from cost reduction and risks within treasury, towards investment to better understand the risks within the business.

What did the crisis do for you?

"The Chinese use two brush strokes to write the word 'crisis'. One brush stroke stands for danger; the other for opportunity. In a crisis, be aware of the danger-but recognize the opportunity."

John F. Kennedy

The crisis has ensured the treasurers unprecedented attention from board (80%) and business teams alike.

Treasury is perceived as adding value to the business although this renewed recognition of its role is not always supported by increases in budget which have remained mainly the same: less than 20% of participants have been able to secure extra resources as a result of the crisis.

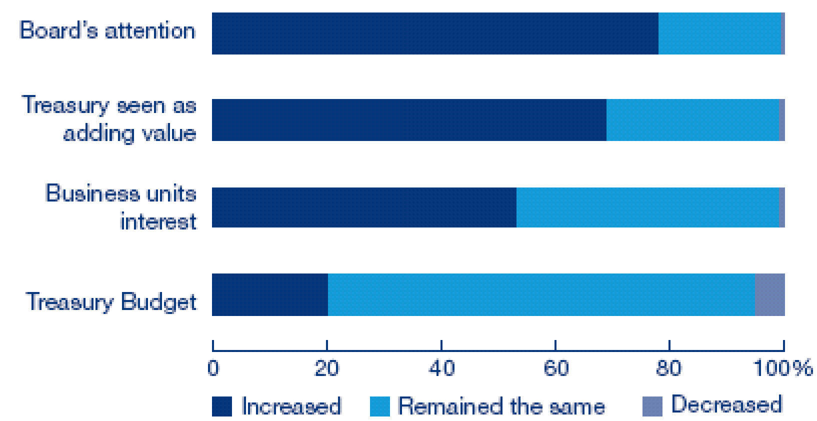


Figure 20: Impact of crisis on treasury team

The valuable contribution of the treasury function is now better understood, as are the disastrous consequences if it fails – now is the time to secure investment in treasury!

Financial Risk Management Framework

2

Financial Risk Management – Main drivers

✓Board and management scrutiny of risk and controls

✓Increase predictability of financial results

✓Mitigate losses

✓Decrease cash flow volatility

✓Avoid unforeseen surprises

✓Allow efficient capital allocation

Designing and Implementing a Financial Risk Management Program

Risk Assessment

- Define and identify risks
- Measure risks
- Determine impact on business decisions

Strategy Development

- Set/validate goals and objectives
- Determine and measure risk appetite
- Set strategy parameters

Implementation

- Develop processes
- Develop infrastructure

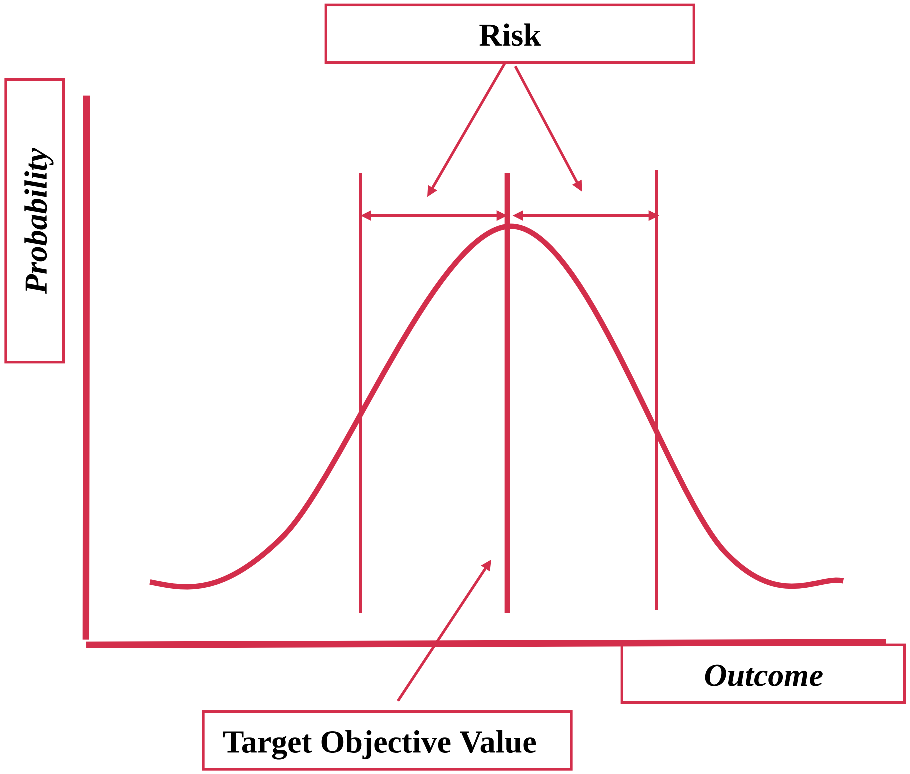
What is risk?

Risk is variability from an expected outcome

Risk can come in may forms:

- Operating
- Strategic
- Financial
- Business

Financial risk is derived from movement in market variables



Definition of Risk

Foreign currency exposure types:

- Transaction
- Translation
- Economic

Commodity exposures:

- Cost of Goods Sold versus budget/market
- Margin volatility

Interest rate exposures:

- Delta in fair market value of debt
- Interest expense/income

Risk Measurement

Quantify impact of risk based on defined objectives or key metrics

Risk Measurement methodologies include:

- Notional measures
- Mark-to-market/fair value
- Sensitivity and scenario analysis
- VaR or other probabilistic approach

Hedge accounting opportunities should be considered

Hedging Horizon

Set hedge horizon based on:

- Risk profile
- Exposure forecast accuracy

Also influenced by:

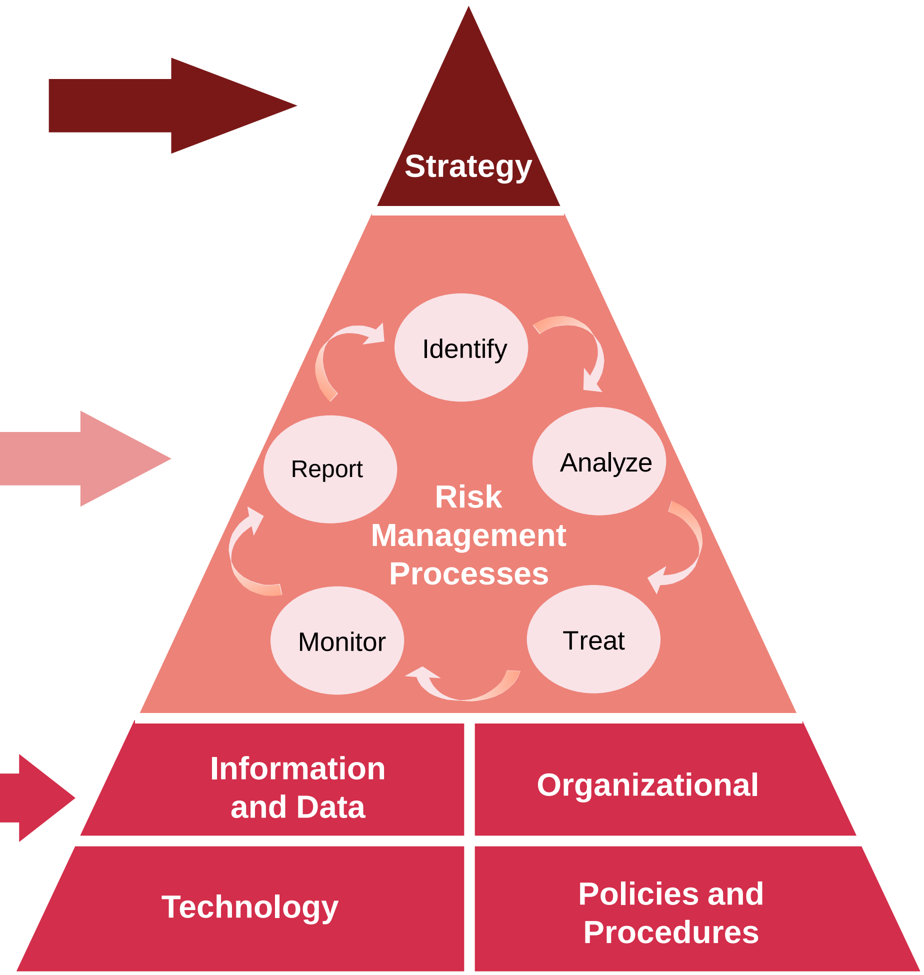
- Market volatility
- Hedge market liquidity
- Hedging instruments
- Cost of long dated hedges

The Financial Risk Management Framework

Strategy – How are objectives, risk and responses aligned across the enterprise?

Processes – What are the formal and informal risk management processes to identify, analyze, manage, monitor and report risks?

Infrastructure – What foundation does the company need to enable the organization to execute the risk management strategy and processes?



PricewaterhouseCoopers
Advisory SpA
Via Monte Rosa, 91
20149 Milano
Tel. +39 0266720563
riccardo.bua.odetti@it.pwc.com

Riccardo Bua Odetti
Partner

La presentazione verbale è il necessario complemento alle pagine seguenti che, quindi, non ha valenza autonoma dalla presentazione stessa.