

**SUNGARD**

AVANTGARD INSIGHTS

# TREASURY CENTRALIZATION:

*AN ESSENTIAL GUIDE FOR  
CORPORATE TREASURERS*

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## INTRODUCTION

Centralization of treasury functions has been a trend amongst the largest North American and European multinational firms for a number of years. Increasingly, the benefits of a centralised treasury are being recognized by companies of all sizes and all regions, from mid-market companies with relatively straightforward cash management, funding and foreign exchange requirements through to large firms with highly sophisticated treasury needs. In today's uncertain financial environment, with rising costs, volatility of risk and increasingly expensive financing, treasury centralization offers some important advantages.

## VALUE OF CENTRALIZATION

There are a variety of reasons why companies decide to centralize their treasury operations, which would typically include cash management, financing, investment and foreign exchange, including both routine activities and strategic management. The factors which bring the most significant benefit, and therefore the most compelling value proposition, will depend on the nature of the business, but some important factors typically include some of the following.

## IDENTIFICATION OF CASH AND RISK

One of the key challenges of maintaining a decentralized approach to treasury is the difficulty in producing an overall view of the company's cash position and exposure to risk on a timely basis. For example, different parts of the business involved in treasury will frequently have different systems and different ways of recording and reporting information. This can mean that it can take a long time to construct a global cash or risk position when combining information from different sources. Consequently, this information is often only produced monthly or even less frequently. It is impossible to make strategic decisions without access to timely, accurate information which is particularly significant during periods of economic volatility.

*"We choose to implement the AvantGard Treasury solution because we wanted to improve visibility into our daily cash positions. We also needed to gain a higher degree of structure surrounding our cash, risk and debt management processes. The solution has thus far met all of our demands in these areas, providing our treasury with the tools necessary in order to make the best possible business decisions and ultimately increase revenue."*

Jeannot Jonas, Director, Global Treasury Operations, Goodrich Corporation

## ACCESS TO FINANCING AND LIQUIDITY

Once a global view of the company's position has been obtained, treasury can act on this information to optimize liquidity across the group. With credit becoming expensive and less readily available, companies need to find ways of accessing capital rather than relying on external borrowing. By centralizing treasury, and establishing an in-house bank to support local business unit requirements, companies can leverage group positions more effectively: for example, cash surpluses in one part of the business can be used to finance deficits in another.

Reducing the need to borrow externally by seeking out cash within the company is an important benefit of centralizing treasury, but where financing still needs to be

obtained, it is likely to be more cost-effective and less problematic to seek funds at group level rather than business units borrowing locally, often with a lower credit rating and higher rate of borrowing. Furthermore, with tighter credit conditions, the least attractive lending from a bank's perspective is an unsecured loan. By centralizing treasury activities, there is a greater opportunity to seek alternative funding methods such as asset-based finance and receivables securitization.

## CASHFLOW FORECASTING

Forecasting is a challenge for most organizations except perhaps those with consistent, recurrent revenue streams. In many cases, forecast information derived from different parts of the business is prone to wide variations and different assumptions in the way it is constructed. Not only is the underlying data frequently unreliable, but it can then be extremely difficult to combine this information in a coherent and consistent fashion. By centralizing this function, using a single system to combine information derived from other systems or allowing business users from across the company to input data through a common channel, a more reliable and transparent approach to forecasting can be achieved. While forecasting remains a complex issue, improvements in this area, in which centralization is an important first step, increases companies' ability to use forecast information for liquidity and finance planning.

## OPERATIONAL EFFICIENCY AND CONTROL

Working in different locations with disparate business practices, controls and systems creates challenges when trying to ensure that the business is adequately protected against error and fraud and that policies and procedures are being observed consistently. This is particularly problematic for companies which report under Sarbanes Oxley or similar corporate governance requirements but shareholders of all firms are scrutinising financial management practices to satisfy themselves that these are best-in-class. In challenging times, operational efficiency is increasingly being considered a source of improved return on equity so this issue is elevated from day-to-day management to one of strategic importance.

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## INVESTMENT PERFORMANCE & RISK

Despite the current economic volatility, companies are still benefitting from a long period of benign market conditions with easy access to cash, low rates compared to previous economic downturns and year-on-year growth. By centralizing balances as far as possible, better use can be made of cash, reducing the need to borrow to finance working capital, capital expenditure, research and development and mergers and acquisitions. Cash can be invested at a higher return than business units can achieve with smaller balances, and the investment policy can be broader than individual business units may have been permitted. For example, different investment types can be used, such as money market funds, and counterparty risk policies can be controlled centrally.

## ECONOMIES OF SCALE

Debt and investment are just two of the areas where acting at group level can have tangible advantages over negotiating with the banks at business unit level. There are other economies of scale which can be achieved too.

## FOREIGN EXCHANGE (FX)

FX is an important area which can be improved by centralizing treasury. Rather than business units converting currency locally to meet their needs, and potentially significant foreign exchange risks across the organization, which may not be easy to quantify, FX rates can be improved and risk mitigated by managing FX centrally. FX positions can be offset, reducing the cost of FX spreads, and ensuring a global view of FX risk.

Many organizations which centralize their treasury function establish a multilateral netting operation to settle their internal invoices. This can substantially reduce both the number of payments and the FX requirement at business unit level.

“We choose to implement a blend of AvantGard Treasury for risk management and the Kiindex Risk Workbench to support our newly created treasury operations, including our hedging initiatives in the energy trading market, because this combination of solutions proved to be an ideal fit with South African Airways’ areas of need. We were attracted to the out-of-the box solution offered, as well as the established and professional reputation that SunGard maintains in the South African market.”

Michael Kleyn, Head of Cash Management, South African Airways

## TREASURY RESOURCING

While this can be a sensitive area, rarely are job losses the result of treasury centralization. Rather, most staff engaged in treasury activities at a business unit level do so part-time alongside other responsibilities. Lifting treasury tasks away from the business unit means that these staff can focus on other activities.

Establishing dedicated treasury centres (either globally or regionally as described in the next section) means that these centres can become centres of excellence, not only engaged in supporting the day-to-day financial requirements of the business but contributing strategically to improving the working capital cycle, enhancing return on equity and assisting in mergers and acquisitions. Working with a central treasury should bring considerable benefits to local finance managers as they can more easily obtain financing (and at a cheaper rate) the spread on foreign currency requirements is reduced (or the need for FX eliminated altogether) and the relevant systems no longer need to be maintained.

## BANKING RELATIONSHIPS

A great deal of resource can often be expended when maintaining banking relationships at a local level. Often, the people managing these relationships are business managers rather than financial experts, and time taken on this activity detracts from the core business. Furthermore, a proliferation of banks and accounts can result in a loss of control over mandates, fragmented cash balances and an inability to negotiate with banks based on the group's credit rating and overall size. By centralizing these relationships, mandates can be managed more effectively, cash centralized in fewer accounts, economies of scale created when negotiating with fewer banks and less local resource required. There is also a significant technology implication as described below.

## TECHNOLOGY

Dissipating treasury activities across the group frequently means that transaction processing and reporting is also spread across multiple systems. There is a cost to maintaining these systems and each business unit needs to use the relevant banking system(s) which in many cases will be integrated with internal systems. A commonly cited industry figure is that it costs upwards of €15,000 a year to maintain each banking interface. The more disparate the banking relationships across the group, the higher the costs will be. Furthermore, we have referred to the problems with producing timely and trustworthy information and ensuring consistent controls and processes when different systems are in place. By centralizing treasury onto a single platform – whether or not treasury is physically located in a single location – banking connectivity and interfaces to internal systems can be rationalized, consistent user profiles, controls and audit can be established and a global view of information can be obtained instantaneously.

## BARRIERS TO CENTRALIZATION

If centralization was easy, however, all companies would already have done so. It is a great deal easier than five years ago, however, with progression in management attitudes and availability of technology, so the challenges are more easily surmountable. The table which follows outlines some typical issues faced by companies contemplating treasury centralization and examples of ways to address them:

CHALLENGE	SOLUTION
Business Culture	<p>Many companies have a decentralized culture where different parts of the business, which may undertake disparate business activities, operate quite independently of each other. This is particularly exacerbated where acquisitions are frequently undertaken. However, many companies which been decentralized in the past have gradually looked to centralize some aspects of the group, such as head office and back office functions which are not specific to the business and where economies of scale can be achieved. With a greater focus by shareholders and executive boards on areas like control and return on equity, the business case for treasury centralization becomes more compelling.</p>
Mergers & Acquisitions	<p>Highly acquisitive companies or those which restructure regularly often find centralization difficult as once some parts of the business have been centralized, this structure changes. Companies in this position which have been successful in centralizing their treasury have often developed a standard procedure for migrating the treasury activities of acquired businesses into a group treasury function. In many cases, this process has become very rapid and efficient. Central to achieving this is the right technology in place centrally into which new business can be integrated quickly and easily so that treasury can focus on issues such as bank accounts, bank relationships, staffing and debt/investment migration.</p>

CHALLENGE (continued)	SOLUTION (continued)
<p>Technology</p>	<p>The majority of companies, whether centralized or decentralized in their business approach, have aimed to standardize their IT infrastructure by using an ERP (enterprise resource planning) system such as SAP or Oracle. Few firms are in the position of having a single version of a single ERP across the enterprise and this can present a problem, as with new acquisitions often comes another ERP and it can take months or even years to migrate to a common platform.</p> <p>A better way to approach this is to implement specialist software (TMS – Treasury Management System) to support a centralized treasury function. This can be integrated with the banks, either by connecting with the banking applications or through SWIFT and also interfaced to internal systems including the ERP and other applications. This is often a less costly and labour-intensive way of supporting treasury.</p>
<p>Cash Management</p>	<p>While debt, investment and foreign exchange are relatively straightforward to migrate to a central treasury environment, cash management can be more difficult, primarily due to the issues of currency controls and restrictions over repatriation of funds in some countries, particularly in Asia.</p> <p>By centralizing banking relationships, many companies have found that consolidating cash flow becomes easier and while small balances in certain countries may remain, these balances are more transparent so the company has better overall visibility and can manage liquidity more strategically.</p>

## TYPES OF CENTRALIZATION

Companies which have centralized their treasury activities have done so in various ways, depending on the culture and geographic spread of business activities. In some cases, companies will prefer a central treasury function in a single location from which all treasury activities are managed. In others, treasury may still operate as a single operation, but with locations in different parts of the world. These regional treasury centres may be responsible for regional cash management and also allow “round the clock” access to the financial markets. By using a single system, with the same database underlying it, the benefits of centralization can be achieved whilst still maintaining more local contact with business units and the local markets.

Another related trend is in financial shared services which have developed significantly in recent years, consolidating activities such as payroll, T&E, payables and receivables. While this document will not focus on these areas, it is important to note that treasury’s involvement with shared service centres is crucial, to understand and influence working capital requirements and cash forecasts. In some cases, treasury is taking a more operational role in these areas by becoming the financial shared service centre for functions such as payables and receivables.

## CONCLUSION

Centralizing business support functions such as treasury is a vital way in which a company can equip itself to build economies of scale and rationalize costs, particularly when acquiring new businesses, therefore increasing return on equity. Every part of the business is continually challenged to demonstrate how it adds value to the rest of the organization and treasury is no exception. Centralization is key to achieving this by lowering the cost of debt, increasing investment return, providing expertise to business units, reducing financial risk and ensuring liquidity across the group. In doing so, forecasting can be improved and ultimately working capital levels reduced, enabling cash to be returned to shareholders or used to finance strategic activities.

The majority of companies, whether centralized or decentralized in their business approach, have aimed to standardize their IT infrastructure by using an ERP system such as SAP or Oracle. Few firms are in the position of having a single version of a single ERP across the enterprise, however with new acquisitions often comes another ERP and it can take months or years to migrate to a common platform.

A better way to approach this is to implement specialist software (TMS – Treasury Management System) to support a centralized treasury function. This can be integrated with the banks, either by connecting with the banking applications or through SWIFT and also interfaced to internal systems including the ERP and other applications. This is often a less costly and labour-intensive way of supporting treasury.

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**About AvantGard**

SunGard's AvantGard is a leading liquidity management solution for corporations, financial institutions and the public sector. AvantGard provides chief financial officers and treasurers with real-time visibility into cash flows and increased operational controls around treasury, receivables and payments management. The solution aggregates data for a single view of cash, drives productivity through automation, and fosters collaboration between trading partners. For more information, visit [www.sungard.com/avantgard](http://www.sungard.com/avantgard).

**About SunGard**

With annual revenue exceeding \$4 billion, SunGard is a global leader in software and processing solutions for financial services, higher education and the public sector. SunGard also helps information-dependent enterprises of all types to ensure the continuity of their business. SunGard serves more than 25,000 customers in more than 50 countries, including the world's 50 largest financial services companies. Visit SunGard at [www.sungard.com](http://www.sungard.com).