

Optimizing and right-sizing liquidity

Life has changed for corporate treasurers since the onset of the greatest financial crisis since the 1930s. Even as economic windstorms swirled, however, forward-looking companies continued to retool and refocus their treasuries, shoring up to seize eventual growth opportunities.

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LIQUIDITY MANAGEMENT: A RECURRING THEME

During the economic downturn, traditional sources of funding became less accessible and liquidity took on greater importance. So did cash flow efficiency. Even with a rebound in sight, these and other liquidity-related issues remain top-of-mind for treasurers.

Citi clients have been using Treasury Diagnostics, a peer-benchmarking tool, to assess strengths and opportunities to improve across a spectrum of functions, policies and practices. The results provide deep insight into current treasury priorities and concerns at leading multinationals around the world. Of particular significance, many companies perform rather less well in liquidity and working capital management, relative to other areas of treasury responsibility.

Consequently, several highly relevant themes dominate treasurers' priorities for the near term. These include improving liquidity planning and management and accelerating cash conversion cycles.

Some critical areas where even minor improvements can provide major paybacks include:

1. Establishing the right level of liquidity
2. Optimizing global liquidity
3. Extracting cash trapped in the order-to-cash cycle

ESTABLISHING THE RIGHT LEVEL OF LIQUIDITY

Recent market attitudes have favored holding large cash balances. However,

history tells us that this trend will not be sustained over the long term. As economic confidence returns, liquidity will remain a priority, but factors such as the opportunity costs of holding excess cash will likely gain in importance.

That said, reducing excess cash balances to more optimal levels may, in fact, be risky where there are significant inefficiencies in a company's financial supply chain. Determining how much cash a company needs involves evaluating a variety of factors to get a clear picture of how much cash is needed, when, and where. This includes assessing material sources and uses of cash, across countries and currencies, and mapping them to their respective cash conversion horizons. In addition, internal and external factors, such as interest rate forecasts and how and where a company plans to restart its growth engine, need to be taken into consideration.

Admittedly, setting liquidity levels can be a complex task. However, having in place the right processes and systems to aggregate and automate data collection across business units simplifies the process.

OPTIMIZING LIQUIDITY STRUCTURES

An efficient operating liquidity structure is a highly effective lever, reducing the level of cash required to run day-to-day operations and providing greater funding flexibility when other alternatives are unavailable or costly. Global cash centralization and pooling structures, both physical and notional, enable companies to offset cash surpluses

and excess among local operating units and reduce their reliance on external funding.

Today, even mid-size companies are using these structures, once the purview of large multinationals, to maximize the value of their internal cash.

EXTRACTING CASH FROM THE ORDER-TO-CASH CYCLE

In their quest to reduce working capital requirements, companies recognize the importance of squeezing as much cash as possible from their purchase-to-pay and order-to-cash cycles.

Typically, companies begin by automating and centralizing processes on the procure-to-pay side. However, an area often left fallow, and one that can reap significant rewards, is the revenue generation side -- from customer order fulfillment to payment processing to the application of outstanding receivables. By centralizing and automating receivables processes, the result is more timely and predictable collections and the elimination of both internal- and bank-related float. What's more, integrated collection processes, combined with improved receivable information and analytics, can enhance decision-making around customer credit practices.

Taking receivables management even further, for companies whose cash position is stronger than their supply chain partners, receivables portfolio financing and distribution financing programs can support sales growth without extending the cash conversion cycle.



CITI TREASURY DIAGNOSTICS REVEALS TOP PRIORITIES FOR TREASURERS IN 2010

One of the tools used by Citi to help companies measure and improve their treasury operations is Citi Treasury Diagnostics, a comparative survey that benchmarks their performance against best practices in six critical areas: liquidity; risk management, working capital, subsidiary funding and repatriation, policy and governance and systems and technology.

Data captured by Treasury Diagnostic revealed seven key priorities for treasurers at major corporations this year as they shore up to seize growth opportunities. At the top of their agenda are:

1. **Establishing the right level of liquidity** - After building up high cash levels over the past three years, companies are focusing on liquidity planning and stress testing to establish optimal levels for organic business expansion.
2. **Releasing cash trapped in emerging markets** - To reduce cash trapped by restrictive capital controls, companies are deploying advanced treasury structures (e.g., re-invoicing centres, intercompany netting), improving cash forecasting, using local liquidity management structures, and strengthening oversight of subsidiary funding & repatriation
3. **Diversifying sources of funding** - By

deploying global liquidity structures to offset cash surpluses and shortages across subsidiaries, and streamlining order-to-cash and procure-to-pay cycles to release cash trapped in working capital, companies are reducing reliance on external funding.

4. **Improving risk management practices** - Treasury's scope has expanded beyond managing risks around foreign exchange, interest rate, and treasury cash investments to managing liquidity risk and supply chain risk.
5. **Actively tackling changes in regulations and tax laws** - As countries have stepped up tax scrutiny and legislative and regulatory changes, companies are reassessing treasury structures including In House Bank domiciles and cash concentration centers.
6. **Integrating global treasury processes** - Centralization of treasury functions to gain a single firm-wide perspective on liquidity and risk proved essential during volatile market conditions. During 2010 integration efforts will continue, with a focus on standardizing policies and processes, setting common performance indicators for staff and rationalizing banking relationships.
7. **Investing in technology** - With technology as the key to stitching together

far-flung operating centers and creating both process and liquidity efficiencies, companies continue to embrace technology-based solutions, and the banking partners who offer them, to ensure a single view of firmwide liquidity and risk.



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